



# PENSION FUND ANNUAL REPORT

2019-20

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## INTRODUCTION

The London Borough of Southwark Pension Fund (the Fund) is the largest pension fund in London in terms of membership and assets. It is part of the national Local Government Pension Scheme (LGPS) and is administered in-house at Southwark Council. The LGPS provides for the occupational pensions of employees, other than teachers, police officers and fire fighters, of local authorities. It is a contributory defined benefit (DB) scheme established by the Superannuation Act 1972. With 5.8 million members, 14,800 employers and assets of £275 billion, the LGPS is one of the largest DB schemes in the world, and the largest DB scheme in England and Wales.

Employer and employee contributions, together with investment returns generated from the Fund's investments make up the majority of income under the Fund. Contributions and other balances not immediately required to meet pension liabilities and other benefits are invested in a diverse range of investment assets.

The investment strategy for the Fund is determined by the Council, as the Administering Authority of the Fund, with advice from the Pensions Advisory Panel (PAP), but individual investment decisions are delegated to externally appointed investment managers.

The Fund's main objective is simple - to have sufficient resources available to meet all future pension entitlements of past and present employees. To ensure that sufficient resources are available to meet these liabilities, the Fund reviews the required contribution rates for all employers every three years following an actuarial valuation of the Fund. The 2019 triennial actuarial valuation was signed off on 31 March 2020 with revised contributions coming into effect on 1 April 2020. The valuation result of a 103% funding level continues to ensure stability of contributions going forward.

The aims of the Fund are to:

- Adequately fund benefits to secure the Fund's solvency and long-term cost efficiency, which should be assessed in light of the risk profile of the Fund and employers; and
- Seek to maintain overall employer contribution rates as nearly constant as possible (and subject to the administering authority not taking undue risks) at reasonable cost to the taxpayers, scheduled and admitted bodies.

The Fund is a mix of final salary benefits for service before 1 April 2014 and a Career Average Revalued Earnings (CARE) scheme for all service after 1 April 2014.

The pension services team has previously been regarded as a 'back office' function with limited investment in new technology and training. The recent appointment of a new pension manager and the restructure that followed his appointment has enabled a large amount of investment in staff and systems.

The team now has a dedicated training officer to train not just pension staff but also external employers; a dedicated communications officer to ensure all communications meet the highest possible standards and; a data team to ensure all pension system data is 'fit for purpose'.

A new high quality website has been built and includes a dedicated employer section, online forms for completion by employee and employer plus detailed guidance for employers.

The pensions function will be the first in London to have a contact centre embedded within it to be the first point of contact for all telephone enquiries.

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Pensions administration software is under review to ensure it is the best system available, and the pensions payroll system is moving from the Council's internal system to a new system directly controlled by the pension team. With these changes in place, the team can continue to strive to become the best pensions function in London.

### **Governance of the Fund**

With effect from 1 April 2015, all authorities that administer the LGPS are required to establish a Local Pensions Board (LPB), whose role is to assist in the good governance of the Fund. In many ways the Board have the same fiduciary duties that would be associated with pension scheme trustees. In addition, there is a National Scheme Advisory Board and two cost control mechanisms which seek to monitor and contain the overall cost of the LGPS at a national level.

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A highlighted risk last year was the number of significant changes to the wider pensions horizon. These remain areas of importance. However the most significant impact on the Fund during 2019-20 has been COVID-19. An ongoing assessment of the impact of the coronavirus pandemic on the Fund will be needed to ensure good governance. This is currently being addressed through the revised Investment Strategy Review. The effects of the COVID-19 pandemic will have a marked impact on market volatility and the Fund will face challenging times ahead during the recovery and renewal phase.

## REPORT FROM THE INDEPENDENT CHAIR OF THE LOCAL PENSION BOARD

Local Pension Boards were established under the 2013 Pensions Act. Each pension Administering Authority is required to establish a Board to assist with the effective and efficient governance and administration of the scheme. The Board is also tasked with ensuring compliance with the various legislative requirements and those of The Pensions Regulator, complementing the already well developed governance structure which underpins the pension scheme.

