Pension Fund

2013-2014 Annual Report and Accounts

NORTHUMBERLAND
Northumberland County Council

www.northumberland.gov.uk

Pension Scheme Tax Reference Number: PSTR 00329946RE

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Contents

Introduction

The purpose of this report is to account for the income, expenditure and net assets of the Northumberland County Council Pension Fund ("the Fund") for the financial year to 31 March 2014.

Information about the economic resources controlled by the Fund is provided by the Net Assets Statement, which summarises the net assets of the Fund, on the basis of current market values.

Information about the additions to, withdrawals from, and changes in value of the Fund during the year to 31 March 2014 is shown in the Fund Account.

The total market value of the Fund, net of liabilities, has increased from £914 million to £944 million as the annual return on the Fund (comprising income and realised/unrealised gains/losses on investments) together with receipts to the Fund have exceeded the payments made from the Fund in the year.

The most significant change in the Fund account was the realised and unrealised profit on investments of £35 million experienced during 2013/2014, reflecting the positive return on investments experienced by funds generally over that period. The aggregate net withdrawal from dealings with members was £5 million in 2013/2014, reflecting the increasing number of pensioners and reducing value of contributions from members as the Fund matures.

The overall annual return on the Fund was 3.8% for the year (14.0% in 2012/2013), which compares with the Fund specific benchmark annual return of 3.4%.

The degree of long term growth of the Pension Fund is seen as a more reliable indicator of performance, as short term fluctuations are evened out. In this context the overall annualised return on the Fund for the ten years to 31 March 2014 was 7.7%, which compares with the benchmark annualised return of 7.9%. Fund returns for the ten-year period were higher than the growth in average earnings and RPI/CPI increases.

Management

Statutory authority

Under the Local Government Pension Scheme Regulations the statutory administering authority responsible for the Fund is:

- **Northumberland County Council**
  County Hall
  Morpeth
  Northumberland
  NE61 2EF

Pension Fund Panel

The above authority has delegated its responsibility for determining investment policy and monitoring investment performance to the Pension Fund Panel which meets at least quarterly. The Panel sets guidelines for and assesses the investment decisions of the Fund's investment managers.

As at 31 March 2014, the membership of the Pension Fund Panel was as follows:

Voting members

Representing Northumberland County Council

Councillor A. W. Reid	**(Chairman)**
Councillor Mrs E. M. Simpson	**(Vice Chairman)**
Councillor D. L. Bawn	
Councillor A. Tebbutt	
Councillor Mrs V. Tyler	
Councillor J. G. Watson	

Non-voting members

Representing employers

Mr Paul Harrison	**Homes for Northumberland Ltd**

Representing employees and pensioners

Ms Sue Dick	**Employee of Northumberland County Council**

Representing employees

Mr Alan Culling	**(UNISON)**
Mr Ian Storey	**(UNISON)**

The Panel is advised by Ms J Holden of Mercer Limited, who is an independent adviser, rather than a member of the Panel.

Investment Management

The day-to-day management of the Fund's investments as at 31 March 2014 was carried out by the following five external managers:

Passive balanced	**Legal & General Investment Management Ltd** **One Coleman Street** **London** **EC2R 5AA**
Corporate bonds	**Wellington Management International Ltd** **Cardinal Place** **80 Victoria Street** **London** **SW1E 5JL**
Global equities	**M&G Investment Management Ltd** **Laurence Pountney Hill** **London** **EC4R 0HH**
Property	**Schroder Investment Management Ltd** **31 Gresham Street** **London** **EC2V 7QA**
Property	**BlackRock** **12 Throgmorton Avenue** **London** **EC2N 2DL**

Private equity

The Panel selected Morgan Stanley of 25 Cabot Square, Canary Wharf, London, E14 4QA, as private equity fund of funds investment provider to the Fund in November 2005. As at 31 March 2014, the Fund had commitments to three of Morgan Stanley's private equity funds of funds. The Panel subsequently selected NB Alternatives, an affiliate of Neuberger Berman Europe Ltd, Lansdowne House, 57 Berkeley Square, London W1J 6ER, as a second private equity fund of funds investment provider in January 2007 and as at 31 March 2014 had a commitment to NB Crossroads Fund XVIII, a private equity fund of funds.

Infrastructure

The Panel selected Global Infrastructure Partners of 12 East 49th Street, 38th Floor, New York, New York 10017, USA, as an infrastructure fund investment provider to the Fund in July 2011. As at 31 March 2014 the Fund had a commitment to Global Infrastructure Partners Fund II. The Panel subsequently selected Antin of 2-8 Avenue Charles de Gaulle, L-1653 Luxembourg, Grand Duchy of Luxembourg, as a second infrastructure fund in September 2013 and as at 31 March 2014 had a commitment to Antin Infrastructure Partners II LP.

Custody

Custody services for the funds managed by the external managers are provided by:

- **The Northern Trust Company**
  50 Bank Street
  Canary Wharf
  London
  E14 5NT

Banking

Banking services for the cash managed in-house are provided by:

- **The Co-operative Bank p.l.c.**
  84-86 Grey Street
  Newcastle upon Tyne
  NE1 6B2

Actuary

Actuarial services for the Fund and the participating employers are provided by:

- **Aon Hewitt Limited**
  8 Devonshire Square
  London
  EC2M 4PL

Solicitors

Legal services are provided by Northumberland County Council's in-house Legal Team. When specialist legal advice is required and the expertise is not available in-house an external solicitor is engaged, for example, Sacker & Partners LLP of 20 Gresham Street, London EC2V 7JE for investment managers' contract review.

AVC Fund Provider

Scheme members can make additional voluntary contributions (AVCs) to the Fund's nominated AVC provider. These contributions are not included in the Fund's assets. During 2013/2014 members were able to take out AVC plans with:

- **The Prudential Assurance Company Limited**
  Laurence Pountney Hill
  London
  EC4R 0HH

Statement of Investment Principles

Northumberland County Council is the administering authority for the Northumberland County Council Pension Fund under the various Local Government Pension Scheme Regulations, and has delegated its responsibility for determining investment policy and monitoring performance to the Pension Fund Panel.

The Pension Fund Panel is comprised of six County Council representatives, one non-voting employer representative, one non-voting employee/pensioner representative and two non-voting trade union representatives. Its responsibilities include overseeing the management of administering Scheme benefits, and consideration of applications for admitted body status to the Fund from qualifying community organisations.

External fund managers have been appointed by the Panel to make the day-to-day investment decisions.

The Panel's investment responsibilities

- **To approve and review the content of the Statement of Investment Principles, annually or more frequently if necessary.**
- **To appoint and review the appointment of investment managers and global custodian.**
- **To monitor the performance of the investment managers, quarterly.**
- **To assess the quality and performance of each investment manager annually, after consulting with the Panel's expert adviser on performance measurement, the investment consultant and the Lead Executive Director Corporate Resources.**
- **To set and review the investment parameters and asset allocation within which the investment managers operate.**
- **To review the appointment of each manager and the investment strategy of the Fund at three yearly intervals, or more frequently if the Panel deems it appropriate.**
- **To appoint expert advisers as appropriate, and monitor their performance.**
- **To ensure that the Fund is managed in accordance with relevant current legislation, guidelines, and best practice and that its investment objective is met.**

Investment objective

The investment objective of the Fund is to achieve a long term return on the Fund's assets which:

- **ensures that the Fund can meet its long term liabilities while minimising the long term cost to participating employers;**
- **recognises the advantages of maintaining the stability of contribution rates;**
- **does not subject the Fund to undue risk.**

Fund structure

The target asset allocation and scheme specific benchmark is:

- **24% in UK equities**
- **36% in overseas equities**
  - **9.0% in US**
  - **9.0% in Europe**
  - **4.5% in Japan**
  - **4.5% in Asia Pacific (Ex Japan)**
  - **9.0% in Emerging Market**
- **15% in index linked securities**
- **10% in corporate bond securities**
- **5% in property**
- **5% in private equity investments**
- **5% in infrastructure investments**

The target investment management structure is:

- **60% with one index tracking (passive) manager**
- **15% with one global equity (active) manager**
- **10% with one corporate bond (active) manager**
- **5% with two property unit trust managers, i.e. 2.5% each**
- **5% in private equity fund of funds investment vehicles**
- **5% in infrastructure investment vehicles**

The Panel determined the Fund structure and benchmark, with advice from the Fund's investment adviser, after considering the following issues:

- **the maturity profile of the Fund liabilities;**
- **the expected level of volatility and returns of various alternative Fund structures,**
- **adequate diversification of assets; and**
- **the Panel's attitude to solvency risk and mismatching risk, and the expected impact on the employers' contribution rates.**

Fund structure is considered every three years or more often if necessary, with the last full review (i.e. an asset liability modelling study) undertaken at two Panel meetings held in October 2009, and a further review in February 2011.

Private equity

The Panel approved a single small investment (less than 0.1% of the total Fund value) in local venture capital, which was launched in January 2002.

The Panel has allocated 5% of the Fund to private equity. The investment in this asset class takes the form of separate investments in private equity funds of funds. The Panel selected Morgan Stanley's Private Markets Fund III LP in November 2005, Morgan Stanley's Global Distressed Opportunities Fund LP in November 2006, NB Crossroads Fund XVIII in January 2007 and Morgan Stanley's Private Markets Fund IV LP in December 2007. Capital of around 7% of total Fund value was committed to these funds in the expectation of achieving an actual allocation of approximately 5% of Fund value over the life of the investments. Each investment is expected to represent at least a ten-year commitment.

Infrastructure

The Panel has allocated 5% of the Fund to infrastructure. The investment in this asset class will take the form of separate investments in infrastructure funds, and as yet the Panel has selected only one infrastructure fund of funds and committed capital of around 3% of total Fund value, with the intention of selecting at least one further infrastructure fund in the future. The Panel selected Global Infrastructure Partners' Fund II LP in July 2011 and Antin Infrastructure Partners Fund II LP in September 2013. Each investment is expected to represent at least a ten-year commitment.

Investment managers

- **Legal & General was appointed as index tracking manager, with effect from 18 December 2001, to manage UK and overseas equities, and fixed interest and index linked securities.**
- **M&G was appointed as global equity (active) manager, with effect from 9 January 2008 for half the actively managed global equity allocation. This was topped up to the full allocation on 7 July 2011.**
- **Wellington was appointed as corporate bond (active) manager, with effect from 1 March 2011.**
- **BlackRock and Schroder were appointed to manage property unit trusts, with effect from 18 December 2001.**

Direct investments

- **The Pension Fund has a capital commitment of $50 million to Morgan Stanley's Private Markets Fund III LP, a private equity fund of funds. The partnership agreement was signed on 7 April 2006, with the first capital call taking place in April 2006.**
- **The Pension Fund has a capital commitment of $10 million to Morgan Stanley's Global Distressed Opportunities Fund LP, a private equity fund of funds. The partnership agreement was signed on 21 December 2006, with the first capital call taking place in January 2007.**
- **The Pension Fund has a capital commitment of $27 million to NB Crossroads XVIII, a private equity fund of funds. The partnership agreement was signed on 27 March 2007, with the first capital call taking place in March 2007.**
- **The Pension Fund has a capital commitment of $30 million to Morgan Stanley's Private Markets Fund IV LP, a private equity fund of funds. The partnership agreement was signed on 7 December 2007, with the first capital call taking place in January 2008.**
- **The Pension Fund has a capital commitment of $43 million to Global Infrastructure Partners' GIP Fund II LP, an infrastructure fund. The partnership agreement was signed on 15 December 2011, with the first capital call taking place in May 2011.**
- **The Pension Fund has a capital commitment of €24 million to Antin Infrastructure Partners II LP, an infrastructure fund. The partnership agreement was signed on 20 December 2013.**

Performance targets

The active managers have the following targets incorporated within their investment management agreements:

	outperformance target over three year rolling periods %p.a.	risk constraint measures in operation
M&G (Global equities)	**2.5**	**μ**
Wellington (Corporate bonds)	**1.5**	**†**

μ M&G (global equities mandate) has an ex-ante tracking error (annualised) of between 4% and 6%.

† Wellington (corporate bonds) ex-ante tracking error (annualised) of less than 3%.

The property unit trusts held by BlackRock and Schroder are measured against the following:

	outperformance target over three year rolling periods %p.a.	whilst avoiding underperformance in any twelve month period %p.a.
Schroder (property unit trust)	**0.50**	**1.50**
BlackRock (property unit trust)	**0.50**	**1.50**

The private equity funds of funds will be measured against a performance target of 6% (gross of fees) per annum over the life of the fund above the appropriate public equity index.

Investment management agreements

- **All agreements with the investment managers allow for their appointments to be terminated by the Council without notice.**
- **Performance will normally be evaluated over three year rolling periods.**
- **The managers have a contractual responsibility to comply with any restrictions imposed by the most up to date Local Government Pension Scheme Investment Regulations.**

Custodian

- **The Northern Trust Company was appointed as global custodian with effect from 1 November 2001.**
- **The Custodian safeguards all assets within the Fund and ensures that all associated income is collected.**
- **The Custodian provides the County Council with monthly statements of assets, cashflows and corporate actions.**

Securities lending

The Fund participates in a securities lending programme managed by its Global Custodian, Northern Trust. Stock on loan is secured via a custom fund collateral section consisting of OECD AAA sovereign debt collateral. Initial collateral levels are not less than 105% of the market value of the borrowed securities unless the borrowed securities and collateral are denominated in the same currency, in which case 102% will apply. All equity loans will have initial collateral of 105% regardless of the currency of collateral except for US equities, which will have a collateral level of 102%. Marking to market is performed every business day.

With effect from July 2011, the Fund does not have any assets managed on a segregated basis, and therefore cannot benefit from the securities lending programme.

Audit responsibilities

- **The Pension Fund is subject to audit by the County Council's external auditor, Deloitte LLP.**
- **The external auditor is responsible for reporting on whether the Northumberland County Council Pension Fund Annual Report and Accounts gives a true and fair view of the amount and disposition of the Fund's assets and liabilities, other than liabilities to pay pensions and benefits after the end of the scheme year.**

Actuary

- **Aon Hewitt was appointed as actuary to the Fund with effect from October 2000, and reappointed following a competitive tendering process in June 2012.**
- **The actuary performs a valuation of the Fund every three years, in accordance with the Local Government Pension Scheme Regulations. The latest actuarial valuation was performed as at 31 March 2013, and revealed a funding level of 81%.**
- **The main purpose of the actuarial valuation is to assess and set the employers' contributions required to achieve 100% funding, whilst keeping the contribution rates as stable as possible. For the majority of the Fund employers, a 22-year deficit recovery period has been adopted.**

Investment adviser

Mercer was appointed as adviser to the Panel in March 2009 in respect of all issues relating to the investment of the Fund's assets.

Performance measurement services

Performance Measurement services are provided to the Fund by WM Company.

Fee structures

- **Investment Managers have ad valorem fee structures in place, except for Wellington, for whom a performance related structure is overlaid.**
- **WM Company (performance measurement) has a fixed fee structure in line with standard industry practice.**
- **Aon Hewitt (actuary) and Mercer (investment adviser) both have fees based on a combination of fixed fees and time costs in line with standard industry practice.**

Restrictions on investments

- **The powers to invest are embodied in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. Significant restrictions are as follows:**
  - **No more than 10% of the fund may be invested in unlisted securities of companies;**
  - **No more than 10% of the fund may be represented by a single holding;**
  - **No more than 10% of the fund may be deposited with any one bank (other than National Savings);**
  - **Loans from the fund, including money used by the administering authority or lent to other local authorities, but not including loans to the Government, may not in total exceed 10% of the value of the fund;**
  - **Each manager may deal in options, futures and contracts for differences for hedging purposes only.**
- **Other than those specified in the regulations, there are no further restrictions placed on the fund managers' ability to invest.**

Use of increased limits under regulation 14(3) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009

The above named regulation permits the administering authority to increase the percentage limits on certain permitted investments, so long as when doing so the authority complies with regulation 15 of the 2009 Regulations.

Insurance contracts

The limit under regulation 14(2) permits a maximum of 25% of the total value of the fund to be invested in any single insurance contract, whereas the increased limit under regulation 14(3) enables the administering authority to increase that limit to 35%.

The Northumberland County Council Pension Fund has two insurance contracts with Legal & General, each originally representing less than 25% of the value of the Fund. However, at the meeting of the Pension Fund Panel held on 30 March 2005, the Panel resolved to increase the maximum permitted in each of these insurance contracts to 35%. The purpose of this increased limit was to facilitate the transfer of assets managed by other fund manager(s) into the Legal & General insurance contracts during a transition to a new Fund structure. The increased limit will remain in place until further review to facilitate any future fund management changes in which Legal & General is used to provide a temporary or permanent manager for assets following the termination of an active manager's appointment. This decision complies with regulation 15 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009.

Contributions to partnerships

The limits under regulation 14(2) permit a maximum contribution of 2% of the total value of the fund to any single partnership and 5% of the total fund value to all partnerships, whereas the increased limits under regulation 14(3) enable the administering authority to increase those limits to 5% and 30% respectively.

The Northumberland County Council Pension Fund has allocated a target of 5% of total Fund value to private equity, and capital may be over-committed in order to achieve the target allocation. Private Equity fund of fund investments are set up as partnerships and therefore the limits on partnerships apply. At the meeting of the Pension Fund Panel held on 19 May 2006, the Panel resolved to increase the limits to accommodate the commitments that may be made in this investment. The limit on all contributions in any single partnership will be raised to 5% and the limit on all contributions to partnerships will be raised to 10%. The purpose of increasing these limits is to enable the Fund to commit capital of up to 10% in all private equity partnerships held, with the purpose of achieving and maintaining the 5% target allocation to this asset class. The increased limits will remain in place for the period in which the Fund maintains its target allocation of 5% to private equity investments. This decision complies with regulation 15 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009.

At the meeting of the Pension Fund Panel held on 23 November 2012, the Panel resolved to extend the increase to the limits on partnerships (as detailed above) to also apply to its 5% allocation to infrastructure investments and to raise the limit on all contributions to partnerships, whether private equity or infrastructure, to 15%.

Risk

- The primary risk upon which the Panel focuses is that arising through a mismatch between the Fund's assets and its liabilities.
- The Panel recognises that whilst increasing risk increases potential returns over a long period, it also increases the risk of a shortfall in returns relative to that required to cover the Fund's liabilities, which generally move in line with gilt yields, as well as producing more short-term volatility in the funding position. The Panel has taken advice on the matter and (in light of the objectives) considered carefully the implications of adopting different levels of risk.
- While the risk introduced through investing a significant proportion of the Fund's assets in equities could lead to volatility in the funding level disclosed at a subsequent actuarial valuation, it is felt that this risk is acceptable in view of the potential benefits of the expected extra returns.
- The Panel recognises the risks that may arise from the lack of diversification of investments. Subject to managing the risk from a mismatch of assets and liabilities, the Panel aims to ensure the asset allocation policy results in an adequately diversified portfolio across a number of managers.
- The documents governing the managers' appointments include a number of guidelines which, among other things, are designed to ensure that only suitable investments are held by the Fund. The managers are prevented from investing in asset classes outside of their mandate without the prior consent of the Panel.
- The safe custody of the Fund's assets is delegated to a professional custodian.
- Should there be a material change in the Fund's circumstances, the Panel will review whether and to what extent the investment arrangements should be altered; in particular whether the current risk profile remains appropriate.
- Risk is also controlled by (at least) quarterly reviews of past performance and future plans of each fund manager, and obtaining the advice of an independent expert who attends all Panel meetings.
- The Panel also determines the degree of risk taken by the investment fund managers by setting performance targets and monitoring the risk levels taken by each manager in order to achieve that target.

Expected returns

- The Fund invests in a range of UK and overseas stocks and bonds. Part of the portfolio is managed on a passive basis where the return is expected to be in line with the market as a whole, and part on an active basis where the objective is to outperform the corresponding markets. A broad measure of the long term return expected on each major asset class is:

Equities	6.6%
Property	4.6%
Private equity	8.8%
Corporate bonds	4.1%
Gilts	2.6%

  However the return in any short-term period, such as one year, may vary significantly from these long-term averages.

- In order to fulfil the assumptions used in the actuarial valuation of the Fund, a minimum return of 6.0% per annum is required long term.

Realisation of investments

- The fund managers have discretion to realise investments whenever they wish to change the investments held. The vast majority of investments held are readily marketable, the principal exceptions being private equity, infrastructure and property, which may take some time to realise; property could take up to two years to realise, depending on the market, but private equity and infrastructure have a lifespan of somewhere between seven and fourteen years, and are therefore a significant long-term commitment.
- The Fund is not sufficiently mature to require the realisation of investments to meet the commitments to pay pensions, therefore there is no policy as yet upon this issue.

Social, ethical and environmental issues

- The Pension Fund Panel does not place restrictions on investment managers in choosing investments in quoted companies except as stated above. The Panel does, however, request that the managers:
  - consider that companies must be run in the long term interests of their shareholders and will need to manage relationships with employees, suppliers and customers effectively. Companies will be expected to behave ethically and have regard for the environment and society as a whole in carrying out their business. These considerations should be taken into account when managers are assessing companies, with issues of material concern being raised in their meetings with management;
  - avoid investing in companies implicated in serious crime;
  - avoid investing in countries covered by United Nations trade embargo.
- The Pension Fund Panel endorses Pensions & Investment Research Consultants (PIRC) Limited's Shareholder Voting Guidelines, and GovernancePlus Guidelines, which cover social, ethical and environmental issues.
- Scheme members have the option of paying additional voluntary contributions. When doing so, scheme members must choose between a number of different types of investments, one of which is an ethically screened portfolio.

Corporate governance

- As a general principle, the Pension Fund Panel expects the Fund's investment managers to comply with the Statement of Principles issued by the Institutional Shareholders' Committee entitled 'The Responsibilities of Institutional Shareholders and Agents' (the 'ISC Principles'), which applies to UK listed companies.
- The Pension Fund Panel requires that its UK equity investment manager votes their shareholdings in accordance with Pensions & Investment Research Consultants (PIRC) Limited's Shareholder Voting Guidelines, and GovernancePlus Guidelines, which cover social, ethical and environmental issues.
- The Panel expects the Fund's investment managers to vote every share owned, where practical.
- The Panel endorses the voting policies of the overseas equity investment managers.

Compliance statement

Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 2009 effectively require administering authorities to state the extent to which they comply with the six principles of investment practice set out in the document published in December 2009 by CIPFA, the Chartered Institute of Public Finance and Accountancy, and called *Investment Decision-Making in the Local Government Pension Scheme: A Guide to the Application of the Myners Principles* and give the reasons for not complying where they do not do so. Therefore, a Compliance Statement is appended to this document.

Statement of Compliance with Myners Principles

Details of 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; and**
- **those persons or organisations should have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.**

Northumberland County Council Pension Fund has a dedicated pensions committee, known as the Pension Fund Panel, which is supported by suitably experienced and qualified officers, the Fund actuary and an independent investment adviser. Other specialist advisers are employed to provide advice on specific issues such as performance measurement. External advice is obtained as required when appropriate in-house expertise is not available.

The Fund's Training Strategy provides the opportunity for members to attend externally run courses such as the tailored three-day training course run by the Employers' Organisation for Local Government. This is in addition to the information provided in Pension Fund Panel papers, and by fund managers and advisers at the meetings. Tailored training is organised, for example on infrastructure as an asset class, when a decision on a particular issue is planned. This provides Panel members with sufficient knowledge to be able to evaluate and challenge the advice they receive.

The investment adviser, who was selected and appointed by the Pension Fund Panel attends all meetings to provide advice, other than those meetings where attendance would result in conflict of interests.

The Pension Fund Panel focuses on setting the strategy for the pension fund and monitoring performance. The Panel delegates the day-to-day administration of the Pension Scheme to the Lead Executive Director Corporate Resources, and delegates the day-to-day investment decisions to external fund managers.

The Pension Fund Panel reviews its structure and composition when necessary and provides members with a handbook containing the terms of reference and operational procedures.

The Fund maintains a Governance Compliance Statement in accordance with regulation 31 of the Local Government Pension Scheme Regulations 2008. This contains further details of the decision making processes.

Panel papers are despatched to members to be received at least 5 days in advance of each meeting to allow members sufficient time to read the papers.

An annual Business Plan is prepared and submitted to the Panel for consideration. Progress against the plan is evaluated annually.

Conflicts of interest are managed actively. At each Panel meeting, elected members are asked to highlight conflicts of interest.

Principle 2: Clear objectives

An overall investment objective(s) should be set out for the fund that take account of the scheme's liabilities, the potential impact on local tax payers, the strength of the covenant for non-local authority employers, and the attitude to risk of both the administering authority and 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. A long term view is taken in setting those objectives.

Asset-liability modelling is undertaken by the investment adviser to aid the setting of investment strategy and to ensure that the Panel understand the risks. The Fund has a scheme-specific investment strategy (i.e. a customised benchmark).

The Pension Fund Panel's attitude to risk is taken into account in setting the investment strategy.

Reviews of investment strategy focus on the split between broad asset classes, i.e. equities, bonds and alternative investments.

Investment management agreements set clear benchmarks and risk parameters and include the requirement to comply with the Fund's Statement of Investment Principles.

The appointments of advisers are reviewed regularly. Investment and actuarial advisers are appointed under separate contracts.

The Funding Strategy requires specific consideration of the covenants of the Fund's participating employers when setting the employer contribution rates and the need 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 local tax payers, the strength of the covenant for participating employers, the risk of their default and longevity risk.

The Fund takes advice from the 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 when assessing risk tolerance. Asset-liability modelling is undertaken by the investment adviser who obtains information from the actuary regarding liabilities to use in the model. All risk measurement in this context is performed with reference to the liabilities.

The funding strategy for the Fund is expressed in relation to the solvency of the Fund. Consideration is given to the affordability of employer contributions at the actuarial valuation.

The Pension Fund operates within the internal control arrangements administered by the County Council which are subject to internal and external audit. The external auditors report annually to the Pension Fund Panel and the County Council's Audit Committee.

The County Council maintains a risk register which includes risks relating to the Pension Fund. The risk register is reported to the Risk Appraisal Panel.

Principle 4: Performance assessment

Arrangements should be in place for the formal measurement of performance of the investments, investment managers and advisers.

Administering authorities should also periodically make a formal assessment of their own effectiveness as a decision-making body and report on this to scheme members.

The performance of the Fund and of the individual fund managers is monitored quarterly by officers, the investment adviser and the Pension Fund Panel. Investment managers are given specific performance and risk targets and these are assessed as part of the monitoring process.

The Pension Fund Panel monitors performance against planned activities shown in the Northumberland County Council Pension Fund annual Business Plan and reviews the appointment of advisers when appropriate.

Training and attendance of Pension Fund Panel members 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**
- **include a statement of their policy on responsible ownership in the statement of investment principles**
- **report periodically to members on the discharge of such responsibilities.**

The Fund instructs its UK equity manager to vote in line with PIRC's recommendations on the FTSE 350. For other equity holdings the Fund delegates its voting to the relevant manager i.e.Legal & General and M&G.

The Fund's policy on responsible ownership is included in the Statement of Investment Principles.

The Fund's annual report and accounts reproduces the Statement of Investment Principles in full. The annual report and accounts and the Statement of Investment Principles 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**
- **provide regular communication to scheme members in the form they consider most appropriate.**

The Fund's policy statements, including its Governance Compliance Statement, Statement of Investment Principles, Statement of Policy Concerning Communication, annual Business Plan and Funding Strategy Statement are maintained regularly. Stakeholders are consulted on changes. Documents are available on the Northumberland County Council website.

The Fund produces an annual report and accounts in which the key documents (listed above) are reproduced in full. A hard copy of the annual report is sent to all participating employers and it is published on the website.

There is an annual meeting held for employers, and a representative of the (non-County Council) employers sits on the Pension Fund Panel.

The Fund produces regular newsletters for pensioner members and for active members and briefings for employers. The website is updated regularly.

Agenda papers for the Pension Fund Panel are published on the website.

Funding Strategy Statement

1. INTRODUCTION

Overview

This Statement, originally prepared in accordance with Regulation 76A of the Local Government Regulations 1997, has been reviewed in accordance with Regulation 35 of the Local Government Pension Scheme (Administration) Regulations 2008 (the Administration Regulations). The Statement describes Northumberland County Council's strategy, in its capacity as Administering Authority (the Administering Authority), for the funding of the Northumberland County Council Pension Fund (the Fund).

The Local Government Pension Scheme Regulations 2013 (the 2013 Regulations) come into force on 1 April 2014. Where reference is made to individual regulations in the Administration Regulations or the Benefits Regulations, the corresponding regulation in the 2013 Regulations is provided alongside in brackets.

As required by Regulation 35(3)(a) of the Administration Regulations (Regulation 58(4)(a) of the 2013 Regulations), the Statement has been prepared having regard to guidance published by CIPFA in March 2004 entitled "Guidance on Preparing and Maintaining a Funding Strategy Statement and to the Fund's Statement of Investment Principles". It also has regard to updated guidance published by CIPFA on 3 October 2012.

Consultation

In accordance with Regulation 35(3)(b) of the Administration Regulations (Regulation 58(1) of the 2013 Regulations), all employers participating within the Northumberland County Council Pension Fund and the principal trade unions representing the contributors have been consulted on the contents of this Statement and their views have been taken into account in formulating the Statement. However, the Statement describes a single strategy for the Fund as a whole.

In addition, the Administering Authority has had regard to the Fund's Statement of Investment Principles published under Regulation 12 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (the Investment Regulations).

The Fund Actuary, Aon Hewitt Limited, has also been consulted on the contents of this Statement.

Purpose of this Statement

The main purpose of this Funding Strategy Statement is to set out the processes by which the Administering Authority:

- **establishes a clear and transparent funding strategy, specific to the Fund, which will identify how employers' pension liabilities are best met going forward;**
- **supports the regulatory requirement in relation to the desirability of maintaining as nearly constant a common rate of contributions as possible; and**
- **takes a prudent longer-term view of funding the Fund's liabilities;**

noting that whilst the funding strategy applicable to individual employers or categories of employers must be reflected in the Funding Strategy Statement, its focus should at all times be on those actions which are in the best long term interests of the Fund.

Links to investment policy set out in the Statement of Investment Principles

The Authority has produced this Funding Strategy Statement having taken an overall view of the level of risk inherent in the investment policy set out in the Statement of Investment Principles and the funding strategy set out in this Statement.

The assets that most closely match the liabilities of the Fund are fixed interest and index-linked Government bonds of appropriate term relative to the liabilities. The Fund's asset allocation as set out in the Statement of Investment Principles invests a significant proportion of the Fund in assets such as equities which are expected but not guaranteed to produce higher returns than Government bonds in the long term. The Administering Authority has agreed with the Fund Actuary that the Funding Target on the ongoing basis will be set after making some allowance for this higher anticipated return. However, the Administering Authority recognises that outperformance is not guaranteed and that, in the absence of any other effects, if the higher expected returns are not achieved the solvency position of the Fund will deteriorate.

The funding strategy recognises the investment targets and the inherent volatility arising from the investment strategy, by being based on financial assumptions which are consistent with the expected return on the investments held by the Fund, and by including measures that can be used to smooth out the impact of such volatility.

The Administering Authority will continue to review both documents to ensure that the overall risk profile remains appropriate including, where appropriate, commissioning asset liability modelling or other analysis techniques.

Review of Statement

The Administering Authority undertook its latest substantive review of this Statement in March 2014.

The Administering Authority will formally review this Statement as part of each triennial valuation of the Fund unless circumstances arise which require earlier action.

The Administering Authority will monitor the funding position of the Fund on an approximate basis at regular intervals between actuarial valuations and will discuss with the Fund Actuary whether any significant changes have arisen that require action.

2. AIMS AND PURPOSE OF THE FUND

Purpose of the Fund

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

Aims of the Fund

The aims of the Fund are:

a) To comply with regulation 36 of the Administration Regulations (Regulation 62 of the 2013 Regulations) and specifically to adequately fund benefits to secure the Fund's solvency while taking account of the desirability of maintaining as nearly a constant contribution rate as possible

The Administering Authority recognises that the requirement to keep employer contribution rates as nearly constant as possible can run counter to the following requirements:

- **the regulatory requirement to secure solvency; which should be assessed in light of the risk profile of the Fund and risk appetite of the Administering Authority and employers;**
- **the requirement that the costs should be reasonable to Scheduled and Admission Bodies, other bodies and to taxpayers (subject to not taking undue risks); and**
- **maximising income from investments within reasonable risk parameters (see (d) below).**

Producing low volatility in employer contribution rates requires material investment in assets which 'match' the employers' liabilities. In this context, 'match' means assets which behave in a similar manner to the liabilities as economic conditions alter. For the liabilities represented by benefits payable by the Local Government Pension Scheme, such assets would tend to comprise gilt edged investments.

Other classes of assets, such as stocks and property, are perceived to offer higher long term rates of return, on average, and consistent with the requirement to maximise the returns from investments within reasonable risk parameters, the Administering Authority invests a substantial proportion of the Fund in such assets. However, these assets are more risky in nature, and that risk can manifest itself in volatile returns over short term periods, and a failure to deliver the anticipated returns in the long term.

This short term volatility in investment returns can produce a consequent volatility in the measured funding position of the Fund at successive actuarial valuations, with knock on effects to employer contribution rates. The impact on employer rates can be mitigated by use of smoothing adjustments at each valuation.

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

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

b) To ensure that sufficient resources are available to meet all liabilities as they fall due

The Administering Authority recognises the need to ensure that the Fund has, at all times, sufficient liquid assets to be able to pay pensions, transfer values, costs, charges and other expenses. It is the Administering Authority's policy that such expenditure is met, in the first instance, from incoming employer and employee contributions to avoid the expense of disinvesting assets. The Administering Authority monitors the position to ensure that all cash requirements can be met.

c) To manage employers' liabilities effectively

The Administering Authority seeks to ensure that all employers' liabilities are managed effectively. In a funding context, this is achieved by seeking regular actuarial advice, ensuring that employers are kept informed and consulted, and through regular monitoring of the funding position and the outlook for employers' contributions.

d) To maximise the income from investments within reasonable risk parameters

The Administering Authority recognises the desirability of maximising investment income within reasonable risk parameters. Investment returns higher than those available on government bonds are sought through investment in other asset classes such as stocks and property. The Administering Authority ensures that risk parameters are reasonable by:

- **restricting investment to the levels permitted by the Investment Regulations;**
- **restricting investment to asset classes generally recognised as appropriate for UK pension funds;**
- **analysing the volatility and absolute return risks represented by those asset classes in collaboration with the Fund's actuary, investment advisers and fund managers and ensuring that they remain consistent with the risk and return profiles anticipated in the funding strategy;**
- **limiting concentration of risk by developing a diversified investment strategy; and**
- **monitoring the mis-matching risk, i.e. the risk that the investments do not move in line with the Fund's liabilities.**

3. RESPONSIBILITIES OF THE KEY PARTIES

The three parties whose responsibilities to the Fund are of particular relevance are the Administering Authority, the individual employers and the Fund Actuary.

Their key responsibilities are as follows:

The Administering Authority will:

a) Administer the Fund

b) Collect investment income and other amounts due to the Fund as set out in the Administration Regulations including employer and employee contributions and, as far as it is able, ensure these contributions are paid by the due date

Individual employers must pay contributions in accordance with Regulations 39 to 43 of the Administration Regulations (Regulations 67 to 70 of the 2013 Regulations). The Administering Authority will ensure that all employers are aware of these requirements especially the requirement of the Pensions Act 1995 that members' contributions are paid by the 19th of the month following the month that it is paid by the member. The Administering Authority may charge interest on late contributions in accordance with Regulation 44 of the Administration Regulations (Regulation 71 of the 2013 Regulations).

The Administering Authority will ensure that action is taken to recover assets from Admission Bodies whose admission agreement has ceased (and from other employers whose participation in the Fund has ceased) by:

- **requesting that the Fund Actuary calculates any deficiency at the date of the cessation of participation; and**
- **notifying the body that it must meet any deficiency at the cessation.**

c) Pay from the Fund the relevant entitlements as set out by the Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (the Benefits Regulations) (Regulations 22 to 52 of the 2013 Regulations)

d) Invest surplus monies in accordance with the regulations

The Administering Authority will comply with Regulation 11 of the Investment Regulations, which states that surplus fund money, not needed immediately, must be invested in a wide variety of suitable investments, after taking proper advice.

e) Ensure that cash is available to meet liabilities as and when they fall due

The Administering Authority recognises this duty and discharges it in the manner set out in section 2(b) above.

f) Manage the valuation process in consultation with the Fund Actuary

The Administering Authority ensures it communicates effectively with the Fund Actuary to

- **agree timescales for the provision of information and provision of valuation results;**
- **ensure provision of data of suitable accuracy;**
- **ensure that the Fund Actuary is clear about the content of the Funding Strategy Statement;**
- **ensure that participating employers receive appropriate communication throughout the process; and**
- **ensure that reports are made available as required by guidance and regulation.**

g) Prepare and maintain a Statement of Investment Principles and a Funding Strategy Statement after due consultation with interested parties

The Administering Authority will ensure that both documents are prepared and maintained in the required manner.

h) Monitor all aspects of the Fund's performance and funding and amend these two documents if required

In order to monitor developments, the Administering Authority may from time to time request informal valuations or other calculations. Generally, these are undertaken quarterly and the calculations will be based on an approximate roll forward of asset and liability values, with liabilities calculated by reference to assumptions consistent with the most recent preceding valuation. Specifically, it is unlikely that the liabilities would be calculated using individual membership data, and nor would the assumptions be subject to review as occurs at formal triennial valuations.

The Administering Authority monitors investment performance of the Fund on a quarterly basis.

The Statement of Investment Principles will be formally reviewed annually, unless circumstances dictate earlier amendment.