The independent Chair of the Local Pension Board attends the Pensions Advisory Panel (PAP). This provides a useful link between the advisory body and the Board. The link is further strengthened by the attendance at the Board of the Strategic Director of Finance and Governance on an ad hoc basis; attendance of other key officers and joint training sessions for the Board and PAP members.

### Terms of Reference, conflicts of interest, membership and attendance

The Board has now been in place for five years and has established itself as part of Southwark's governance structure in relation to the Fund. The Board's core functions are set out in the Terms of Reference at [www.southwark.gov.uk/council-and-democracy/pensions/local-pension-board](http://www.southwark.gov.uk/council-and-democracy/pensions/local-pension-board).

### Conflicts of interest

There were two potential incidents of conflict of interest arising during 2019-20. The first related to the re-appointment of the Chair. This was resolved by the exit from the meeting of the current Chair prior to the appointment vote. The second related to two employer representatives declaring an interest in the presentation on the actuarial valuation at the February 2020 meeting. The potential conflict related in particular to the employer contribution rates set from 1 April 2020.

The composition of the Local Pension Board is listed below.

Independent Chair	Mike Ellsmore
Scheme Member Representatives	Diana Lupulesc (employee representative) Neil Tasker (employee representative) Tony O'Brien (retired employee representative) Susan Murray (retired employee substitute)
Employer representatives	Dominic Cain (Vice Chair) (employer representative) Allan Wells (employer representative) Mike Antoniou (schools employer representative)

The Board meets quarterly and the current membership and attendance at meetings during 2019-20 is set out in the table on the next page. The Board agendas and minutes can be accessed at [www.southwark.gov.uk/council-and-democracy/pensions/local-pension-board](http://www.southwark.gov.uk/council-and-democracy/pensions/local-pension-board).

Name	Title/Company	10 April 2019	10 July 2019	9 October 2019	26 February 2020
<b>Mike Ellsmore</b>	Independent Chair	A	✓	✓	✓
<b>Diana Lupulesc</b>	Scheme Member Representative	✓	✓	✓	✓
<b>Neil Tasker</b>	Scheme Member Representative	A	✓	A	A
<b>Tony O'Brien</b>	Retired Scheme Member Representative	✓	✓	✓	A
<b>Susan Murray</b>	Substitute Retired Scheme Member Representative	A	A	A	✓
<b>Dominic Cain</b>	Employer Representative (Vice-Chair)	✓ (2)	✓	✓	✓
<b>Allan Wells (1)</b>	Employer Representative	NA	NA	NA	A
<b>Mike Antoniou</b>	Schools Employer Representative	✓	✓	✓	✓
<b>Fiona Dean (3)</b>	Substitute Employer representative	✓	NA	NA	NA

Notes

- (1) *Allan Wells joined the Board in January 2020*  
(2) *Dominic Cain (Vice Chair) chaired meeting*  
(3) *Fiona Dean: left the Board in April 2019*

- ✓ *Attended*  
× *Absent*  
A *Absent with apologies*

## Knowledge and understanding/training

As set out in the national guidance for Local Pension Boards, knowledge and understanding is a key part of being an effective Board member. Board members continuously engage in training programmes in order to develop and refresh their skills and knowledge and have access to The Pensions Regulator public service toolkit and the CIPFA guide for Local Pension Boards. The Board has undertaken briefing sessions and training on the Regulator's codes of practice and on actuarial valuations and moving forward into 2020-21 has agreed a new comprehensive training plan. A training needs analysis was conducted in 2019-20 to identify the training gaps of Board members and inform the training plan going forward.

## Work during the year

The Board commissioned Barnett Waddingham to conduct an independent assessment of the Fund's compliance with The Pensions Regulator's Code of Practice 14 (COP14). This was completed and reported to the Board in February 2020.

The report recognised that the Board had driven improvements in governance and acknowledged that many initiatives and substantive changes were already underway to improve the governance and performance of the Fund. As recommended, an action plan is being developed and the Board will monitor progress throughout 2020-21.

The Fund actuaries, Aon, presented the 2019 triennial actuarial valuation results to the Board in February 2020. The Board acknowledged the strong improvement in funding position between the 2016 and 2019 valuations.

The Board also received Pensions Advisory Panel agendas and continues to focus on particular areas of interest. During the year, the Board has considered:

- An ongoing review of the pensions administration function with continuing scrutiny of the development of key performance indicators;
- Investment Strategy Review;
- Progress on the London Collective Investment Vehicle (LCIV);
- Revised and updated Fund risk register; and
- Reviewing the progress of the LGPS good governance review commissioned by the Scheme Advisory Board and The Pension Regulator's engagement report on governance and administration risks.

## Future work

Looking ahead, our agenda will inevitably be dominated by the COVID-19 pandemic. To date the Fund has shown great resilience particularly with regard to the performance of the Fund's assets, funding levels and the effectiveness of the pension administration service.

The McCloud judgement will have a significant impact on the pension administration service and the service will need to be resourced adequately. The Board will keep a close watching brief on the implementation of McCloud.

The implementation of the governance review mentioned previously will also be closely monitored.

At national level, the Scheme Advisory Board has commissioned a review of governance in the LGPS. This has been put on hold during the pandemic but as it progresses the Board will monitor the outcomes from the review once finalised.

The skills and knowledge requirements of Board members continue to get more onerous and the Board will need to ensure that its members keep up to date.

## Expenses

The total expenses incurred by the Board for 2019-20 was **£21,301** analysed as set out below:

Allowance – Independent Chair	£2,882
COP14 Review	£11,000
Annual Insurance Fees	£5,040
Training	£1,330
Trade Union Allowance	£1,049
<b>Total</b>	<b>£21,301</b>



Mike Ellsmore  
Independent Chair, Southwark Local Pension Board



## GOVERNANCE POLICY AND COMPLIANCE

The Fund's Governance Compliance Statement is included at Appendix 6 of this report.

The Pensions Advisory Panel (PAP) meets quarterly and membership for 2019-20 comprised:

- Councillors:** Victoria Mills (*Chair*)  
Eliza Mann  
Jon Hartley (from October 2019)  
Peter Babudu (until May 2019)
- Officers:** Duncan Whitfield (*Strategic Director of Finance and Governance*)  
Officer with specialist knowledge of pensions finance and investments  
Officer with specialist knowledge of pensions administration
- Observers:** Chris Cooper (*Unison*) – *employee representative until May 2019. Retired employee representative from October 2019.*  
Karim Jalali (*GMB*) (*until May 2019*)  
Julie Timbrell (*from October 2019*) (1)  
Derrick Bennett (*from October 2019*)
- Advisers:** Susan Greenwood (*Mercer Ltd*)  
David Cullinan (*Independent Adviser*)

The table below shows attendance at meetings held during the year. The final scheduled meeting in March 2020 was postponed due to the COVID-19 pandemic and was rescheduled for 2020-21.

Meeting attendance 2019-20				
Name	Title/Company/Department	14 May 2019	22 October 2019	11 Feb 2020
Victoria Mills (Chair)	Elected member	✓	✓	✓
Eliza Mann	Elected member	A	✓	A
Jon Hartley	Elected member	✓	A	A
Duncan Whitfield	Strategic Director of Finance and Governance	✓	A	A
Officer with specialist knowledge of pensions finance and investments	Finance and Governance	✓	✓	✓
Officer with specialist knowledge of pensions administration	Finance and Governance	✓	✓	✓
Chris Cooper	Unison	✓	✓	x
Julie Timbrell (1)	Unison	NA	NA	✓
Karim Jalali	GMB	✓	NA	NA
Derrick Bennett	GMB	NA	NA	
David Cullinan	Independent Adviser	✓	✓	✓

Investment Advisers	Mercer	✓	✓	✓
Mike Ellsmore	Chair of Local Pension Board	✓	✓	A

Notes

- ✓ *Attended*
- ✗ *Absent*
- A *Absent with apologies*

## Knowledge and skills

As an Administering Authority of the LGPS, Southwark Council recognises the importance of ensuring that all staff and elected members charged with the financial management and decision making with regard to the Fund are fully equipped with the knowledge and skills to discharge duties and responsibilities allocated to them. It therefore seeks to appoint individuals who are both capable and experienced and it will provide training for staff and members of the PAP to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. Ongoing informal training was provided in quarterly PAP meetings to ensure members have an appropriate understanding of the recommendations they make to the Strategic Director of Finance and Governance.