The Administering Authority will formally review this Statement as part of each triennial valuation process unless circumstances arise which require earlier action.

i) Effectively manage any potential conflicts of interest arising from its dual role as both Administering Authority and as a Scheme Employer

Individual employers will:

- **deduct contributions from employees' pay correctly;**
- **pay all contributions, including their employer contribution as determined by the Fund Actuary, promptly by the due date;**
- **develop a policy on certain discretions and exercise those discretions within the regulatory framework, ensuring that the Administering Authority has copies of current policies covering those discretions;**
- **pay for additional benefits awarded to members, early release of benefits or other one off strain costs in accordance with agreed arrangements; and**
- **notify the Administering Authority promptly of all changes to membership, or other changes which affect future funding;**
- **note and if desired respond to any consultation regarding the Funding Strategy Statement, the Statement of Investment Principles or other policies.**

The Fund Actuary will:

a) **Prepare triennial actuarial valuations including the setting of employers' contribution rates and issuing a Rates and Adjustments Certificate, after agreeing assumptions with the Administering Authority and having regard to the Funding Strategy Statement**
Valuations will be prepared in accordance with generally accepted actuarial methods and reported on in accordance with current actuarial reporting Standards issued by the Financial Reporting Council, to the extent that the Standards are relevant to the Fund.

b) **Prepare advice and calculations in connection with**

- **bulk transfers and individual benefit-related matters;**
- **valuations on the cessation of admission agreements or when an employer ceases to employ any active members; and**
- **bonds and other forms of security against the financial effect on the Fund of employer's default.**

c) **Assist the Administering Authority in assessing whether employer contributions need to be revised between actuarial valuations as required by the Administration Regulations (or the 2013 Regulations)**

d) **Ensure that the Administering Authority is aware of any professional guidance requirements which may be of relevance to the Fund Actuary's role in advising the Administering Authority.**
Such advice will where appropriate take account of the funding position and funding and investment strategy of the Fund, along with other relevant matters.

4. FUNDING STRATEGY

Risk based approach

The Fund utilises a risk based approach to funding strategy.

A risk based approach entails carrying out the actuarial valuation on the basis of the assessed likelihood of meeting the funding objectives, rather than relying on a 'deterministic' approach which gives little idea of the associated risk. In practice, three key decisions are required for the risk based approach:

- **the Solvency Target (the value of assets the Administering Authority requires the Fund to hold to meet the Fund's liabilities);**
- **the Trajectory Period (how quickly the Administering Authority requires the Fund to get there); and**
- **the Probability of Funding Success (the current likelihood as required by the Administering Authority that the Fund will actually achieve the Solvency Target by the end of the Trajectory Period).**

These three choices, supported by risk modelling carried out by the Fund Actuary, define the appropriate levels of contribution payable now and, by extension, the appropriate valuation approach to adopt now. Together they measure the riskiness of the funding strategy.

These three terms are considered in more detail below.

Solvency Target

The Administering Authority's primary aim is long-term solvency. Accordingly, employers' contributions will be set to ensure that 100% of the liabilities can be met over the long term. The Solvency Target is the value of assets which the Administering Authority wishes the Fund to hold at the end of the Trajectory Period (see later) to meet this aim.

The Fund is deemed to be solvent when the assets held are equal to or greater than 100% of the Solvency Target, where the Solvency Target is the value of the Fund's liabilities evaluated using appropriate actuarial methods and assumptions.

For employers:

- **regarded by the Administering Authority as being of sound covenant with an indefinite period to expected cessation; or**
- **with guarantors of sound covenant agreeing to subsume the employer's assets and liabilities following cessation;**

appropriate actuarial methods and assumptions are taken to be measurement by use of the Projected Unit method of valuation, and using assumptions such that, if:

- **the Fund had reached the Solvency Target; and**
- **its financial position continued to be assessed by use of such methods and assumptions; and**
- **contributions were paid in accordance with those methods and assumptions;**

then there would be a chance of at least 80% that the Fund would continue to be 100% funded after a reasonable timeframe. The level of funding implied by this is the Solvency Target. For the purpose of this Statement, the required level of chance is defined as the Probability of Maintaining Solvency.

For all other employers, including bodies with limited duration in the Fund or whose liabilities are expected to be orphaned following cessation, the required Probability of Maintaining Solvency will be set at a more prudent level dependent on circumstances. For most such bodies, the chance of achieving solvency will be set commensurate with assumed investment in an appropriate portfolio of Government index linked and fixed interest bonds after cessation.

Probability of Funding Success

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

- **Consistent with the aim of enabling employers' contribution rates to be kept as nearly constant as possible, the required chance of achieving the Solvency Target at the end of the relevant Trajectory Period for each employer or employer group can be altered at successive valuations within an overall envelope of acceptable risk.**
- **Following a valuation, the Administering Authority will not permit contributions to be set that have an unacceptably low chance of achieving the Solvency Target at the end of the relevant Trajectory Period.**

Funding Target

The Funding Target is the value of assets which the Fund needs to hold at the valuation date to pay the liabilities at that date as indicated by the chosen valuation method and assumptions. It is a product of the triennial actuarial valuation exercise and is not necessarily the same as the Solvency Target. It is instead the product of the data, chosen assumptions, and valuation method. The valuation method including the components of Funding Target, future service costs and any adjustment for the surplus or deficiency simply serve to set the level of contributions payable, which in turn dictates the chance of achieving the Solvency Target at the end of the Trajectory Period (defined below). The Funding Target will be the same as the Solvency Target only when the methods and assumptions used to set the Funding Target are the same as the appropriate funding methods and assumptions used to set the Solvency Target (see above).

Consistent with the aim of enabling employers' contribution rates to be kept as nearly constant as possible:

- **Contribution rates are set by use of the Projected Unit valuation method for most employers. The Projected Unit method is used in the actuarial valuation to determine the cost of benefits accruing to the Fund as a whole and for employers who continue to admit new members. This means that the contribution rate is derived as the cost of benefits accruing to employee members over the year following the valuation date expressed as a percentage of members' pensionable pay over that period.**
- **For employers who no longer admit new members, the Attained Age valuation method is normally used. This means that the contribution rate is derived as the average cost of benefits accruing to members over the period until they die, leave the Fund or retire.**

Application to different types of body

Some comments on the principles used to derive the Funding Target for different bodies in the Fund are set out below.

For employers:

- **regarded by the Administering Authority as being of sound covenant with an indefinite period to expected cessation; or**
- **with guarantors of sound covenant agreeing to subsume the employer's assets and liabilities following cessation;**

the Administering Authority will adopt a general approach in this regard of assuming indefinite investment in a broad range of assets of higher risk than risk free assets. With regard to guarantors, they must have been judged to be of suitable covenant by the Administering Authority (see section on Guarantors in section 5).

For all other employers, including bodies with limited duration in the Fund or whose liabilities are expected to be orphaned following cessation, the Administering Authority will have regard to the potential for participation to cease (or to have no contributing members), the potential timing of such cessation, and any likely change in notional or actual investment strategy as regards the assets held in respect of the body's liabilities at the date of cessation (i.e. whether the liabilities will become 'orphaned' or a guarantor exists to subsume the notional assets and liabilities).

Full funding

The Fund is deemed to be fully funded when the assets held are equal to 100% of the Funding Target. When assets held are greater than this amount the Fund is deemed to be in surplus, and when assets held are less than this amount the Fund is deemed to be in deficiency.

Smoothing adjustments

Consistent with the aim of enabling employer contribution rates to be kept as nearly constant as possible, and having regard to the risks inherent in such an approach, the Administering Authority may also agree with the Fund Actuary the use of explicit smoothing adjustments in the calculation of the Funding Target. It is unlikely that use of these smoothing adjustments will be extended to employers whose participation in the Fund is for a fixed period (for example, an employer admitted by virtue of having been awarded a best value outsourcing contract).

Trajectory and Recovery Periods

The Trajectory Period in relation to an employer is the period between the valuation date and the date on which solvency is targeted to be achieved.

Where an actuarial valuation reveals that the Fund is in surplus or deficiency against the Funding Target, employers' contribution rates will be adjusted to target restoration of the Funding Target over a period of years (the Recovery Period). The Recovery Period in relation to an employer or group of employers is therefore a period over which any adjustment to the level of contributions in respect of a surplus or deficiency relative to the Funding Target used in the valuation is payable. As noted earlier, the valuation method, including components of the Funding Target, future service costs and adjustment for surplus or deficiency simply serve to set a level of contributions payable, which in turn dictates the chance of achieving the Solvency Target at the end of the Trajectory Period.

For simplicity, the Trajectory Period for the largest employer (or employer group) in the Fund and the Recovery period are both set to be the same.

The Recovery Period applicable for each participating employer is set by the Administering Authority in consultation with the Fund Actuary and the employer, with a view to balancing the various funding requirements against the risks involved due to such issues as the financial strength of the employer and the nature of its participation in the Fund.

The Administering Authority recognises that a large proportion of the Fund's liabilities are expected to arise as benefit payments over long periods of time. For employers of sound covenant, the Administering Authority is prepared to agree to Recovery Periods which are longer than the average future working lifetime of the membership of that employer. (i.e. the estimated period of time until the last active member leaves or retires). The Administering Authority recognises that such an approach is consistent with the aim of keeping employer contribution rates as nearly constant as possible. However, the Administering Authority also recognises the risk in relying on long Recovery and Trajectory Periods and has agreed with the Fund Actuary a limit of 22 years for both, for employers which are assessed by the Administering Authority as being long term secure employers.

The Administering Authority's policy is to set Recovery Periods for each employer which are as short as possible within this framework. In general for employers that are closed to new entrants and the participation is of sufficient term the Recovery Period is set to be the estimated future working lifetime of the active membership.

The exception to this limit is Northumberland College, for whom the Administering Authority has agreed to use a Recovery Period of 30 years to assist in smoothing contribution rates as the employer transitions to an alternative Funding Target.

For employers whose participation in the Fund is for a fixed period it is unlikely that the Administering Authority and Fund Actuary would agree to a recovery period longer than the remaining term of participation.

The Administering Authority obtains the opinion of Northumberland County Council's Executive Director of Wellbeing and Community Health Services to categorise each academy in Northumberland into one of three groups: A meaning robustly viable; B meaning viability less certain; or C meaning concerns over viability. Each academy is categorised at inception and at each valuation date. For category A academies, a 22 year Recovery Period is applied; for category B a 14 year Recovery Period is applied; and for category C a Recovery Period of up to 7 years is applied unless the Administering Authority receives an instruction from the Department for Education to lengthen the Recovery Period of a specified academy, in which case, a Recovery Period of up to 22 years may be applied for category B and C academies.

A period of 22 years has been used for Northumberland County Council, the largest employer in the Fund. Trajectory and Recovery Periods for other employers or employer groups may be shorter and may not necessarily be the same as each other in order to suitably balance risk to the Fund and cost to the employer.

Stepping

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

Grouping

In some circumstances it is desirable to group employers within the Fund together for funding purposes to calculate employer contribution rates. Reasons might include reduction of volatility of contribution rates for small employers, facilitating situations where employers have a common source of funding or accommodating employers who wish to share the risks related to their participation in the Fund.

The Administering Authority recognises that grouping can give rise to cross subsidies from one employer to another over time. Employers may be grouped entirely, such that all of the risks of participation are shared, or only partially grouped such that only specified risks are shared. The Administering Authority's policy is to consider the position carefully at each valuation and to notify each employer that is grouped that this is the case, which other employers it is grouped with, and details of the grouping method used. If the employer objects to this grouping, it will be offered its own contribution rate.

Following commencement in the Fund, non-academy Scheduled Bodies with less than 20 contributing members will be included within the 'Small Scheduled Bodies' group by default.

All employers in the Fund are grouped together in respect of the risks associated with payment of benefits on death in service and ill-health retirement. In other words, the cost of such benefits is shared across all the employers in the Fund. Such benefits at no fault of the employer can cause funding strains which could be significant for some of the smaller employers without insurance or sharing of risks. The Fund, in view of its size, does not see it as cost effective or necessary to insure these benefits externally and this is seen as a pragmatic and low cost approach to spreading the risk.

Notional Sub Funds

In order to establish contribution rates for individual employers or groups of employers it is convenient to notionally subdivide the Fund as a whole between the employers, as if each employer had its own notional sub fund within the Fund.

This subdivision is for funding purposes only. It is purely notional in nature and does not imply any formal subdivision of assets, nor ownership of any particular assets or groups of assets by any individual employer or group.

Roll forward of Sub Funds

The notional sub fund allocated to each employer will be rolled forward allowing for all cashflows associated with that employer's membership, including contribution income, benefit outgo, transfers in and out and investment income allocated as set out below. In general no allowance is made for the timing of contributions and cashflows for each year are assumed to be made half way through the year with investment returns assumed to be uniformly earned over that year. Further adjustments are made for:

- **a notional deduction to meet the expenses paid from the Fund in line with the assumption used at the previous valuation;**
- **allowance for any known material internal transfers in the Fund (cashflows will not exist for these transfers). The Fund actuary will assume an estimated cashflow equal to the value of the liabilities transferred from one employer to the other unless some other approach has been agreed between the two employers;**
- **allowance for death in service and other benefits shared across all employers in the Fund (see earlier); and**
- **an overall adjustment to ensure the notional assets attributed to each employer is equal to the total assets of the Fund which will take into account any gains or losses related to the orphan liabilities.**

In some cases information available will not allow for such cashflow calculations. In such a circumstance:

- **where, in the opinion of the Fund Actuary, the cashflow data which is unavailable is of low materiality, estimated cashflows will be used; and**
- **where, in the opinion of the Fund Actuary, the cashflow data which is unavailable is material, or the results of the cashflow approach appears to give unreliable results perhaps because of unknown internal transfers, the Fund Actuary will instead use an analysis of gains and losses to roll forward the notional sub fund. Analysis of gains and losses methods are less precise than use of cashflows and involve calculation of gains and losses to the surplus or deficiency exhibited at the previous valuation. Having established an expected surplus or deficiency at the current valuation, comparison of this with the liabilities evaluated at the current valuation leads to an implied notional asset holding.**

Fund maturity

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

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

5. SPECIAL CIRCUMSTANCES RELATED TO CERTAIN EMPLOYERS

Interim reviews for Admission Bodies

Regulation 38(4) of the Administration Regulations (Regulation 64 of the 2013 Regulations) provides the Administering Authority with a power to carry out valuations in respect of employers which are expected to cease at some point in the future and for the Fund Actuary to certify revised contribution rates, between triennial valuation dates.

The Administering Authority's overriding objective at all times is that, where possible, there is clarity over the Funding Target for that body, and that contribution rates payable are appropriate for that Funding Target. However, this is not always possible as any date of cessation of participation may be unknown (for example, participation may be assumed at present to be indefinite), and also because market conditions change daily.

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

- **Where the date of cessation is known, and is more than three years after the most recent preceding triennial actuarial valuation, or is unknown and assumed to be indefinite, interim valuations will generally not be carried out at the behest of the Administering Authority.**
- **For Transferee Admission Bodies falling into the above category, the Administering Authority sees it as the responsibility of the relevant Scheme Employer to instruct it if an interim valuation is required. Such an exercise would be at the expense of the Relevant Scheme Employer unless otherwise agreed.**
- **A material change in circumstances, such as the date of cessation becoming known, material membership movements or material financial information coming to light may cause the Administering Authority to informally review the situation and subsequently formally request an interim valuation.**
- **For an employer whose participation is due to cease within three years of the most recent preceding triennial valuation, the Administering Authority will monitor developments and may see fit to request an interim valuation at any time.**

Notwithstanding the above guidelines, the Administering Authority reserves the right to request an interim valuation of any employer at any time if Regulation 38(4) of the Administration Regulations (Regulation 64(4) of the 2013 Regulations) applies.

Guarantors

Some employers may participate in the Fund by virtue of the existence of a Guarantor. The Administering Authority maintains a list of employers and their associated Guarantors. The Administering Authority, unless notified otherwise, sees the duty of a Guarantor to include the following:

- **If an employer ceases and defaults on any of its financial obligations to the Fund, the Guarantor is expected to provide finance to the Fund such that the Fund receives the amount certified by the Fund Actuary as due, including any interest payable thereon.**
- **If the Guarantor is an employer in the Fund and is judged to be of suitable covenant by the Administering Authority, the Guarantor may defray some of the financial liability by subsuming the residual liabilities into its own pool of Fund liabilities. In other words, it agrees to be a source of future funding in respect of those liabilities should future deficiencies emerge.**

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

Bonds and other securitisation

Regulation 7 of the Administration Regulations (Part 3 of Schedule 2 of the 2013 Regulations) creates a requirement for a new Admission Body to carry out to the satisfaction of the Administering Authority (and the Scheme Employer in the case of a Transferee Admission Body admitted under Administration Regulation 6(2)(a) (or falling under paragraph 1(d) of Part 3 of Schedule 2 of the 2013 Regulations)) an assessment taking account of actuarial advice of the level of risk on premature termination by reason of insolvency, winding up or liquidation.

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

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

- **In the case of Transferee Admission Bodies admitted under Regulation 6(2)(a) of the Administration Regulations (Paragraph 1(d) of Part 3 of Schedule 2 of the 2013 Regulations) and other Admission Bodies with a Guarantor, and so long as the Administering Authority judges the relevant Scheme Employer or Guarantor to be of sufficiently sound covenant, any bond exists purely to protect the relevant Scheme Employer or Guarantor on default of the Admission Body. As such, it is entirely the responsibility of the relevant Scheme Employer or Guarantor to arrange any risk assessments and decide the level of required bond. The Administering Authority will be pleased to supply some standard calculations provided by the Fund Actuary to aid the relevant Scheme Employer or Guarantor, but this should not be construed as advice to the relevant Scheme Employer or Guarantor on this matter.**

- **In the case of Transferee Admission Bodies admitted under Regulation 6(2)(a) or 6(20)(b) of the Administration Regulations (Paragraph 1(d) or 1(e) of Part 3 of Schedule 2 of the 2013 Regulations), where the Administering Authority does not judge the relevant Scheme Employer to be of sufficiently strong covenant, and other Admission Bodies with no Guarantor or where the Administering Authority does not judge the Guarantor to be of sufficiently strong covenant, the Administering Authority must be involved in the assessment of the required level of bond to protect the Fund. The admission will only be able to proceed once the Administering Authority has agreed the level of bond cover. The Administering Authority will supply some standard calculations provided by the Fund Actuary to aid the relevant Scheme Employer form a view on what level of bond would be satisfactory. The Administering Authority will also on request supply this to the Admission Body or Guarantor. This should not be construed as advice to the Scheme Employer, Guarantor or Admission Body.**

- **The Administering Authority notes that levels of required bond cover can fluctuate and it will review, or it recommends that the relevant Scheme Employer reviews the required cover, at least once a year.**

Subsumed liabilities

Where an employer is ceasing participation in the Fund such that it will no longer have any contributing members, it is possible that another employer in the Fund (the 'accepting employer') has agreed to provide a source of future funding in respect of any emerging deficiencies in respect of those liabilities.

In such circumstances the liabilities are known as subsumed liabilities (in that responsibility for them is subsumed by the accepting employer). For such liabilities the Administering Authority will assume that the investments held in respect of those liabilities will be the same as those held for the rest of the liabilities of the accepting employer. Generally this will mean assuming continued investment in more risky investments than Government bonds.

Orphan liabilities

Where an employer is ceasing participation in the Fund such that it will no longer have any contributing members, unless any residual liabilities are to become subsumed liabilities, the Administering Authority may act on the basis that it will have no further access for funding from that employer once any cessation valuation, carried out in accordance with Regulation 38 of the Administration Regulations (Regulation 64 of the 2013 Regulations), has been completed and any sums due have been paid. Residual liabilities of employers from whom no further funding can be obtained are known as orphan liabilities.