During 2019-20 members of the PAP received training on specific work areas being considered. Training was provided on actuarial valuations in advance of the results of the 2019 triennial actuarial valuation being reported to PAP members.

Following the results of the 2019 actuarial valuation, an investment strategy review commenced. A training session was provided prior to the review being undertaken. This included the investment strategy review cycle, considerations and setting objectives, managing risk and application to the Fund.

Training was also provided on measuring the Fund's carbon footprint and the complexities involved in the measurement of some of the asset classes the Fund invests in.

A training session on LGPS pooling was provided. This covered an update on pooling and the work of the London Collective Investment Vehicle (LCIV). The advantages and difficulties of pooling were also covered.

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## MANAGEMENT AND FINANCIAL PERFORMANCE

### Scheme management and advisers

Advisers	Mercer Limited David Cullinan (Independent Adviser)
Actuary	Aon
Performance monitoring	PIRC Performance Analytics
Investment managers	BlackRock Advisors (UK) Ltd Newton Investment Management Limited Nuveen Real Estate Legal & General Investment Management Limited Brockton Capital LLP Frogmore Real Estate Partners Investment Managers Limited M&G Real Estate Invesco Real Estate Glennmont Partners Temporis Capital
Custodian	JP Morgan
Auditor	Grant Thornton
AVC providers	AEGON
Banker	RBS
Communications adviser	Concert, a Buck company

## Risk management

The Fund's risks are managed in accordance with the Council's risk management policy and strategy. In line with this strategy, the Fund maintains a risk register, which sets out the controls in place to manage the risks identified. The key risks facing the Fund are:

Risk description	Risk category	Risk controls (mitigation)
The Fund's asset allocation strategy is not sufficient to meet obligations and liabilities.	Financial	<p>Reports on the funding level are produced quarterly by the Fund Actuary and reviewed by the Pensions Advisory Panel (PAP).</p> <p>An investment strategy review is conducted following each triennial actuarial valuation, to determine optimal asset allocation for the Fund.</p> <p>Actual asset allocation is reported to the PAP on a quarterly basis, with variances of actual allocation to target discussed.</p> <p>The Fund holds investments in assets, the value of which are linked to inflation, a key driver of pension liabilities, such as index linked gilts</p>
Employer data is inaccurate or contributions received late creating a financial or regulatory risk to the Fund.	Financial	<p>Administration strategy sets out the roles and responsibilities clearly and consequences of non-compliance and communication strategy ensures employers reminded of information required.</p> <p>Regular monitoring of contributions and verification of monthly returns.</p> <p>Rollout of the iConnect portal allows employers to efficiently upload information directly to the Fund with automatic verification checks.</p> <p>New pension services structure includes a specialist data management team.</p>
Failure of third party providers of investment management and custodial services, including London Collective Investment Vehicle (LCIV), could have a serious financial impact on the Fund.	Financial	<p>Contracts are monitored regularly.</p> <p>PAP is provided with quarterly information for each manager. Where there are concerns additional monitoring is put in place to ensure financial risks are kept to an acceptable level.</p>

Risk description	Risk category	Risk controls (mitigation)
		<p>Third parties provide Fund with an annual SAS70 (or equivalent) report which provides assurance from their auditors that adequate controls are in place and are operating effectively.</p> <p>Assets will be transferred to the LCIV only upon satisfactory business case and due diligence.</p>
<p>COVID-19 pandemic impacts Fund performance and income from investments, resulting in a reduction in Fund value and impact on ability to pay pensions.</p>	<p>Financial</p>	<p>Ongoing monitoring of Fund performance and investment markets.</p> <p>Advice obtained from investment advisers on continuing suitability of asset allocation.</p> <p>Review of pre-pandemic decisions on investment strategy changes.</p> <p>Review of scheme employers' financial strength and likelihood of exit. The Fund holds investments in diversified assets, reducing volatility and ensuring long-term stability.</p> <p>Cash flow monitored on a regular basis. Investment income reinvested and not required to pay pensions.</p>
<p>Employers fail to provide information that Fund requires resulting in poor service, increased complaints and possible fines and penalties.</p>	<p>Reputational</p>	<p>Employer/HR function going through business transformation exercise, with emphasis on more robust processes and better understanding of fund requirements.</p>
<p>Reliance on a smaller pool of specialist staff across LGPS impacts on ability to recruit and retain staff.</p>	<p>Staffing and culture</p>	<p>Use of external advisers with specialist knowledge.</p> <p>Develop and implement training programmes to help ensure staff are equipped with appropriate skills and knowledge and to show recognition of value placed on them.</p>