The Administering Authority will seek to minimise the risk to other employers in the Fund that any deficiency arising on the orphan liabilities creates a cost for those other employers to make good such deficiency. To give effect to this, the Administering Authority may seek funding from the outgoing employer sufficient to enable it to match the liabilities with low risk investments, generally Government fixed interest and index linked bonds.

However, if these liabilities are deemed to be small compared to the liabilities of the whole Fund (and therefore the risk related to these liabilities is small) then the Administering Authority may decide to use the Funding Target used for Scheduled Bodies for practical reasons.

Any excess or deficient returns on the notional or actual assets attributable to these liabilities relative to the Funding Target will be added to or deducted from the investment return to be attributed to the notional assets of all employers in the Fund.

Cessation valuations

Where an employer ceases participation, a cessation valuation will be carried out in accordance with Regulation 38 of the Administration Regulations (Regulation 64 of the 2013 Regulations). That valuation will take account of any activity as a consequence of cessation of participation regarding any existing contributing members (for example any bulk transfer payments due) and the status of any liabilities that will remain in the Fund.

In particular, the cessation valuation may distinguish between residual liabilities which will become orphan liabilities, and liabilities which will be subsumed (see above) by other employers.

For subsumed liabilities the cessation valuation will anticipate continued investment in assets similar to those held in respect of the subsuming employer's liabilities.

For orphan liabilities the Funding Target in the cessation valuation will anticipate investment in low risk investments such as Government bonds or be calculated in the same way as subsumed liabilities as considered appropriate.

For the avoidance of doubt, if an academy were to cease participation in the Fund, in the absence of another employer of sound covenant taking responsibility for future funding of residual liabilities, the resulting cessation valuation would be carried out on a Funding Target consistent with orphan liabilities as detailed above.

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

The Administering Authority's policy is that in the normal course of events any deficiency that exists at the cessation of the participation of an employer, will be payable immediately as a single payment. In extreme cases the Administering Authority may be prepared to agree payment over a period of years. However this period is very unlikely to exceed five years and any decision will be at the Administering Authority's discretion.

6. IDENTIFICATION OF RISKS AND COUNTER MEASURES

The Administering Authority's overall policy on risk is to identify all risks to the Fund and to consider the position both in aggregate and at an individual risk level. The Administering Authority will monitor the risks to the Fund, and will take appropriate action to limit the impact of these both before and after they emerge, wherever possible. The main risks to the Fund are:

Liability

The main risks include interest rates, pay and price inflation, changing retirement patterns and other demographic risks. The Administering Authority will ensure that the Fund Actuary investigates these matters at each valuation or, if appropriate, more frequently, and reports on developments. The Administering Authority will agree with the Fund Actuary any changes which are necessary to the assumptions underlying the measure of solvency to allow for observed or anticipated changes.

If significant liability changes become apparent between valuations, the Administering Authority will notify all participating employers of the anticipated impact on costs that will emerge at the next valuation and consider whether to require the review of bonds that are in place for Admission Bodies.

Regulatory and compliance

These risks relate to changes to general and LGPS regulations, national pension requirements or HM Revenue & Customs rules. The LGPS is also going through a major structural change. The Administering Authority will prepare for LGPS 2014 and will keep abreast of all proposed changes and, where possible, express its opinion during consultation periods after careful consideration. The Administering Authority's policy will be to ask the Fund Actuary to assess the impact on costs of any changes and, where these are likely to be significant, the Administering Authority will notify employers of this likely impact and the timing of any change.

Liquidity and maturity

The LGPS is going through a series of changes, each of which will impact upon the maturity profile of the LGPS and have potential cash flow implications. The increased emphasis on outsourcing and other alternative models for service delivery may result in the following:

- **active members leaving the LGPS;**
- **transfers of responsibilities between different public sector bodies;**
- **scheme changes which might lead to increased opt-outs; and/or**
- **spending cuts and their implications.**

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

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

Governance

This covers the risk of unexpected structural changes in the Fund membership (for example the closure of an employer to new entrants or the large scale withdrawal or retirement of groups of staff), and the related risk of the Administering Authority not being made aware of such changes in a timely manner.

The Administering Authority's policy is to require regular communication between itself and employers, and to ensure regular reviews of such items as bond arrangements, financial standing of non-tax raising employers and funding levels.

Particular examples are set out below:

Early retirement strain payments

No allowance is made in the triennial valuation and consequent employer rates for the additional value of the benefits when a member is made redundant or leaves on the grounds of efficiency.

To counter the potential increase in Funding Target emerging at the next valuation, a payment is calculated (using methods and assumptions agreed with the Fund Actuary) and made by the Scheme Employer to the Fund to meet this additional cost at the date the member is made redundant or leaves on the grounds of efficiency.

Body ceasing to exist with unpaid deficiency

Some employers can cease to exist and/or become insolvent leaving the employers in the Fund open to the risk of an unpaid deficiency. Any such deficiency will be met by the relevant Scheme Employer with regard to a Transferee Admission Body and there is therefore no risk to other employers in the Fund (provided of course that the relevant Scheme Employer is itself of good covenant). Any unpaid deficiency in relation to other employers falls on other employers in the Fund and the Administering Authority will ensure that risks are reduced by use of bond arrangements or ensuring there is a Guarantor to back the liabilities of the body.

Employers with a small and declining number of contributing members

A recent legal judgement indicates that under the current LGPS regulations employers with no contributing members cannot be charged contributions under Regulation 36 of the Administration Regulations (Regulation 62 of the 2013 Regulations). This ruling, however, does not affect the ability to collect contributions following a cessation valuation for Admission Bodies under Regulation 38 of the Administration Regulations (Regulation 64 of the 2013 Regulations). The regulations may alter in the future but there is a risk of a body ceasing to pay contributions with a deficiency in the Fund.

The Administering Authority will monitor Scheme Employers with declining membership to ensure that funding is close to 100% by the time the last member leaves service and may alter the funding strategy accordingly. It will also ensure that a cessation valuation is carried out for employers once it is clear there will be no contributing members relating to that employer in the future.

Investment

This covers items such as the performance of financial markets and the Fund's investment managers, asset reallocation in volatile markets, leading to the risk of investments not performing (income) or increasing in value (growth) as forecast.

Examples of specific risks are:

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

The specific risks associated with assets and asset classes are:

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

The Administering Authority reviews each investment manager's performance quarterly and at least annually considers the asset allocation of the Fund by carrying out a review with its Investment Adviser. The Administering Authority also annually reviews the effect of market movements on the Fund's overall funding position.

Employer

These risks arise from the ever-changing mix of employers, from short-term and ceasing employers, and the potential for a shortfall in payments and/or orphaned liabilities.

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

The Administering Authority maintains a knowledge base on its employers, their basis of participation and their legal status (e.g., charities, companies limited by guarantee, group/subsidiary arrangements) and uses this information to inform the choice of Funding Strategy for each employer.

Choice of Solvency and Funding Targets

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

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

The Administering Authority will not adopt assumptions for bodies regarded by the Administering Authority as being of sound covenant which, in its judgement, and on the basis of actuarial advice received, are such that it is less than 55% likely that the strategy will deliver funding success. Where the probability of funding success is less than 65% the Administering Authority will not adopt assumptions which lead to a reduction in the aggregate employer contribution rate to the Fund.

Smoothing

The Administering Authority recognises that utilisation of a smoothing adjustment in the solvency measurement introduces an element of risk, in that the smoothing adjustment may not provide a true measure of the underlying position. If such an adjustment is used, the Administering Authority's policy is to review the impact of any adjustment made at each valuation to ensure that it does not alter the disclosed solvency level by more than 5%.

Recovery period

The Administering Authority recognises that permitting surpluses or deficiencies to be eliminated over a Recovery Period rather than immediately introduces a risk that action to restore solvency is insufficient between successive measurements. The Administering Authority's policy with regard to Recovery Periods is set out in section 4 of this Statement.

Statement of Policy Concerning Communication

Introduction

This is the Statement of Policy Concerning Communication of the Northumberland County Council Pension Fund ("the Fund"), which is administered by Northumberland County Council, the administering authority.

The Local Government Pension Scheme (Administration) Regulations 2008 require all Local Government Pension Scheme funds in England and Wales to publish a statement of policy concerning communication with members and employing authorities.

Communication with all Scheme members, i.e. pensioner members, deferred pensioner members and active members

The County Council automatically provides a range of Scheme booklets to employees eligible to join the Local Government Pension Scheme upon joining the employment of the County Council, and provides the booklets to participating employers to give to their new employees.

Booklets are also provided upon request, and distributed at information points within County Hall.

All Scheme booklets are available on the Northumberland County Council website, together with links to other useful websites.

Pension Section staff are available to give and receive advice and information by telephone, letter, email, and in person within County Hall. Appointments are not necessary, but private interview facilities can be made available if required.

Communication with pensioner members

The County Council sends annual newsletters to pensioner members by post. The annual newsletter is also available via the website.

At the time of retirement specific information is made available to each individual pensioner, this includes:

- **A statement detailing the calculation of his/her pension and lump sum.**
- **A letter explaining the arrangements for paying his/her pension.**
- **A leaflet explaining his/her appeal rights.**
- **A leaflet explaining the provisions of the Pension Increase legislation.**
- **A leaflet explaining the abatement provisions should he/she become re-employed.**

All retiring members are asked to complete a questionnaire giving their views on the quality and range of services provided by the Pension Section.

Communication with deferred pensioner members

The County Council sends annual benefit statements by post to deferred pensioner members and through them Scheme members are kept informed of future pension benefit entitlement.

At the time of leaving employment specific information is made available to each individual deferred beneficiary, this includes:

- **A statement detailing the calculation of his/her pension and lump sum entitlement and information regarding when the benefits are due for payment together with any early release provisions**
- **A leaflet explaining his/her appeal rights.**
- **A booklet setting out his/her options with regard to LGPS rights, e.g. effecting transfer to a new employer's pension scheme, etc.**

Communication with active members

On appointment, an eligible employee is provided with scheme literature and a form which enables him/her to request further information regarding the transfer of earlier pension rights into the LGPS and/or effecting a death benefit or partner's pension nomination. Subsequently the scheme member will be provided with a notice confirming his/her admission to the Scheme and detailing his/her rights to count previous service if appropriate. Further notices will be issued to the scheme member upon material changes to his/her circumstances which affect his/her right to reckon scheme membership (e.g. moving from full-time to part-time employment).

Active members are also provided with information concerning their appeal rights.

The County Council sends annual benefit statements by post to active members, and an (at least) annual newsletter by post updating members on any relevant changes. The newsletters are also available via the website

The Pension Section of the County Council holds annual meetings (road shows) for the contributors in at least three locations throughout the County, to explain Scheme benefits and offer an opportunity to deal with individuals' questions. Information regarding AVC's and other methods of making additional pension contributions are discussed at these events.

The Pension Section is located in the Northumberland County Council main office (County Hall) and active members have access to advice and information from staff upon request.

Ad hoc meetings and presentations are organised to discuss specific pension issues with groups of employees e.g. those transferring to a new employer under TUPE transfers

All new entrants to the Scheme are asked to complete a questionnaire giving their views on the quality and range of services provided by the Pension Section.

Communication with representatives of members

Two Trade Union representatives have seats on the Northumberland County Council Pension Fund Panel, in the capacity as observers. The seats on the Panel entitle those representatives to all of the Reports, policy documents, presentations and some of the training made available to the voting members of the Panel.

Communication with prospective members

The County Council automatically provides Scheme booklets to all new employees who are eligible to join the Local Government Pension Scheme at the start of their employment with the County Council, and provides the booklets to participating employers to give to their new employees.

The Pension Section of the County Council holds annual meetings (road shows) in at least three locations throughout the County and invites prospective members to attend, to explain Scheme benefits and offer an opportunity to deal with individuals' questions.

Communication with employing authorities

Following the amalgamation of the district and borough councils in Northumberland with Northumberland County Council which took place with effect from 1 April 2009, one non-voting seat on the Northumberland County Council Pension Fund Panel was allocated to an employer representative and one to an employee/pensioner representative. The purpose of the employer representative seat is to give representation on the Panel to all of the other employers (i.e. other than Northumberland County Council) participating in the Fund. Prior to 1 April 2009 three out of the six Northumberland district/borough councils had seats on the Panel, with full voting rights.

The County Council holds an annual meeting with the employers in December or January each year, at which all aspects of the Fund's investments and actuarial position are discussed, together with any Scheme changes. The results of any actuarial valuation and relevant topics are covered when appropriate.

The County Council provides each participating employer with a detailed and prescriptive Scheme Guide and relevant updates, which sets out the responsibilities and information requirements of the employers. An employer section of the Northumberland County Council website has been established and updates for employers are made available via this site.

Employers are sent a hard copy of the Fund's Annual Report and Accounts each year.

Employers were consulted on the initial Statement of Investment Principles (SIP) for the Northumberland County Council Pension Fund, and are sent an annual updated copy as part of the Annual Report and Accounts.

Employers are sent a copy of and consulted each year upon the Fund's annual Business Plan.

Employers are consulted on other ad hoc policy statements, such as the Fund's Governance Policy, as the need arises.

Employers were consulted on the first Funding Strategy Statement (FSS) for the Fund.

Training on pension matters is offered to human resources and payroll personnel within the County Council.

Periodically participating employers are asked to complete a questionnaire giving their views on the quality and range of services provided by the Pension Section.

The SIP, the FSS, the Report and Accounts are all available via the website.

Governance Compliance Statement

Approved at the Pension Fund Panel meeting on 20 November 2009

Compliance Standard	Arrangements in Place/Action Taken	Action Complies with Principle? Yes/No/Partial	Reason for non-Compliance (if applicable)
Structure			
The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing council.	The terms of reference for the Pension Fund Panel, as set out in the Northumberland County Council Constitution, include all matters relating to the investment of the Pension Fund and all administering authority matters appertaining to the Fund as a whole.	Yes	
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.	The Pension Fund Panel comprises of six Northumberland County Councillors. Participating employers are also represented on the Pension Fund Panel by one representative who has observer status. Scheme members (i.e. contributors and pensioners) are represented by two trade union representatives and one employee/pensioner representative, all three of whom have observer status on the Pension Fund Panel.	Yes	
That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	There is no secondary committee or panel.	N/A	
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.	There is no secondary committee or panel.	N/A	

Compliance Standard	Arrangements in Place/Action Taken	Action Complies with Principle? Yes/No/Partial	Reason for non-Compliance (if applicable)
Representation			
That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include :-			
i) employing authorities (including non-scheme employers, e.g. admitted bodies);	Employing authorities are represented by the six Pension Fund Panel members. The six members are all councillors of Northumberland County Council, a unitary council which represents around 90% of the contributors to the Northumberland County Council Pension Fund. Other participating employers are represented by one non-voting employer representative. Other employers are also represented by the Pension Fund Panel members, some of whom have representative links with several of the other participating employers.	Yes	
ii) scheme members (including deferred and pensioner scheme members);	Scheme members are represented by two non-voting trade union observers. Employees and pensioners are also represented by one non-voting employee/pensioner representative.	Yes	
iii) independent professional observers; and	There are no independent professional observers on the Pension Fund Panel.	No	An independent professional observer has not been considered necessary in the past. There is a cost associated with having an independent professional observer on the Panel and it is not clear that any benefits would outweigh the cost. The role of independent observer is more relevant in the private sector where conflicts of interest are more likely than in the LGPS.

Compliance Standard	Arrangements in Place/Action Taken	Action Complies with Principle? Yes/No/Partial	Reason for non-Compliance (if applicable)
Representation			
iv) expert advisors (on an ad-hoc basis).	The Pension Fund Panel investment adviser attends all meetings.	Yes	
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.	All Panel members and observers are treated equally in terms of access to papers and training.	Yes	
Selection and Role of Lay Members			
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.	New Panel members are offered induction training and copies of key documents, such as the Statement of Investment Principles, as well as a Pension Fund Panel handbook which explains the role of the member on the Panel.	Yes	
Voting			
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.	The six Pension Fund Panel members have voting rights; the two trade union representatives, the one employer representative and the one employee/pensioner representative have observer status only, though they participate in the decision making. Voting rights have not been extended to the trade union and employee/pensioner representative observers on the Panel because they represent Scheme members whose pension rights are guaranteed in law and are not dependent on Fund performance and therefore bear none of the investment risk. Voting rights have not been extended to the employer representative who has observer status on the Panel because doing so would merely duplicate the representation provided by the Panel members themselves.	Yes	

Compliance Standard	Arrangements in Place/Action Taken	Action Complies with Principle? Yes/No/Partial	Reason for non-Compliance (if applicable)
Training/Facility Time/Expenses			
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.	All new members of the Pension Fund Panel are offered induction training by an officer. All Panel members are offered the Employers' Organisation three-day training as well as other training courses, conferences and meetings. All Panel members receive training provided by fund managers' presentations and by the Panel adviser as part of the Panel meetings. Expenses are reimbursed in accordance with the County Council's expenses scheme.	Yes	
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.	The policy applies equally to all members of the Pension Fund Panel. There is no secondary committee or panel.	Yes	
Meetings (frequency/quorum)			
That an administering authority's main committee or committees meet at least quarterly.	The Pension Fund Panel meets at least quarterly.	Yes	
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.	There is no secondary committee or panel.	N/A	
That administering authorities who do not include lay members in their formal governance arrangements, provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	Trade union observers and the employee/pensioner representative on the Pension Fund Panel represent lay members.	N/A	

Compliance Standard	Arrangements in Place/Action Taken	Action Complies with Principle? Yes/No/Partial	Reason for non-Compliance (if applicable)
Access			
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.	All Panel members and observers are treated equally in terms of access to papers and advice.	Yes	
Scope			
That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	The terms of reference for the Pension Fund Panel, includes all administering authority matters appertaining to the Fund as a whole, and therefore the Panel considers 'wider issues' and not just investments. The one exception to this principle is that the Northumberland County Council Constitution provides that its Staff Committee should, where necessary, exercise administering authority discretion over the payment of death grants. At its meeting held on 16 November 2007, the Pension Fund Panel gave consideration to bringing the responsibility for death grant discretion within the remit of the Panel, but resolved to leave it with the Staff Committee, where the practical arrangements were working well.	Yes	

Compliance Standard	Arrangements in Place/Action Taken	Action Complies with Principle? Yes/No/Partial	Reason for non-Compliance (if applicable)
Publicity			
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.	The first Northumberland County Council Pension Fund Governance Policy Statement, published in March 2006, was distributed to all employers and all relevant trade unions, and comments were invited. The first Governance Compliance Statement, published in February 2008 was similarly consulted upon. Each revision of the Governance Compliance Statement will be consulted upon. The Governance Policy Statement and Governance Compliance Statement are published on the Northumberland County Council website. The Governance Policy Compliance Statement is reproduced in full within the Northumberland County Council Pension Fund Annual Report, a copy of which is distributed to all participating employers with active Scheme members.	Yes	

Pension Fund Panel Training

The Pension Fund Panel recognises the importance of ensuring that the members charged with the financial management and decision-making with regard to the pension scheme are fully equipped with the knowledge and skills to discharge the duties and responsibilities allocated to them.