The Fund's biggest overall risk (as identified above) is that its assets fall short of its liabilities resulting in there being insufficient funds to pay benefits to members as they fall due. The investment objectives have

been set with the aim of maximising investment returns over the long term within specific risk tolerances. This aims to optimise the likelihood that the promises made regarding members' pensions and other benefits will be fulfilled.

The Strategic Director of Finance and Governance (SDFG) has overall responsibility for all aspects of the administration and investments of the Fund. The Pensions Advisory Panel (PAP) act in their role as advisers to the SDFG, taking into account the advice they receive from the Fund's external advisers. They make recommendations to the SDFG on matters relating to the management of the Fund. The management of risks is a key factor in all recommendations made by the Panel, thereby ensuring any risks to the Council arising from the Fund are kept to an acceptable level.

The investment adviser and performance measurement provider carry out the following evaluations which are reviewed by the PAP on a quarterly basis:

- Independent evaluation and analysis of Fund performance;
- Reviewing benchmarks and asset allocation; financial markets review; and
- Reviewing changes in the investment managers' business (through manager ratings).

Investments are monitored to ensure they are compliant with the LGPS regulations.

All the Fund's assets are managed by external investment managers. They are required to provide an audited internal controls report annually to the Fund, which sets out how they ensure the Fund's assets are managed in accordance with their Investment Management Agreement. A range of investment managers have been appointed to diversify manager risk. The Fund's assets are held for safekeeping by the custodian (who also provides independent valuations of the Fund's investments).

The Funding Strategy Statement was reviewed in January 2020 and sets out the key risks (including demographic, regulatory and governance) to not achieving full funding in line with the strategy. The Actuary reports on these risks at each triennial actuarial valuation and more regularly if circumstances require. The last triennial actuarial valuation was completed on 31 March 2019.

## Financial performance

During 2019-20 the Fund decreased in value by £60 million (3.7%) to £1,582 million. A detailed analysis of the movement can be found in the Statement of Accounts for the Fund as Appendix 2 of this report, and is summarised below.

	2017-18 £000	2018-19 £000	2019-20 £000
<b>Opening net assets</b>	<b>1,494,992</b>	<b>1,530,947</b>	<b>1,641,986</b>
Contributions and joiners	54,711	58,891	65,787
Benefits and leavers	(59,400)	(64,076)	(71,384)
Investment income less taxes	14,470	15,432	15,287
Management expenses	(6,422)	(7,508)	(8,881)
Profit on sale and change in investment value	32,596	108,300	(61,254)
<b>Increase in Fund value</b>	<b>35,956</b>	<b>111,039</b>	<b><u>(60,445)</u></b>
<b>Closing net assets</b>	<b>1,530,947</b>	<b>1,641,986</b>	<b>1,581,541</b>

During the year, the net cash flow from membership (contributions and joiners, less benefits paid and leavers) was negative, a net reduction of £5.6 million. The overall membership has increased slightly over the last twelve months. The Fund has matured over the last five years, with deferred and pensioner members increasing. Contributions from active members remain stable. There was a large increase in transfers in during 2019-20 (£10.6 million in 2019 compared to £2.7 million in 2018-19).

During 2019-20 there was a decrease in Fund value of 3.7%, compared to the previous year's increase of 7.3%. The decrease was due to the large movements in investment values in the final quarter due to the impact of the global pandemic. The Investment Policy and Performance section provides more detailed analysis of investment performance over the year.

## INVESTMENT POLICY AND PERFORMANCE

### Investment policy

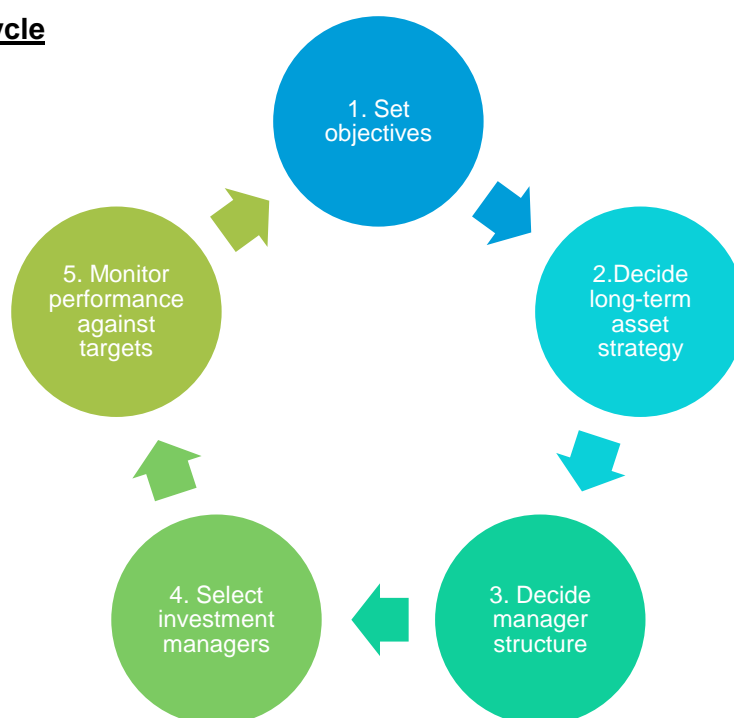
The Fund is managed with regard to a strategic asset allocation benchmark. This is reviewed every three years, following the Fund's triennial actuarial valuation. The strategic asset allocation is set to provide the required return, over the long-term, to ensure that all pension payments can be met. The actual asset allocation may differ from the strategic benchmark within tolerances that are agreed by the Pensions Advisory Panel (PAP) on the advice of the Fund's investment advisers. The distribution of investments is reported to PAP quarterly and monitored monthly by the investments team.

The Fund's investment objective is to support an investment strategy and structure which incorporate an appropriate balance between risk and return considering the Fund's specific liabilities. In doing this, the investment strategy reviews both manager performance and long-term allocation between various asset classes as returns between these classes can vary significantly.

The Funding Strategy Statement (FSS) and the Investment Strategy Statement (ISS) set out the Fund's policies on funding and investments. The FSS is included as Appendix 3 of this report and the ISS as Appendix 4.

The ISS sets out the investment strategy of the Fund, provides transparency in relation to how the Fund investments are managed, outlines the Fund's approach to managing risk, how environmental, social and governance (ESG) issues are taken into account and the approach with regard to pooling of investments.

### The investment strategy cycle



The ISS sets out the Fund's strategic asset allocation with a target benchmark allocation for each asset class as set out in the table on the next page.



Asset class	Strategic allocation %	Investment style %	Maximum allocation %	Role (s) within the strategy
<b>Equity</b>	50	Passive 40.0	65	Expected long-term growth in capital and income in excess of inflation over the long term.
		Active 10.0		
<b>Diversified Growth</b>	10	Active 10.0	20	Primarily for diversification from equities. Equity like returns over time with a lower level of risk.
<b>Absolute Return Fixed Income</b>	5	Active 5.0	10	Diversified approach to fixed income investing which is not dependent on the direction of interest rates.
<b>Index Linked Gilts</b>	10	Passive 10.0	40	Low risk (relative to the liabilities) asset that provides inflation linked income and protection from falling interest rates.
<b>Property</b>	20	Core UK Property 14.0	30	Provides diversification from equities and fixed income. Generates investment income and provides some inflation protection.
		Pooled Fund 6.0		
<b>Sustainable Infrastructure</b>	5	Limited Partnership 5.0	10	Asset class provides additional diversification from traditional asset classes. Generates sustainable, reliable income with significant linkage to inflation. Provides risk mitigation from declining fossil fuel usage.