Most members of the Panel have attended at least part of the series of three training days organised by the Employers' Organisation for Local Government (Local Government Pensions Committee), which are specifically targeted at elected members with responsibility for the investment of local authority pension funds. All new and existing Panel members are actively encouraged to attend.

All new members of the Panel receive/are offered an induction seminar given by an officer.

Members are offered the opportunity to attend relevant courses and conferences as they arise, particularly those organised by the LGC, NAPF and the Northern Pensions Conference. Members are invited to attend the annual meeting for employers which includes a presentation by the Fund's actuary.

Members receive briefings from fund managers each quarter on the managers' processes and topics of interest such as risk and control.

Members receive training and advice, both verbal and written, from the Pension Fund Panel adviser and officers at Panel meetings and as part of the Pension Fund Panel papers distributed in advance of the meetings.

Members acknowledge that there is a cost associated with training.

Assessment of the Effectiveness of the Pension Fund Panel Decisions made in 2013/2014

Overall assessment

The Panel faced a major challenge as a result of membership changes following the May 2013 Northumberland County Council elections when five out of the six voting Panel members were replaced. This membership change has been very well managed, and the Panel has continued to implement decisions through the year. New members have shown commitment to training, continuity has been achieved in other aspects of the operation of the Panel such as the advisers to the Fund, and the former Pension Manager's attendance at meetings has been maintained.

The Panel would particularly draw attention to the following achievements in the year:

- **it has implemented changes within the active bond portfolio to protect capital value in the event of future increases in gilt yields; and**
- **it has taken the opportunity to significantly reduce the risk level implicit in the 31 March 2013 actuarial valuation of the Fund compared with the risk in the 31 March 2010 valuation; and**
- **it has been instrumental in changing DfE's stance on giving a guarantee to LGPS funds relating to outstanding LGPS liabilities on academy closure.**

Governance arrangements in 2013/2014

Administrative arrangements

The Panel met five times in the 2013/2014 Council year:

- **four meetings for the normal quarterly business including the review of investments and monitoring the appointed fund managers; and**
- **one further ad hoc meeting to deal with the selection of a private equity investment and restructuring of the actively managed bond portfolio.**

The Panel also attended a Fund-specific training event to receive information from the Fund actuary relating to the actuarial valuation of the Fund as at 31 March 2013.

The number of meetings held has been appropriate to allow sufficient time to consider all agenda items and ensure sufficient training and experience have been gained by the members before making the decisions required.

The length of the meetings (i.e. usually a full day) has been appropriate to enable members to consider complex subject matter, and time has been allowed in the meetings for effective challenge of the external fund managers and other advisers.

The Panel has allocated sufficient time at each meeting to consider each decision fully and to understand the inherent risks involved in pension fund investment and the Local Government Pension Scheme.

The Panel has organised additional meetings where necessary to further consider an issue when focus on a single issue is required. For example, to ensure that members could give their full attention, the Panel allocated one day to the training event held in September 2013 at which the Fund actuary presented information about the 2013 valuation.

The Panel has delegated authority to the Lead Executive Director Corporate Resources, in consultation with the Chairman and Vice-Chairman, when necessary, to ensure that matters could be progressed on a timely basis without the need to revert to the committee.

The minutes of meetings and reports presented to the Panel were of adequate detail for members to ensure that officers had acted on and implemented the decisions taken.

The papers for the meetings were circulated well in advance to allow adequate time for Panel members to read and consider the issues. The papers were prepared to an adequate standard and included a short summary of each agenda item to aid the reader in understanding the key points. Urgent items, to be tabled at meetings, have been kept to a minimum.

The papers have been presented at the meetings by officers and advisers with sufficient technical knowledge, experience and skill to assist members in understanding the key areas.

The meetings have been conducted in a format which has allowed for decisions to be reached promptly but after appropriate consideration. Suitably qualified officers and advisers have been in attendance at all meetings and have been allowed the opportunity to provide advice during meetings to ensure that decisions made comply with the regulations and best practice.

The Chairman has conducted the meetings to ensure that all members have been encouraged to express their views. All Panel members have contributed to effective and efficient meetings.

In prior years, Panel members have implemented improvements to the arrangements for the meetings including:

- **providing an opportunity immediately after receiving a presentation from a fund manager to capture members' views so that a synopsis of those views can be brought back to future meetings as an aide-memoir; and**
- **changing the practice regarding despatch of information received from the fund managers to reduce the volume of papers sent to members for the quarterly meetings.**

Panel members have ensured that the views of the observer status participants have been fully considered.

In prior years, the Panel has considered and approved a programme of future meetings for the investment managers who will be requested to attend meetings. The programme takes a risk based approach to allocating time for the Panel to interview and question the managers, and allows for flexibility so managers can be requested to attend more frequently should the Panel deem it appropriate. The programme of meetings allows sufficient time for the Panel to understand the fund managers' philosophy and processes and time for effective challenge. The Panel has been pro-active in determining the frequency of the fund managers' attendances at the meetings.

The Panel monitors the cost of transitions of assets from one fund manager to another.

Meetings have been conducted following the protocols as set out in the Northumberland County Council Constitution.

Access to advice

The Panel recognises the importance of understanding its responsibilities to the employers participating in the Fund and, in particular, the need to understand and manage investment (asset allocation) risk. The Panel has had access to appropriate advice and has obtained advice in the year from suitably qualified specialists including:

- **investment advice from Mercer;**
- **actuarial advice from Aon Hewitt;**
- **legal advice on contracts entered into from Sacker.**

Senior officers of the Council, such as the Lead Executive Director Corporate Resources and Head of Legal Services, have attended Panel meetings when necessary.

The Panel has an assessment process to formally measure the performance of the investment adviser on an annual basis.

External audit

The Panel had the opportunity to question and engage with the external auditor (Deloitte) to discuss the accounting and administration arrangements for the Pension Fund and the Scheme. This provided an independent check on the work of the officers and the Pension Team.

Performance measurement adviser

The Panel had the opportunity to question and engage with the independent performance measurement adviser (WM Company) to discuss the performance of the external investment managers. This provided an independent check on the investment managers, the information provided in the Panel papers, and, to some extent, the advice provided by the investment adviser (Mercer).

Continuity

Pension Fund investment is long term in nature and expertise takes time to build up. Continuity is vitally important for effective decision making, with some decisions, such as the decisions about asset allocation, being made over the course of several meetings. During 2013/2014 the Panel has had continuity in the three most important areas for its effectiveness as a decision-making body, namely:

- **its own membership;**
- **its investment adviser; and**
- **the officers who support the work of the Panel.**

Training

The Panel recognises that pension fund investment is a technical area and the importance of spending time on training. The Panel has received adequate training for the decisions taken in the year, for example, for selecting the new private equity fund investment, where the Panel was supported by Mercer's advice and research information throughout the process. New Panel members in particular have devoted time to attend relevant and tailored training events.

Communication with stakeholders

The Panel has promoted effective communication with the stakeholders of the Scheme and Fund, such as road-shows and newsletters for the contributors (employees). Panel members have attended the annual employers' meetings which have provided them with valuable feedback.

Statement of Investment Principles (SIP)

The Panel has considered and approved the Fund's SIP during 2013/2014.

Key decisions, including investment decisions, made in 2013/2014

The Panel has taken advice from Mercer on all investment decisions made and obtained Mercer's research information and ratings each quarter for all of the Fund's external investment managers.

Asset allocation decisions

The investment adviser, Mercer, carried out a review of the active bond portfolio with the Panel in 2013/2014. The Panel implemented a change to the active bond portfolio managed by Wellington with the intention of providing protection for the portfolio value in the event of future increases in gilt yields.

Setting the risk level in the 31 March 2013 actuarial valuation

The Panel considered information presented by the Fund actuary at the initial results stage of the NCC Pension Fund 2013 actuarial valuation. The actuary obtained the Panel's input in setting the discount rate used in the valuation. The discount rate determines the risk inherent in the valuation. A discount rate of 5.3% and a 22 year deficit recovery were set for the main employers in the Fund and this implied a probability of funding success of (approximately) **75%** within the 2013 valuation, a significant improvement on the (approximately) **70%** probability of funding success inherent within the 2010 valuation.

Funding strategy

When setting the funding strategy for the Fund with effect from 1 April 2014, the Panel took account of the most up to date information about covenant risk posed to the Fund by the participating employers, with the aim of protecting the Fund (and ultimately the council tax payer) against potential default risk.

During 2013/2014, the current Panel continued the work of the previous Panel to ensure that the funding strategy adopted by the Fund remained appropriate and proportionate to address the covenant risk imposed by academies in the LGPS. Following the Government's implementation of the Academies Act 2010, Northumberland County Council, among others, communicated on many occasions with DfE about the covenant risk posed by academies on LGPS funds and sought a DfE guarantee. This culminated, in July 2013, in DfE setting out details of a guarantee relating to outstanding LGPS liabilities on academy closure. The DfE guarantee was seen by the Panel, and others, as a very welcome step forward. After July 2013 the Panel continued to work with DfE to address the scope of the guarantee. This work enabled the Fund to change its strategy for academies and move them from the orphan to the subsumption funding target (for on-going contributions only) when the 31 March 2013 actuarial valuation was finalised in 2014.

Administration

The Fund's accounts are the responsibility of:

- **Steven Mason**
  Lead Executive Director Corporate Resources

Assisted by:

- **Alison Elsdon**
  Head of Corporate Services

and

- **Colin Logan**
  Head of Financial and Customers Services

Staff members within the Pension Team of the Corporate Resources Directorate are responsible for administering the Scheme, including the calculation and administration of benefit payments and transfer values, as well as recording employee and employer contributions and the maintenance of employees' pension records, and pensioners' and deferred pensioners' records.

Staff members within the Business Support (Corporate Services) Team of the Corporate Resources Directorate maintain the Fund's accounts and investment records, prepare quarterly reports to the Pension Fund Panel, produce the Annual Report and Accounts and act as a point of contact with the Fund's investment managers, advisers and auditors.

External audit

The Northumberland County Council Pension Fund financial statements are audited by:

- **Deloitte LLP**
  One Trinity Gardens
  Broad Chare
  Newcastle upon Tyne
  NE1 2HF

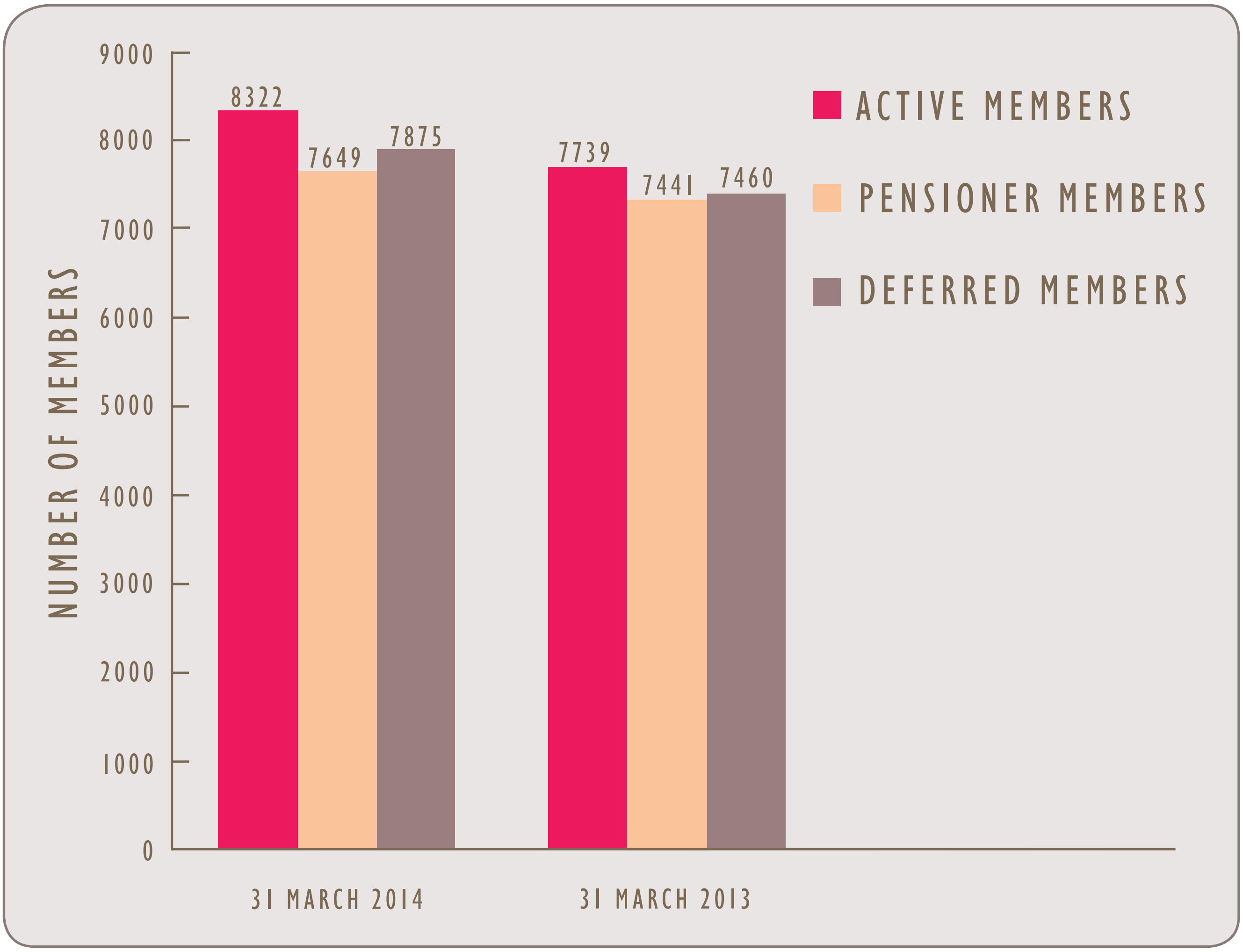
Scheme Members

The Fund's members are current employees and councillors (active members), retired employees and councillors (pensioner members) and deferred pensioner members of the County Council and a number of other scheduled and admitted bodies. As at 31 March 2014, the Fund had 8,322 active members and 7,649 pensioner members.

Firefighters and teachers have separate pension arrangements and do not therefore participate in the Fund.

The following graph is an analysis of the Fund members as at 31 March 2014.

Fund members as at 31 March 2014



Further details of the membership are given in Appendix 1.

Fund Performance

Annual returns

Over the year, the Northumberland County Council Pension Fund outperformed its benchmark by 0.4%* (expressed on a geometric basis).

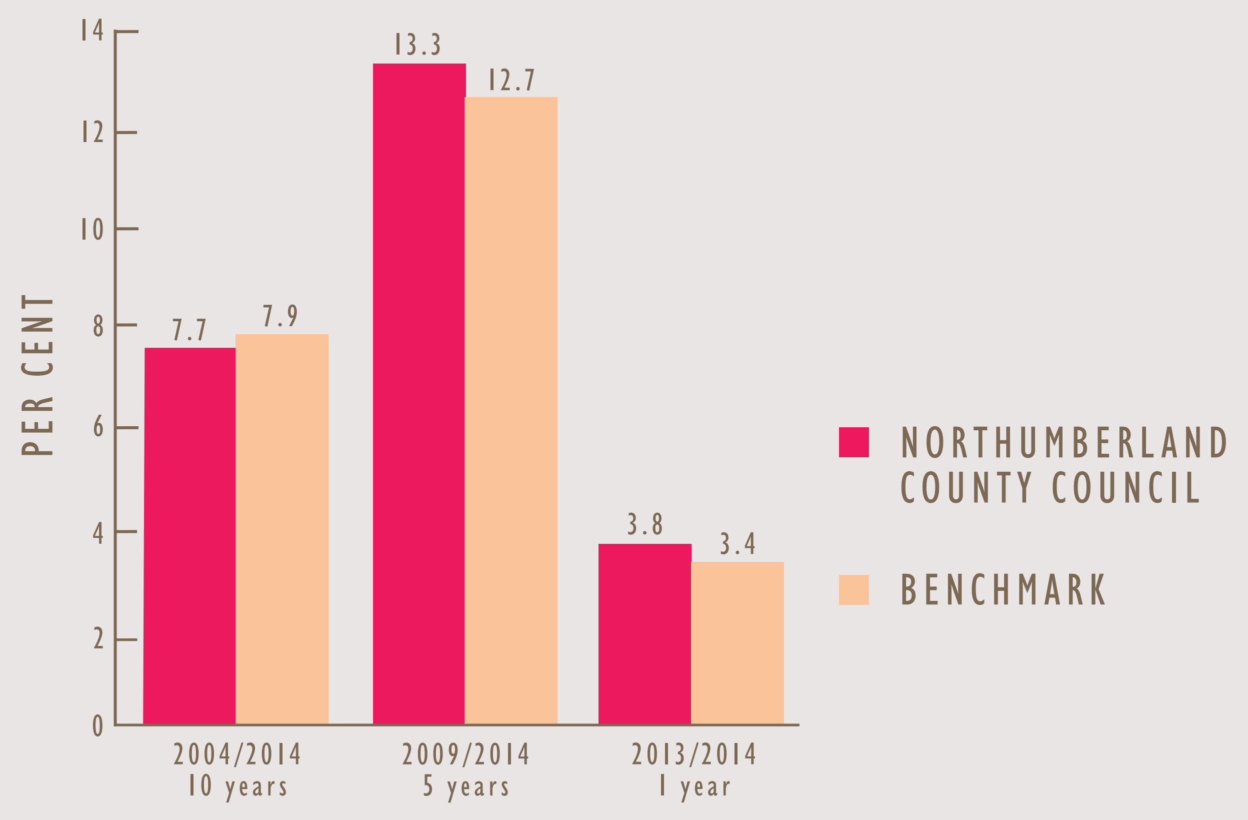
YEAR ENDING 31 MARCH	2010	2011	2012	2013	2014
Fund performance	40.8%	6.4%	5.3%	14.0%	3.8%
Benchmark	36.7%	7.6%	4.8%	14.2%	3.4%

* Relative performance is shown as the geometric difference between the Fund return and its benchmark, rather than the arithmetic difference. This is in line with industry standard and to allow for accurate linking of relative returns over time.

Annualised returns

The following shows the Northumberland County Council Pension Fund's longer-term returns compared with the Fund specific benchmark.

Comparison of annualised returns



Analysis of returns

Returns for year ended 31 March 2014

Manager (investment category)	Fund %	Benchmark %
Legal & General (index tracker)	3.5	4.1
M&G (global equities)	7.2	6.7
Wellington (bonds)	-1.5	0.8
BlackRock (property)	12.4	11.9
Schroder (property)	14.8	11.9
Combined Fund	3.8	3.4

Market commentary

The average local authority LGPS pension fund returned 6% in 2013/2014.

Equity markets continued to perform strongly in the year with most developed markets producing returns in the high teens in local currency, however much of this return was eroded for UK investors in the US and Japan by the strength of Sterling which gained 9% against the US Dollar and 17% against the Yen over the year.

UK equities were below the overseas average but still returned 11% for the year. Active managers continued to add value relative to the FTSE All-Share index, the fourth consecutive year that this has now occurred.

UK bonds posted only their third year of negative results in the last twenty, giving up some of the extremely strong results of the recent past. Index-linked gilts likewise, produced a small negative for the year.

The performance of alternative investments was disappointing. Private equity returned 5% whilst hedge funds averaged only 4%.

Pooled multi-asset (diversified growth) investments returned only 3% for the year.

Property returned 11% for the year, whilst an excellent result in absolute terms this was below the IPD index.

The Fund's returns

The Northumberland County Council Pension Fund produced a return of 3.8% in 2013/2014 which was well above the growth in average earnings of 1.5% for the same period.

The Fund return of 3.8% was above its benchmark. Asset allocation detracted 0.1% from performance, while stock selection added 0.5% over the period.

Manager performance was mixed. Schroder, BlackRock and M&G beat their respective benchmarks, but this was partly offset by Legal & General and Wellington underperforming their benchmarks.

The WM Local Authority Pension Fund Universe for 2013/2014 produced an average return of 6.4% in the period. The range of returns was 10.1% for the 5th ranked to 3.5% for the 95th ranked fund. Northumberland County Council Pension Fund ranked 91st in 2013/2014 (50th in 2012/2013).

Over five years the Fund returned 13.3% p.a. which was above the benchmark return of 12.7% p.a. giving a relative outperformance of 0.5% p.a. and ranking 35th in the Local Authority Universe.

Over ten years the Fund achieved a return of 7.7% (annualised). This compares well with the RPI return of 3.3% p.a. and the average earnings index return of 3.1% p.a., and ranks 50th in the Local Authority Universe but is below the fund's benchmark return of 7.9% p.a. for the same period.

Independent Auditor's Report to the Members of Northumberland County Council in respect of Northumberland County Council Pension Fund

We have examined the pension fund financial statements for the year ended 31 March 2014, which comprise the Fund Account, the Net Assets Statement and the related notes 1 to 23.

This report is made solely to the members of Northumberland County Council, as a body, in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by the Audit Commission. Our audit work has been undertaken so that we might state to the Authority those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Lead Executive Director Corporate Resources and the auditor

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

Our responsibility is to report to you our opinion on the consistency of the pension fund financial statements within the pension fund annual report with the pension fund financial statements in the statement of accounts of Northumberland County Council, and its compliance with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2013/14.

We also read the other information contained in the pension fund annual report as described in the contents section and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the pension fund financial statements.

We conducted our work in accordance with the guidance issued by the Audit Commission. Our report on the administering authority's full annual statement of accounts describes the basis of our opinion on those financial statements.

Opinion

In our opinion, the pension fund financial statements are consistent with the full annual statement of accounts of Northumberland County Council for the year ended 31 March 2014 and comply with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2013/14.

Paul Thomson
For and on behalf of Deloitte LLP
Appointed Auditor
Newcastle

30 September 2014

Fund Account

For the year ended 31 March 2014

2012/2013 £'000		Note	2013/2014 £'000
Contributions and benefits			
442,955	Contributions	5	42,153
3,631	Transfers in from other pension funds	6	1,452
46,586			43,605
(42,862)	Benefits	7	(45,976)
(1,982)	Payments to and on account of leavers	8	(1,870)
(983)	Administrative expenses	9	(918)
(45,827)			(48,764)
759	Net additions/(withdrawals) from dealings with members		(5,159)
Returns on investments			
2,153	Investment income	10	2,257
111,182	Profit and losses on disposal of investments and changes in value of investments	11	34,713
(2,047)	Investment management expenses	12	(2,012)
111,288	Net returns on investments		34,958
112,047	Net increase in the net assets available for benefits during the year		29,799
802,375	Net assets of the Fund at 1 April 2013		914,422
914,422	At 31 March 2014		944,221

Steven P Mason

Steven Mason
Lead Executive Director Corporate Resources
30 September 2014

Net Assets Statement

As at 31 March 2013 £'000		Note	As at 31 March 2014 £'000
	UK investments		
	POOLED INVESTMENT VEHICLES		
38,546	- Property		41,510
317,934	- Equity		334,205
145,968	- Index linked		164,427
25	VENTURES AND PARTNERSHIPS		18
	Overseas investments		
	QUOTED		
91,694	- Other fixed interest		90,315
	POOLED INVESTMENT VEHICLES		
250,433	- Equity		254,442
67,675	VENTURES AND PARTNERSHIPS		64,846
912,275		11	949,763
725	Other investment balances	11	2,082
913,000		11	951,845
8,007	Cash deposits		2,215
1,351	Current assets	13	720
(7,936)	Current liabilities	14	(10,559)
914,422	Net assets of the Fund at 31 March 2014	15	944,221

The accounts summarise the transactions of the Fund and the net assets. They do not take account of obligations to pay pensions and benefits which fall due after the end of the Fund year. The actuarial position of the Fund, which does take account of such obligations, is dealt with in the Statement of the Actuary and the Whole of Pension Fund Disclosures under IAS26 (also prepared by the actuary) shown in Appendices 2 and 3 respectively of the Annual Report and these accounts should be read in conjunction with that.

Notes to the Financial Statements

1. Basis of preparation

The accounts have been prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and comply with the provisions of Chapter 2 of the Statement of Recommended Practice, Financial Reports of Pension Schemes (Revised May 2007), except if reference to the contrary is made.

2. Accounting policies

The accounts have been prepared on an accruals basis, except for transfers of benefits to and from other schemes which are accounted for on a receipts and payments basis, and except that the net asset statement does not include liabilities to pay pensions after the end of the Fund year.
The principal accounting policies are as follows:

Investments

Valuation of investments

Investments are shown at their market value which has been determined as follows:

1) Quoted securities are valued at the bid price quotations at close of business on 31 March 2014;

(2) Pooled investment vehicles are stated at the bid prices quoted by their respective managers on 31 March 2014;

(3) Other unlisted securities, including partnerships, are valued with regard to latest dealings and other appropriate financial information as provided by their respective managers or those controlling the partnerships;

(4) Overseas securities and cash are translated into sterling at the rate ruling at the net assets statement date.

Investment Income

Dividends and interest on stocks are credited to the Fund in the year in which they become ex-dividend. Interest receivable on loans and deposits is accounted for on an accruals basis. Foreign income has been translated into sterling at the date of the transactions, when received during the year, or at the exchange rates applicable at 31 March 2014 where amounts were still outstanding at the year end.

Investment gains and losses

Realised and unrealised gains and losses on investments arising in the year to 31 March 2014 are credited to the Fund.

Investment transactions

Investment transactions arising up to 31 March 2014 but not settled until later are accrued in the accounts.

Contributions

Contributions represent the total amounts receivable from the various employers participating in the Fund in respect of their own contributions and those of their pensionable employees. The employers' contributions are made at rates determined by the Fund's actuary.

Contributions due at 31 March 2014 are accrued in the accounts but no provision is made for employees' and employers' contributions relating to sums due on pay awards not yet settled.

Benefits and refunds

Benefits and refunds are accounted for in the year in which they become due for payment.

Transfer values

Transfer values are those sums paid to or received from other pension schemes for individuals and relate to periods of previous pensionable employment.

Transfer values received and transfer values paid are accounted for on a receipts and payments basis.

Administrative expenses

Direct and indirect staff costs for the pension team, together with apportioned costs for the use of Northumberland County Council's premises, systems and services are charged to the Fund.

Events after the reporting period

Events that occurred after 31 March 2014 which provide evidence of conditions that existed as at 31 March 2014 are included in the accounts. Events that are indicative of conditions that arose after 31 March 2014 are not included, except for events with material effect which are disclosed in the notes to the accounts.

Financial instruments

All of the Fund's assets and liabilities, as shown in the net asset statement, are classified as financial instruments, and the principal accounting policies applied in accounting for them are described elsewhere in this note.

Obligations to pay promised retirement benefits

The actuarial present value of promised retirement benefits is shown in a separate actuarial report accompanying the accounts, entitled "Whole of Pension Fund Disclosures under IAS26" and shown as Appendix 3 to the Annual Report. This treatment follows "Option C", as set out in IAS26 *Accounting and Reporting by Retirement Benefit Plans.*

3. Critical judgements in applying accounting policies

The most significant judgements in applying accounting policies are as follows:

Unquoted private equity and infrastructure investments

Private equity and infrastructure investments are valued based on forward looking estimates and judgements made by the general partners (i.e. those controlling the partnerships) to the funds invested in.

Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits, as disclosed in Appendix 3, is prepared by the Fund actuary adopting "Option C" of IAS26. Option C requires actuarial valuation of the liabilities on an IAS19 basis to be prepared at formal triennial valuations only, the most recent being as at 31 March 2013. The liability disclosed in Appendix 3 is subject to significant variances depending on the assumptions adopted.

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

The items in the Net Assets Statement as at 31 March 2014 and Appendix 3 involving assumptions about the future and major sources of estimation uncertainty for which there is a significant risk of material adjustment to the value disclosed within the next financial year are as follows:

	Uncertainties	Effect if actual results differ from assumptions
Unquoted private equity and infrastructure investments	There are no publicly listed prices for the Fund's investments in private equity and infrastructure and therefore there is a degree of estimation and judgement involved in the valuations used.	Total private equity and infrastructure investments disclosed in the accounts amount to £65 million. The Fund's performance measurement service provider, WM Company, estimates potential volatility consistent with a one standard deviation movement in the change in value of private equity as an asset class over the latest three years of 8.2%. This equates to a tolerance of +/- £5 million.
Actuarial present value of promised retirement benefits	Estimation of Fund deficit depends on a number of complex judgements relating to the discount rate used, and factors such as projected salary growth and inflation, commutation rates and mortality rates. The Fund actuary provides advice about the assumptions used in calculating the deficit. The effects of changes in individual assumptions can be measured.	An increase of 0.5% in the discount rate assumption would decrease the pension liability by approximately £110 million. An increase of 0.25% in assumed salary inflation would increase the pension liability by approximately £14 million. A one year increase in assumed life expectancy would increase the pension liability by approximately £31 million.

There are no new relevant accounting standards which have been issued but not yet adopted by the CIPFA Code of Practice on Local Authority Accounting in the United Kingdom.

5. Contributions

2012/2013 £'000		2013/2014 £'000
	Employers' normal contributions	
15,343	Administering authority	14,693
3,050	Scheduled bodies	3,540
2,446	Admitted bodies	2,347
	Employers' other contributions	
12,139	Deficit funding	12,321
1,689	Strain on the Fund following early retirements	1,140
	Members	
8,288	Normal	8,112
42,955		42,153

6. Transfers in from other pension funds

2012/2013 £'000		2013/2014 £'000
3,631	Individual transfers in from other schemes	1,452
3,631		1,452

7. Benefits

2012/2013 £'000		2013/2014 £'000
	Pensions	
33,075	Administering authority	34,292
1,733	Scheduled bodies	1,926
1,412	Admitted bodies	1,453
5,962	Commutation of pensions and lump sum retirement benefits	7,193
680	Lump sum death benefits	1,112
42,862		45,976

8. Payments to and on account of leavers

2012/2013 £'000		2013/2014 £'000
-	Refunds to members leaving service	2
1,980	Individual transfers to other schemes	1,868
2	Payments for members joining state scheme	-
1,982		1,870

9. Administrative expenses

2012/2013 £'000		2013/2014 £'000
719	Administration and processing	669
190	Actuarial and advisory fees	162
22	Audit fee	17
52	Other	70
983		918

10. Investment income

2012/2013 £'000		2013/2014 £'000
2	Dividends from equities	-
1,933	Income from pooled investment vehicles	2,077
161	Income from ventures and partnerships	209
30	Net interest on cash deposits	(29)
27	Other	-
2,153		2,257

11. Investments

	Value at 1 April 2013	Purchases at cost	Sales proceeds	Change in market value	Value at 31 March 2014
	£'000	£'000	£'000	£'000	£'000
Actively managed investments	299,695	73,293	(80,497)	13,243	305,734
Passively managed investments	612,580	36,136	(26,230)	21,543	644,029
	912,275	109,429	(106,727)	34,786	949,763
Other investment balances	725			(73)	2,082
Total	913,000			34,713	951,845

	Value at 1 April 2012	Purchases at cost	Sales proceeds	Change in market value	Value at 31 March 2013
	£'000	£'000	£'000	£'000	£'000
Actively managed investments	271,014	10,353	(11,579)	29,907	299,695
Passively managed investments	528,805	49,942	(47,427)	81,260	612,580
	799,819	60,295	(59,006)	111,167	912,275
Other investment balances	1,506			15	725
Total	801,325			111,182	913,000

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

Transaction costs are included in the cost of purchases and sale proceeds. Transaction costs include costs charged directly to the Fund such as fees, commissions, and stamp duty, and indirect costs incurred through the bid-offer spread on investments within pooled investment vehicles. Direct transaction costs incurred in the year amounted to £nil (£nil in 2012/2013). Indirect transaction costs are not separately provided to the Fund.

Other investment balances

As at 31 March 2013 £'000		As at 31 March 2014 £'000
520	Outstanding dividends, tax and other investment income	78
205	Cash deposits	2,004
725		2,082

12. Investment management expenses

The Fund Account shows investment management fees and custody charges charged to the Fund. Investment management fees are calculated as a percentage of the market value of the portfolio managed. For one fund manager there is an adjustment for under or over performance compared to the appropriate index. Custody is charged for separately. Indirect costs charged within pooled investment vehicles are not separately provided to the Fund.

13. Current assets

As at 31 March 2013 £'000		As at 31 March 2014 £'000
	Contributions due from employers in respect of	
814	Employers	310
272	Members	63
214	Strain on the Fund contributions due from employers	15
49	Retirement grants prepaid	329
2	Other	3
1,351		720

These can be further analysed as follows:

As at 31 March 2013 £'000		As at 31 March 2014 £'000
147	Central government bodies	44
650	Other local authorities	9
66	NHS bodies	87
488	Bodies external to general government	580
1,351		720

14. Current liabilities

As at 31 March 2013 £'000		As at 31 March 2014 £'000
7,399	Due to Northumberland County Council	9,583
166	Retirement/death grants due	307
189	Investment management and custodial fees due	557
182	Other	112
7,936		10,559

These can be further analysed as follows:

As at 31 March 2013 £'000		As at 31 March 2014 £'000
7,399	Other local authorities	9,583
-	NHS bodies	-
537	Bodies external to general government	976
7,936		10,559

15. Analysis of investments

The total market value of the Fund as at 31 March 2014 was £944.2 million (£914.4 million as at 31 March 2013) which can be analysed as follows:

As at 31 March 2013 £m		As at 31 March 2014 £m	%
568.4	UK and overseas equities	588.6	62.3
237.7	Fixed interest and index linked	254.7	27.0
38.5	Property unit trusts	41.5	4.4
67.7	Ventures and partnerships	64.9	6.9
0.7	Other investment balances	2.1	0.2
1.4	Cash deposits and net current (liabilities)/assets	(7.6)	(0.8)
914.4		944.2	100.0

The majority of the Fund's value is held in equities. Analysis by geographical area is as follows:

As at 31 March 2013 £m		As at 31 March 2014 £m	%
318.0	United Kingdom	334.2	56.8
61.9	Europe	66.1	11.2
64.8	North America	65.2	11.1
33.7	Japan	30.4	5.2
31.1	Pacific	31.9	5.4
58.9	Other	60.8	10.3
568.4		588.6	100.0

Analysis of UK equity investments by industrial sector is as follows:

As at 31 March 2013 £m		As at 31 March 2014 £m	%
3.2	Basic materials	4.8	1.4
13.8	Consumer goods	18.4	5.5
13.4	Consumer services	6.9	2.1
16.7	Financials	20.4	6.1
14.4	Health care	12.3	3.7
18.6	Industrials	16.7	5.0
8.6	Oil and gas	7.4	2.2
10.3	Technology	19.3	5.8
2.0	Utilities	-	-
217.0	Other (including managed funds)	228.0	68.2
318.0		334.2	100.0

Fund value and proportions

The values and proportions of the Fund's assets managed externally are as follows:

As at 31 March 2013 £m		As at 31 March 2014 £m	%
612.6	Legal & General Investment Management	644.0	67.7
101.7	M&G Investment Management	109.1	11.5
91.7	Wellington Management International	90.3	9.5
46.3	Morgan Stanley (private equity)	44.2	4.6
14.2	NB Alternatives (private equity)	12.8	1.3
19.2	Schroder Investment Management	20.6	2.2
20.1	BlackRock	21.2	2.2
7.2	GIP (infrastructure)	9.6	1.0
913.0		951.8	100.0

Net current liabilities (net of cash deposits) of £7.6 million are not externally managed and therefore not shown in the analysis above.

All fund managers operating pooled investment vehicles are registered in the United Kingdom.

16. Significant holdings

As at 31 March 2014, the Fund had holdings in certain pooled investment vehicles which individually represented more than 5% of the total value of Fund net assets. These holdings were:

- **£112.6 million (11.9%) in the UK Equity Index Fund managed by Legal & General Investment Management, and a further £112.6 million (11.9%) also in the UK Equity Index Fund managed by Legal & General Investment Management, each in a separate insurance contract.**
- **£82.2 million (8.7%) in the Over Five Year Index Linked Gilts Fund managed by Legal & General Investment Management, and a further £82.1 million (8.7%) also in the Over Five Year Index Linked Gilts Fund managed by Legal & General Investment Management, each in a separate insurance contract.**
- **£109.0 million (11.5%) in the Global Leaders Fund managed by M&G Investment Management.**
- **£57.5 million (6.1%) in the Multi Sector Credit Portfolio managed by Wellington Management International.**

17. Additional voluntary contributions (AVCs)

Scheme members may make AVCs that are invested with the Fund's nominated AVC provider. A wide range of investment types is offered to members and benefits obtained are on a money purchase basis. These contributions are not included in these accounts in accordance with regulation 4(2)(b) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 which prohibits administering authorities from crediting AVCs to the Pension Fund.

During 2013/2014 members were able to invest in an AVC plan with Prudential. Prudential was engaged as AVC provider to the Fund in February 2001 to replace Equitable Life, and all new AVCs taken out after that date were with Prudential. Equitable Life replaced Phoenix Life Limited and some members have continued to contribute to existing AVC investments with both Equitable Life and Phoenix Life Limited.

Aggregate contributions paid by members during 2013/2014 to AVC investments were £436,090 (£314,121 in 2012/2013) to Prudential, £120 (£110 in 2012/2013) to Equitable Life, and £3,514 (£3,919 in 2012/2013) to Phoenix Life Limited.

As at 31 March 2014, the aggregate value of the AVC investments with Prudential was £2,148,449 (£1,848,864 as at 31 March 2013), with Equitable Life was £50,136 (£50,969 as at 31 March 2013), and with Phoenix Life Limited was £33,413 (£44,654 as at 31 March 2013).

18. Related party transactions

Northumberland County Council administers the Pension Fund. During 2013/2014 the Pension Fund had an average balance of £4.3 million borrowed from the Council for which it paid interest of £30,588 (and an average balance of £1.9 million loaned to the Council during 2012/2013 for which it received interest of £30,513). The costs incurred by the Council in administering the Fund, excluding audit fees, are recharged to the Fund on an annual basis. In 2013/2014 these costs amounted to £576,250 (£630,330 in 2012/2013). £9,582,580 was due to the Council at 31 March 2014 (£7,398,821 at 31 March 2013).

Employer contributions for Pension Fund Panel members and senior management who are members of the Scheme are paid in accordance with the rates set by the actuary in the Rates and Adjustments Certificate, and active member contributions are paid in accordance with rates set in the Local Government Pension Scheme Regulations. The terms and conditions which apply to Panel members and senior managers are the same as those which apply to all other Scheme members. Four voting Panel members were members of the Scheme as at 31 March 2014 (four as at 31 March 2013).

19. Fund's operations, funding and membership

Northumberland County Council Pension Fund is part of the Local Government Pension Scheme (LGPS), which is a statutory, funded pension scheme. The benefits of the Scheme are defined and guaranteed in law.

The LGPS is contracted out of the State Second Pension (S2P) and must provide benefits that are broadly equivalent to, or better than members would have received had they been members of S2P. Benefits provided include a tax-free lump sum, with the option to commute pension for lump sum, and a guaranteed pension based on final salary upon retirement.

Local authority employees other than those aged over 75, those on contracts of less than three months who have not elected to join, teachers and fire-fighters, are automatically admitted to the LGPS, unless they opt out. Automatic enrolment legislation also applies to all eligible workers. The list of all participating employers in the Northumberland County Council Pension Fund as at 31 March 2014 is shown in Appendix 1.

The LGPS changed with effect from 1 April 2014 to a career average scheme for service accrued on and after 1 April 2014; service accrued prior to 31 March 2013 remains linked to final salary.

Northumberland County Council Pension Fund collects contributions from active members of the LGPS and their employers. It pays pensions and related expenses, and reimburses Northumberland County Council for the costs incurred in administering the LGPS. Surplus funds, not needed for the day-to-day expenses, are invested with external fund managers for long term growth.

As a funded scheme, contributions received from employers and employees and transfer values received are invested in the Fund to meet the benefits when they fall due. Future returns on investments and future benefits payable are not known in advance, therefore the employer contributions payable are regularly reviewed (every three years) by the Fund actuary to ensure their adequacy for the Fund's long term solvency. The last statutory actuarial valuation of the Fund was carried out as at 31 March 2013. Investment, inflation and longevity risks are carried by the employers and not by the individual Scheme members.

Northumberland County Council is the administering authority for Northumberland County Council Pension Fund under the LGPS Regulations, and has delegated its responsibility for determining investment policy and monitoring performance to the Pension Fund Panel.

The Pension Fund Panel comprises six County Council representatives, one non-voting employer representative, one non-voting Scheme member representative and two non-voting Trade Union representatives.

External fund managers have been appointed to make the day-to-day investment decisions.

As at 31 March 2014 there were five external fund managers, namely Legal & General Investment Management, M&G Investment Management, Wellington Management International, BlackRock, and Schroder Investment Management.

As at 31 March 2014 the Fund also had private equity investments with Morgan Stanley, NB Alternatives and Capital North East, and an infrastructure investment with Global Infrastructure Partners.

The Northern Trust Company provides custodial services for the Fund.

20. Statement of Investment Principles (SIP)

Northumberland County Council Pension Fund's SIP is shown on pages 8 to 15 of this report.

21. Outstanding commitments

As at 31 March 2014 the Fund had outstanding commitments to six investments.

	Initial commitment	Capital payments made	Outstanding commitment as at 31 March 2014	
Morgan Stanley Private Markets III	**$50.0m**	**$46.6m**	**$3.4m**	**£2.1m**
Morgan Stanley GDO Fund	**$10.0m**	**$9.3m**	**$0.7m**	**£0.4m**
NB Crossroads Fund XVIII	**$27.0m**	**$22.4m**	**$4.6m**	**£2.8m**
Morgan Stanley Private Markets IV	**$30.0m**	**$26.2m**	**$3.8m**	**£2.3m**
Global Infrastructure Partners II-C	**$43.0m**	**$11.8m**	**$31.2m**	**£18.7m**
Antin Infrastructure Partners II	**€24.0m**	**-**	**€24.0m**	**£19.8m**
Total outstanding commitments				**£46.1m**

Outstanding capital commitments totalled £46.1 million as at 31 March 2014 (£34.9 million as at 31 March 2013). Capital is payable by the Fund to these private equity and infrastructure investments when called. Amounts called are irregular in value and timing, and are typically spread over a period of up to ten years. The maximum unexpired commitment period as at 31 March 2014 was two years for Morgan Stanley Private Markets Fund III and Morgan Stanley GDO Fund, three years for NB Crossroads Fund XVIII and Morgan Stanley Private Markets Fund IV, nine years for Global Infrastructure Partners Fund II-C, and twelve years for Antin Infrastructure Partners II.

22. Financial instruments

The value of financial instruments, classified into one of three levels according to the quality and reliability of information used to determine values, is as follows:

	As at 31 March 2014		
	Level 1	Level 3	Total
	£'000	£'000	£'000
Financial assets at fair value through profit and loss	884,899	64,864	949,763
Loans and receivables	5,017	-	5,017
Financial (liabilities) at amortised cost	(10,559)	-	(10,559)
Net financial assets	879,357	64,864	944,221

	As at 31 March 2013		
	Level 1	Level 3	Total
	£'000	£'000	£'000
Financial assets at fair value through profit and loss	844,575	67,700	912,275
Loans and receivables	10,083	-	10,083
Financial (liabilities) at amortised cost	(7,936)	-	(7,936)
Net financial assets	846,722	67,700	914,422

Level 1 means financial instruments valued using unadjusted quoted prices in active markets for identical assets or liabilities; level 2 means financial instruments valued using mainly observable market data and level 3 means financial instruments valued using unobservable inputs.

The majority of the Fund assets are valued based on quoted prices and are classified as level 1. The Fund has no financial instruments classified as level 2 and has private equity and infrastructure investments classified as level 3 which are based on the valuations provided by the general partners to the funds invested in. Private equity and infrastructure investments are categorised as "ventures and partnerships" in the Net Assets Statement.

Net gains and losses on financial instruments can be analysed as follows:

2012/2013 £'000		2013/2014 £'000
111,167	Financial assets at fair value through profit and loss	34,786
15	Loans and receivables	(73)
111,182	Total net gains on financial instruments	34,713

23. Nature and extent of risk arising from financial instruments

Overall Fund risk

All Fund assets and liabilities, as disclosed in the Net Assets Statement, are classified as financial instruments. However, as stated at the foot of the Net Assets Statement, it excludes the most significant Fund liability, namely the obligations to pay pensions and benefits which fall due after the end of the year. The actuarial position of the Fund, which values such pension obligations, is dealt with in the Statement of the Actuary and the Whole of Pension Fund Disclosures under IAS26 shown in Appendices 2 and 3 respectively to this report.

The sole purpose of holding Fund assets is to invest contributions received from employees and employers, together with transfer values received and investment income, so that there are sufficient funds available to pay pensions when the active and deferred members become pensioner members.

The primary risk for the Fund is the risk that Fund assets do not match the liabilities over the long term. It is the gap between the assets and liabilities, known as the funding deficit (or surplus), which is most relevant to the Fund's participating employers, who are responsible for meeting the funding deficit. Focussing on the risks surrounding the assets alone therefore gives only a partial picture. For example, should UK gilt yields increase this would reduce the value of the Fund's holdings in UK gilts, but it would also reduce the actuarial value placed on the liabilities to pay pensions by considerably more, and therefore reduce any funding deficit.

Overall Fund risk and the actions taken to manage that risk are described in the Fund's Statement of Investment Principles, shown on pages 8 to 15 of this report, and in the Funding Strategy Statement, shown on pages 20 to 35 of this report.

The key controls are:

- **the actuarial valuation of the Fund which is carried out every three years and sets the employer contribution rates;**
- **the asset liability modelling study which is carried out every three years or more frequently if necessary, to consider alternative asset allocations for the Fund and the long term impact on employer contribution rates; and**
- **quarterly monitoring by the Pension Fund Panel of the Fund investments and of the updated estimated funding position.**

The remainder of this note only considers risk in relation to the financial instruments disclosed on the Net Assets Statement.

Credit risk

Credit risk is the risk that the counterparty to a transaction or financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss.

The Fund is exposed to credit risk on its externally managed investment portfolio, on cash deposits managed in-house, and on the contributions receivable from the Fund's participating employers.

The market values of investments usually reflect an assessment of credit risk in their pricing and as a result the risk of loss is implicitly provided for in the fair value of the Fund's investments. Credit risk is also managed through the selection and monitoring of the Fund's custodian and investment managers, and via their contracts with the Fund. All investment managers and the custodian are required to provide the Fund with an up to date AAF06/01 report, or equivalent, annually. The Fund's active bond manager, Wellington Management International, considers credit risk as part of its portfolio construction.

Credit risk on cash deposits managed in-house is managed by Northumberland County Council's Treasury Management Team, following the Council's Treasury Management Policy. This policy is described in detail in Northumberland County Council's Annual Report.

Credit risk on contributions receivable from employers is minimised by regular monitoring of the monthly receipt of payments from employers. There is no provision for doubtful debts against the amounts due from employers as at 31 March 2014. The LGPS Regulations require that a risk assessment of any new transferee admitted body is carried out, and that a bond or guarantee is obtained where necessary. The Pension Fund Panel must approve the admission of any new community admission body. Bonds or guarantees have been obtained for the Fund's admitted employers, where possible. The Fund is potentially exposed to credit risk from certain scheduled employers that have neither tax-raising powers nor a guarantee from central government.

None of the Fund's financial assets are past due or impaired.

Liquidity risk

Liquidity risk is the risk that the Fund will not be able to meet its financial obligations as they fall due.

The Fund holds in-house cash resources to meet day-to-day needs and to pay pensions. If there is insufficient cash available to meet immediate needs, units in the Fund's holdings with Legal & General Investment Management, which totalled £644.0 million as at 31 March 2014, can be realised at short notice and at minimal cost. In five out of the last ten years the Fund has experienced net withdrawals from dealings with members, with the maximum withdrawal in a single year being £5.2 million.

With the exception of investments in private equity and infrastructure, there are no commitments to contribute further capital to any of the existing Fund investments. When private equity/infrastructure capital calls are received, payment is made out of in-house cash surpluses, or, if there are insufficient funds available, units held with Legal & General are realised. Note 21 to the accounts shows further information about outstanding commitments to private equity and infrastructure investments.

Market risk

Market risk is the risk of loss from fluctuations in equity and commodity 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.

Market risk is inherent in the investments that the Fund holds. To mitigate market risk, the Fund invests in a diversified portfolio, to include a variety of asset classes, geographical regions and industrial sectors. The Fund is also managed by five different investment managers, each with different investment styles and strategies, and different benchmarks and performance targets. The LGPS Regulations contain prescribed limits to prevent overconcentration in certain asset classes and encourage diversification. Full details of asset allocation and management structure are described in the Fund's Statement of Investment Principles shown on pages 6 to 14 of this report.

The purpose of diversifying the portfolio of assets in the Fund is to reduce the impact of price movements, because it is unlikely that all asset classes will move in the same direction at the same time.

To manage market risk, the Pension Fund Panel and its adviser regularly review the Fund's asset allocation and management structure, and monitor investment managers' performance on a quarterly basis.

Market risk can be divided into three elements, namely other price risk, interest rate risk and currency risk. These are considered further below.

Market risk - other price risk

Other price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices. The Fund is exposed to other price risk on all of its investment assets. This risk is mitigated by asset and manager diversification. Price risk can be quantified as follows:

	As at 31 March 2014 £'000	Percentage change %	Value on on increase £'000	Value on decrease £'000
UK equities	**334,205**	**12.3**	**375,279**	**293,131**
Overseas equities	**254,442**	**11.8**	**284,441**	**224,443**
Index linked	**164,427**	**8.9**	**178,979**	**149,875**
Other fixed interest	**90,315**	**4.2**	**94,108**	**86,522**
Property	**41,510**	**1.7**	**42,220**	**40,800**
Ventures and partnerships	**64,864**	**8.2**	**70,157**	**59,571**
Other investment balances	**2,082**	**-**	**2,082**	**2,082**
Total investment assets	**951,845**	**7.1**	**1,019,331**	**884,359**

	As at 31 March 2013	Percentage change	Value on on increase	Value on decrease
	£'000	%	£'000	£'000
UK equities	317,934	13.4	360,410	275,458
Overseas equities	250,433	12.7	282,188	218,678
Index linked	145,968	8.4	158,186	133,750
Other fixed interest	91,694	6.0	97,205	86,183
Property	38,546	1.2	39,009	38,083
Ventures and partnerships	67,700	8.9	73,725	61,675
Other investment balances	725	-	725	725
Total investment assets	**913,000**	**8.5**	**990,331**	**835,669**

The percentage change for total investment assets as at 31 March 2014 and as at 31 March 2013 includes the impact of correlation across asset classes, so the value on increase/decrease amounts do not sum to the total investment assets shown above.

Potential price changes are determined based on the observed historical volatility of asset class returns. The potential volatilities are consistent with a one standard deviation movement in the change in value of the assets over the latest three years. The analysis shown above assumes all other potential variables remain the same. The price risk shown above includes interest rate risk and currency risk as they cannot be separated out of market price movements.

Market risk - interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate as a result of interest rate changes. The Fund is exposed to interest rate risk on its fixed interest investment assets. This risk is mitigated by asset and manager diversification. Interest rate risk can be quantified as follows:

	As at 31 March 2014	Value following 1% decrease in interest rates	Value following 1% increase in interest rates
	£'000	£'000	£'000
Index linked	164,427	199,416	129,436
Other fixed interest	90,315	92,895	87,736
Total fixed interest investments	**254,742**	**292,311**	**217,172**

	As at 31 March 2013	Value following 1% decrease in interest rates	Value following 1% increase in interest rates
	£'000	£'000	£'000
Index linked	145,968	176,855	115,081
Other fixed interest	91,694	97,065	86,322
Total fixed interest investments	**237,662**	**273,920**	**201,403**

Bond instruments tend to fall in value when interest rates rise and rise in value when interest rates fall. The analysis above shows the likely effect of a 1% increase or decrease in interest rates on the value of the bond instruments held by the Fund. It assumes all other potential variables remain the same, and ignores the effect a change in interest rates might have on the value of other investments held.

Market risk - currency risk

Currency risk is the risk of the value of a financial instrument changing as a result of changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that were purchased in any currency other than sterling. This risk is mitigated by asset and manager diversification. Currency risk can be quantified as follows:

	As at 31 March 2014 £'000	Percentage change %	Value on on increase £'000	Value on decrease £'000
Equities				
Europe	66,093	4.1	68,790	63,396
North America	65,228	7.6	70,192	60,264
Japan	30,394	11.5	33,901	26,887
Pacific	31,932	6.1	33,883	29,981
Other	60,795	6.4	64,668	56,922
Other fixed interest	90,315	5.2	95,020	85,610
Ventures and partnerships	64,846	8.1	70,079	59,613
Total overseas investments	409,603	5.3	431,289	387,917

	As at 31 March 2013 £'000	Percentage change %	Value on on increase £'000	Value on decrease £'000
Equities				
Europe	61,894	7.2	66,332	57,456
North America	64,808	8.3	70,187	59,429
Japan	33,716	11.8	37,684	29,748
Pacific	31,109	6.3	33,072	29,146
Other	58,906	6.4	62,694	55,118
Other fixed interest	91,694	5.3	96,572	86,816
Ventures and partnerships	67,675	8.7	73,590	61,760
Total overseas investments	409,802	5.6	432,754	386,850

The percentage change for total overseas investments as at 31 March 2014 and as at 31 March 2013 includes the impact of correlation across currencies, so the value on increase/decrease amounts do not sum to the total overseas investments shown above.

Potential value changes are determined based on the observed historical volatility of currency movements relative to sterling. The potential volatilities are consistent with a one standard deviation movement in currencies relative to sterling over the latest three years. The analysis shown above assumes all other potential variables remain the same.

Appendix 1

Fund Membership

As at 31 March 2014

	Active members	Pensioner members	Deferred members
Northumberland County Council - Employees	6,425	6,951	6,891
- Councillors	20	12	12
Local Government Pension Scheme Employers (known as “Scheduled Bodies”)			
Ashington Town Council	3	0	0
Bede Academy	82	7	27
Berwick Academy	42	4	4
Blyth Academy (formerly Blyth Community College)	64	3	1
Blyth Quays Academy	124	3	12
Choppington Parish Council	2	0	0
Corbridge Parish Council	1	0	0
Cramlington Learning Village Academy	77	5	8
Haltwhistle Community Campus Academy	41	0	1
Hexham Town Council	5	4	0
Homes for Northumberland Ltd	200	69	119
Meadowdale Academy	28	2	11
Morpeth Town Council	5	2	0
Northumberland College	192	130	220
Northumberland Church of England Academy	280	36	91
Northumberland Inshore Fisheries and Conservation Authority	14	4	3
Northumberland National Park Authority	51	26	92
Northumberland Valuation Tribunal Service	1	8	0
Northumbria Magistrates Courts Committee	0	82	62
Ponteland Town Council	1	1	0
Seaton Valley Council	1	0	0
Three Rivers Learning Trust Academy	135	5	29
West Bedlington Town Council	1	0	0
Admitted Bodies			
Action for Children	24	1	5
Age UK Northumberland	6	12	14
Barnardo’s Services Ltd	14	0	8
Berwick Borough Housing Ltd	10	8	4
Blyth Valley Arts and Leisure Trust	131	16	64
Bullough Cleaning Services Ltd	12	0	0
Community Action Northumberland	0	23	24
Creative Management Services Ltd	5	0	5
Feversham School	0	26	14
Helping Hands Community Care	1	0	0
Isos Housing Ltd	23	55	21
North Country Leisure	64	11	54
Northumberland Aged Mineworkers Homes Association	8	7	0
Northumberland County Blind Association	5	4	6
Northumbria Healthcare NHS Foundation Trust	60	67	49
Queens Hall Arts	4	1	1
Superclean Services Wothorpe Ltd	4	0	0
Tees Active Ltd	1	0	0
The Disabilities Trust	1	3	3
The Maltings (Berwick) Trust	1	1	2
Three Rivers Housing Association Ltd	2	1	0
Wansbeck Homes	122	39	14
Woodhorn Charitable Trust	29	5	4
Other bodies pre 1974	0	15	0
	8,322	7,649	7,875

Appendix 2

Statement of the Actuary for the year ended 31 March 2014

Introduction

The Scheme Regulations require that a full actuarial valuation is carried out every third year. The purpose of this is to establish that the Northumberland County Council Pension Fund (the Fund) is able to meet its liabilities to past and present contributors and to review employer contribution rates. The latest full actuarial investigation into the financial position of the Fund was completed as at 31 March 2013 by Aon Hewitt Limited, in accordance with Regulation 36 of the Local Government Pension Scheme (Administration) Regulations 2008.

Actuarial position

1. The valuation as at 31 March 2013 showed that the funding ratio of the Fund had increased since the previous valuation with the market value of the Fund's assets at that date (of £914.4M) covering 81% of the liabilities allowing, in the case of current contributors to the Fund, for future increases in pensionable pay.

2. The valuation also showed that the aggregate level of contributions required to be paid by participating employers with effect from 1 April 2014 is:

- **16.4% of pensionable pay. This is the rate calculated as being sufficient, together with contributions paid by members, to meet the liabilities arising in respect of service after the valuation date.**

Plus

- **Monetary amounts to restore the assets to 100% of the liabilities in respect of service prior to the valuation date over a recovery period of 22 years from 1 April 2014, amounting to £11.4M in 2014/15, and increasing by 3.9% p.a. thereafter.**

3. In practice, each individual employer's position is assessed separately and contributions are set out in Aon Hewitt Limited's report dated 31 March 2014 (the "actuarial valuation report"). In addition to the contributions shown above, payments to cover additional liabilities arising from early retirements (other than ill-health retirements) will be made to the Fund by the employers.

4. The funding plan adopted in assessing the contributions for each individual employer is in accordance with the Funding Strategy Statement. Different approaches adopted in implementing contribution increases and individual employers' recovery periods are set out in the actuarial valuation report.

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

Discount rate for periods in service		
	Scheduled Bodies	**5.3% p.a.**
	Orphan Bodies	**5.2% p.a.**
Discount rate for periods after leaving service		
	Scheduled Bodies	**5.3% p.a.**
	Orphan Bodies	**3.7% p.a.**
Rate of pay increases (additional allowance made for promotional increases)		**3.9% p.a.**
Rate of increase to pension accounts		**2.4% p.a.**
Rate of increases in pensions in payment (in excess of Guaranteed Minimum Pension):		**2.4% p.a.**

The assets were valued at market value.

Further details of the assumptions adopted for the valuation were set out in the actuarial valuation report.

6. The valuation results summarised above are based on the financial position and market levels at the valuation date, 31 March 2013. As such the results do not make allowance for changes which have occurred subsequent to the valuation date.

7. The formal actuarial valuation report and the Rates and Adjustments Certificate setting out the employer contribution rates for the period from 1 April 2014 to 31 March 2017 were signed on 31 March 2014. Contribution rates will be reviewed at the next actuarial valuation of the Fund as at 31 March 2016.

8. This Statement has been prepared by the current Actuary to the Fund, Aon Hewitt Limited, for inclusion in the accounts of the Fund. It provides a summary of the results of their actuarial valuation which was carried out as at 31 March 2013. The valuation provides a snapshot of the funding position at the valuation date and is used to assess the future level of contributions required.

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

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

Aon Hewitt Limited
21 May 2014

Appendix 3

Whole of Pension Fund Disclosures under IAS26

Northumberland County Council Pension Fund ("the Fund")

23 May 2014

Prepared for

Northumberland County Council, as Administering Authority to the Fund

Prepared by

Chris Archer FIA

Aon Hewitt Ltd

1 Introduction

Addressee

This report sets out pension cost information required by Northumberland County Council in its capacity as Administering Authority to the Fund (the "Administering Authority") in order to meet their disclosure requirements in relation to their pension obligations as specified by the accounting standard, IAS 26.

We have carried out this work in relation to benefits payable from the Northumberland County Council Pension Fund (the "Fund").

Related Documents

The advice provided in this report is supported by advice contained in the following documents:

- **IAS 26 Terms of Reference dated 27 March 2014 (the 'Terms of Reference').**
- **Advice in relation to the actuarial assumptions was provided by Aon Hewitt in a document dated 23 May 2014 ('Assumptions Advice').**

In addition, the following document should be referred to which contains a more detailed description of the approach taken in valuing liabilities, further detail on the demographic assumptions and the treatment of data.

- **Actuarial Valuation at 31 March 2013 – Northumberland County Council Pension Fund dated 31 March 2014 (the '2013 Valuation').**

Background

The Code of Practice indicates that the Fund accounts for the year ending 31 March 2014 should disclose the "actuarial present value of the promised retirement benefits" as set out in IAS 26 and that the actuarial present value should be calculated on assumptions set in accordance with IAS 19 rather than on the funding assumptions.

CIPFA put forward three options for disclosing the actuarial present value of promised retirement benefits and further detail on these can be found in our Terms of Reference document noted above.

The Administering Authority has chosen "Option C" which was confirmed to us in an e-mail dated 27 March 2014. Option C requires the actuarial valuation of the liabilities on an IAS 19 basis to be prepared at formal triennial valuations only, the most recent being as at 31 March 2013. Under Option C this, together with other related information, should be disclosed in an actuarial report which will accompany the notes to the accounts.

The calculations contained in this document have been carried out on a basis consistent with our understanding of IAS 19.

I confirm that I am a Fellow of the Institute and Faculty of Actuaries.

Document structure

This document is structured as follows:

- **Section 1 summarises the scope of the work we have undertaken.**
- **Section 2 sets out the results of our calculations together with some comments on the calculations.**
- **Appendix A summarises the data used in our calculations.**
- **Appendix B sets out a brief explanation of the method we have used in preparing the figures.**
- **Appendix C sets out compliance and legal considerations.**

Methodology

The approach to our calculations under the various options was set out in the Terms of Reference. Comments on the methodology as it applies to IAS 26 are set out as Appendix B.

2 Information Required for IAS 26

Introduction

IAS 26 requires the "actuarial present value of the promised retirement benefits" to be disclosed, which is the IAS 26 terminology for what IAS 19 refers to as the "defined benefit obligation".
The information set out below relates to the actuarial present value of the promised retirement benefits in the Fund which is part of the Local Government Pension Scheme. The Fund provides defined benefits, based on members' Final Pensionable Pay.

Actuarial present value of promised retirement benefits

Paragraph 6.5.2.7 of CIPFA's Code of Practice on local authority accounting for 2013/14 sets out that the actuarial present value of promised retirement benefits based on projected salaries should be disclosed. The results at as 31 March 2013, together with the 2010 figures are shown in the table below. The corresponding fair value of Fund assets is also shown in order to show the level of surplus or deficit within the Fund when the liabilities are valued using IAS 19 assumptions. We do not believe the Authority needs to show the 2010 figures under IAS 26 if it does not wish to do so. The Code of Practice is not clear if the fair value of assets and the surplus / deficit at 31 March 2013 also needs to be disclosed but you may want to include these figures for clarity.

	Value as at 31 March 2013 £M	**Value as at 31 March 2010 £M**
Fair value of net assets	**914.4**	**719.0**
Actuarial present value of the promised retirement benefits	**1,281.2**	**1,209.3**
Surplus / (deficit) in the Fund as measured for IAS26 purposes	**(366.8)**	**(490.3)**

Assumptions

The latest full triennial actuarial valuation of the Fund's liabilities was carried out as at 31 March 2013. The principal assumptions used for the purpose of IAS 26 by the Fund's independent qualified actuaries were:

	31 March 2013 (% p.a.)	**31 March 2010 (% p.a.)**
Discount rate	**4.4**	**5.5**
RPI Inflation	**3.4**	**3.9**
CPI Inflation	**2.4**	**3.0**
Rate of increase to pensions in payment*	**2.4**	**3.9**
Rate of increase to deferred pensions*	**2.4**	**3.9**
Rate of general increase in salaries **	**3.9**	**5.4**

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

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

Principal demographic assumptions

Post retirement mortality	31 March 2013	31 March 2010
Males		
Base table	Standard SAPS Normal Health All Amounts (S1NMA)	Standard SAPS Normal Health All Amounts (S1NMA)
Scaling to above base table rates **	100%	100%
Allowance for future improvements	CMI 2012 with a long term rate of improvement of 1.5% p.a.	CMI 2009 with a long term rate of improvement of 1.25% p.a.
Future lifetime from age 65 (currently aged 65)	22.8	22.1
Future lifetime from age 65 (currently aged 45)	25.0	24.0
Females		
Base table	Standard SAPS Normal Health All tables (S1NFA)	Standard SAPS Normal Health All tables (S1NFA)
Scaling to above base table rates **	100%	100%
Allowance for future improvements	CMI 2012 with a long with long term improvement of 1.5% p.a.	CMI 2009 with a long Cohort improvements of 1.25% p.a.
Future lifetime from age 65 (currently aged 65)	25.3	24.3
Future lifetime from age 65 (currently aged 45)	27.6	26.3

* A rating of x years means that members of the Fund are assumed to follow the mortality pattern of the base table for an individual x years older than them. The ratings shown apply to normal health retirements.

** The scaling factors shown apply to normal health retirements

Commutation	31 March 2013	31 March 2010
	Each member was assumed to surrender pension on retirement, such that the total cash received (including any accrued lump sum from pre 2008 service) is 75% of the permitted maximum.	Each member is assumed to exchange 50% of the maximum amount permitted, of their past service pension rights on retirement, for additional lump sum. Each member is assumed to exchange 75% of the maximum amount permitted, of their future service pension rights on retirement, for additional lump sum.

Changes in benefits during the accounting period

There have been no changes in benefits during the accounting period. No allowance has been made in our calculations for the new Scheme benefits accruing from 1 April 2014.

Key risks associated with reporting under IAS 26

Volatility of results

Results under IAS 26 can change dramatically depending on market conditions. The defined benefit obligation is linked to yields on AA-rated corporate bonds, while a significant proportion of the assets of the Fund are invested in equities. Changing markets in conjunction with discount rate volatility will lead to volatility in the funded status of the pension fund.

If at any time during the year you want us to provide you with an update of the IAS 26 position, please let us know.

Choice of accounting assumptions

The calculation of the actuarial present value of the promised retirement benefits involves projecting future cash-flows from the Fund many years into the future. This means that the assumptions used can have a material impact on the surplus / deficit. As such, the Administering Authority should ensure that it understands the reasoning behind the assumptions adopted and are comfortable that they are appropriate.

Furthermore, the Administering Authority should bear in mind that, as required by the accounting standard, the assumptions (with the exception of the discount rate) have been set so that they represent a best estimate of future experience from the Fund. In practice future experience within the Fund may not be in line with the assumptions adopted. This means that the liabilities shown in this report only represent one view of the future and the true position could be different from those shown. For example members could live longer than foreseen or inflation could be higher or lower than allowed for in the calculations.

Sensitivity of results to key assumptions

In order to understand the magnitude of the possible volatility in the balance sheet position and to understand which assumptions are most important in determining the size of the liabilities, it is helpful to understand how sensitive the results are to key assumptions.

The revised version of IAS 19 requires entities to disclose information about the sensitivity of the defined benefit obligation to changes in key assumptions although it is not clear that IAS 26 or the CIPFA Code of Practice requires this information. Please let us know if you require this information.

GMP equalisation

The Government intends that GMPs will be equalised in due course. At present it is not appropriate to allow for this in the accounts because the methodology for implementing the equalisation is uncertain. However, once the methodology is clarified, the defined benefit obligation will increase and it is likely that the associated cost will need to be recognised through the profit and loss account. As such, a risk exists as to the magnitude of the impact of equalising GMPs.

Appendix A Data Summary

Active members at 31 March 2013

		Number	Average age	Total Pensionable Pay (£000 p.a.)	Average Pensionable Pay (£ p.a.)	Average service (years)
Men	**2013**	2,175	46.8	50,193	23,077	13.5
	2010	2,369	46.4	53,296	22,497	13.5
Women	2013	5,565	46.2	77,114	13,857	7.2
	2010	6,079	45.2	79,053	13,004	6.6
Total	2013	7,740	46.4	127,307	16,448	8.9
	2010	8,448	45.5	132,349	15,666	8.5

Note: Pay is that over the year to the respective valuation date. Annualised pay is included for entrants in the last year. Part time pay is included for part-timers.

Deferred pensioners at 31 March 2013

		Number	Average age	Total pension (£000 p.a.)	Average pension (£ p.a.)
Men	2013	1,924	44.9	4,374	2,273
	2010	1,758	44.5	3,529	2,008
Women	2013	5,658	45.7	6,187	1,093
	2010	4,857	44.6	4,526	932
Total	2013	7,582	45.5	10,561	1,393
	2010	6,615	44.5	8,055	1,218

Note: The deferred pensions include increases granted in April 2013 (2010). In addition to the numbers above there were members who had yet to decide whether to take a transfer payment. Suitable allowance has been made for these in our calculations.

Pensioners at 31 March 2013

		Number	Average age	Total pension (£000 p.a.)	Average pension (£ p.a.)
Men	2013	2,727	70.0	22,428	8,225
	2010	2,532	69.4	19,166	7,570
Women	2013	3,683	69.4	11,892	3,229
	2010	3,291	68.6	9,444	2,870
Dependants	2013	967	76.2	2,755	2,849
	2010	943	76.5	2,344	2,485
Total	2013	7,377	70.5	37,075	5,026
	2010	6,766	70.0	30,954	4,575

Note: The pensions include increases granted in April 2013 (2010). The 2013 figures include 54 children (2010:45) who are in receipt of pensions. Suitable allowance has been made for these in our calculations.

Appendix B Explanation of Actuarial Methods Used

Benefits valued

Our calculations relate to benefits payable from the Fund (as set out in LGPS Regulations at the relevant times) and related arrangements. These benefits include retirement pensions and benefits on members' death and leaving service.

A summary of the benefits that have been valued can be found in the reports on the actuarial valuations of the Fund as at 31 March 2013 and 31 March 2010.

Unfunded defined benefit obligations e.g. discretionary pensions benefits being paid under the Local Government (Early Termination of Employment) (Discretionary Compensation) Regulations (generally referred to as Compensatory Added Years), have not been valued as they do not form part of the Fund. However, they may be required in the IAS 19 figures prepared for individual employers within the Fund.

Data

The valuation of accrued pension benefits for IAS 26 purposes requires detailed information in respect of each member such as date of birth, gender, date of joining the fund, their accrued pension and so forth.

This information was supplied by the Administering Authority for the 2013 and 2010 formal actuarial valuations of the Fund in the form of a standardised data extract from the Authority's administration systems.

The formal valuation process (which is a precursor to the valuation for IAS 26 purposes) involves a series of structured validation tests on the data items for integrity and reasonableness. These tests, together with any actions taken in respect of specific data issues, are documented as part of the normal valuation process.

Where tests reveal issues with the data, the Administering Authority is contacted with a view to resolving all data queries. Only when the data queries have been resolved to the satisfaction of the Fund Actuary, will the valuation proceed.

We can confirm that no data issues were identified at either the 2013 or the 2010 valuations that would have any material effect on the calculations presented in this report. Overall, it is our opinion that the data presented at both valuations is sufficiently accurate, relevant and complete for the Administering Authority to rely on the resulting IAS 19 (IAS 26) figures.

Assumptions

IAS 19 sets out the following general requirements for the setting of assumptions:

- **Actuarial assumptions shall be unbiased and mutually compatible; and**
- **Financial assumptions shall be based on market expectations, at the balance sheet date, for the period over which the obligations are to be settled.**

Furthermore IAS 19 requires that the assumed discount rate is determined by reference to market yields at the balance sheet date on high quality corporate bonds and in countries where there is no deep market in such bonds, the market yield (at the balance sheet date) on government bonds shall be used.

CIPFA have informed us that under IAS 26 the assumptions are ultimately the responsibility of the Administering Authority. Any assumptions that are affected by economic conditions (financial assumptions) should reflect market expectations at the balance sheet date.

The key financial assumptions are set out on the first page of Section 2 and the derivation of the assumptions is set out in our assumptions letter referred to in the Related Documents section.

Method and calculations

The figures at 31 March 2013 have been based on a full calculation of the liabilities using the same method as for the full 2013 triennial valuation Fund, but with IAS 19 financial assumptions used.

Assets

IAS 19 requires that assets be valued at Fair Value which is defined as the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction. For the purposes of this exercise we have taken the asset values directly from the Fund's audited annual accounts as at 31 March 2013.

Treatment of Risk Benefits

To value the risk benefits we have valued service related benefits based on service completed to the date of calculation only.

Expenses

Scheme administration expenses are not reserved for in the Net Present Value of Actuarial Liabilities, consistent with the treatment adopted for individual employers who require IAS 19 disclosures. If the Fund wishes the administration expenses to be treated in a different way they should discuss this further with their auditor and ourselves.

IFRIC 14

IFRIC 14 is an interpretation of paragraph 58 of the IAS 19 accounting standard setting out limits to the amount of surplus that can be recognised by employing organisations in their accounts. We do not believe it has any relevance to IAS 26.

Appendix C Compliance and Disclaimer

Compliance with actuarial standards

This report should be read in conjunction with the supporting documents listed in Section 1.

This report and the work related to it, is subject to and complies with the Financial Reporting Council Limited's Pensions Technical Actuarial Standard and the Technical Actuarial Standards on reporting actuarial information, data and modelling.

The results of the calculations provided in this document constitute a valuation exercise.

Disclaimer

The calculations contained in this report have been made on a basis consistent with our understanding of IAS 19 and IAS 26. Figures required for other purposes should be calculated in accordance with the specific requirements of those purposes. It must not be assumed that figures produced for the purposes of IAS 26, which we present in this report, have any relevance beyond the scope of the Financial Reporting Standards requirements.

This report is prepared on the instructions of the Administering Authority as appropriate ("you" or "your") in relation to the preparation of IAS 26 figures for the Administering Authority's financial reporting as at the accounting date. It has been prepared at this date, for the purpose and on the basis set out in this report and for the benefit and use of the Administering Authority.

This report should not be used or relied upon by any other person for any other purpose including, without limitation, other professional advisers, including your auditors and accountants ("third parties" or "third party"), to the Administering Authority. All third parties are hereby notified that this report shall not be used as a substitute for any enquiries, procedures or advice which ought to be undertaken or sought by them. We do not accept any responsibility for any consequences arising from any third party seeking to rely on this report.

We neither warrant nor represent (either expressly or by implication) to any third party who receives this report that the information contained within is fair, accurate or complete, whether at the date of its preparation or at any other time.

Unless we provide express prior written consent, no part of this report should be reproduced, distributed or communicated to any other person other than to meet any statutory requirements and, in providing this report, we do not accept or assume any responsibility for any other purpose or to anyone other than the Administering Authority as appropriate.

We recognise that your auditors may request you directly to see a copy of our report, as part of their audit process and under statutory requirements. We agree that you may release our report to those auditors for such purpose however in making such disclosure, you shall ensure that this disclaimer remains attached to this report, and you further agree that you shall ensure that your auditors have read this disclaimer. For the avoidance of doubt, if we are approached directly by any third party for copies of this report or requested to answer queries about the report, we will require such third party to accept a third party release non reliance letter agreeing that we did not prepare the report for the third party and we do not accept any legal obligations to them. Please rest assured that this approach does not affect our contractual obligations to you as our client, with whom we continue to hold a duty of care in accordance with our terms of engagement.

This report was based on data available to us at the effective date of our calculations and takes no account of developments after that date except where explicitly stated otherwise.

With respect to data on which we have relied in producing this report, whilst we have taken certain limited steps to satisfy ourselves that the data provided to us is of a quality sufficient for the purposes of our investigation, including carrying out certain basic tests for the purpose of detecting manifest inconsistencies, it is not possible for us to confirm the accuracy or completeness of the detailed information provided. Whilst the Administering Authority may have relied on others for the maintenance of accurate data, it is their responsibility to ensure the adequacy of these arrangements and ultimately the Administering Authority that bears the primary responsibility for the accuracy of such information provided. The information used is summarised in various sections of this report and Appendix A.

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Northumberland County Council

for you, for now, for the future