The financial assumptions specified in the FSS are consistent with those in the ISS. The council's FSS documents these specific processes and:

- Establishes a clear and transparent fund-specific strategy;
- Supports the requirement for maintaining as nearly constant primary employer contribution rates as possible;
- Sets contributions as to ensure the solvency and long term cost efficiency of the Fund;
- Ensures that regulatory requirements regarding the setting of contributions are met; and
- Takes a prudent longer-term view of funding the Fund's liabilities.

The ISS and FSS are reviewed following the Fund's triennial valuation to ensure that investment objectives are aligned to the Fund's valuation. Updates are also undertaken on an ongoing basis to reflect any changes agreed by the PAP.

The actuarial valuation as at 31 March 2019 showed the Fund's assets covered 103% of liabilities compared with 88% at the previous valuation as at 31 March 2016. The discount rate for the three years' commencing 1 April 2020 has been set at 4.05% per year.

### Effect of the COVID-19 pandemic on investment returns

During the quarter to March 2020 the Fund value fell by 11% due to the effects on investment markets of the COVID-19 pandemic. The Fund's performance was impacted by its heavy weighting to global equities, which reflected the FTSE All World return for the quarter of -16%.

Following the results of the 2019 triennial actuarial valuation, a review of the Fund's investment strategy began. Decisions were made regarding changes to the Fund's investments. The agreed changes will be implemented during 2020-21 and will be subject to ongoing monitoring and review with regards to the continuing expected volatility in the investment markets.

### Investment asset and manager allocations

Asset class	Manager	31-Mar-19	31-Mar-20	31-Mar-20	Strategic benchmark	Difference
		£m	£m	%	%	%
Global Equity	BlackRock	349.3	321.6	20.9	20	0.9
	Legal & General	367.3	329.8	21.4	20	1.4
	Newton	172.4	165.9	10.8	10	0.8
<b>Total Global Equity</b>		<b>889.0</b>	<b>817.3</b>	<b>53.1</b>	<b>50</b>	<b>3.1</b>
Diversified Growth	BlackRock	167.5	163.0	10.6	10	0.6
<b>Total Diversified Growth</b>		<b>167.5</b>	<b>163.0</b>	<b>10.6</b>	<b>10</b>	<b>0.6</b>
Absolute Return Bonds	BlackRock	124.8	120.8	7.9	5	2.9
<b>Total Absolute Return Bonds</b>		<b>124.8</b>	<b>120.8</b>	<b>7.9</b>	<b>5</b>	<b>2.9</b>
<b>Total Fixed Interest Gilts</b>		<b>8.0</b>	<b>6.2</b>	<b>0.4</b>	<b>0</b>	<b>0.4</b>
Property	Nuveen	243.0	195.7	12.7	15	-2.3
	M&G	21.7	22.4	1.5	1.5	0
	Invesco	14.6	15.0	1.0	1.5	-0.5
	Frogmore	7.7	8.8	0.6	1	-0.4
	Brockton	3.1	4.2	0.3	1	-0.7

<b>Total Property</b>		<b>290.1</b>	<b>246.0</b>	<b>16.1</b>	<b>20</b>	<b>-3.9</b>
Sustainable Infrastructure	Glennmont	0	11.7	0.8	2	-1.2
	BlackRock	0	0	0	1.5	-1.5
	Temporis	0	20.1	1.3	1.5	-0.2
<b>Total Sustainable Infrastructure</b>		<b>0</b>	<b>31.8</b>	<b>2.1</b>	<b>5</b>	<b>-2.9</b>
Index Linked Gilts	BlackRock	66.2	68.1	4.4	5	-0.6
	Legal & General	83.4	85.4	5.5	5	0.5
<b>Total Index Linked Gilts</b>		<b>149.6</b>	<b>153.5</b>	<b>9.9</b>	<b>10</b>	<b>-0.1</b>
Derivatives	Newton	0.1	0.2	0.0	0	0.0
<b>Total Derivatives</b>		<b>0.1</b>	<b>0.2</b>	<b>0.0</b>	<b>0</b>	<b>0.0</b>
<b>Total</b>		<b>1,629.1</b>	<b>1,538.8</b>	<b>100</b>	<b>100</b>	<b>0</b>

As at 31 March 2020, the actual asset allocation for equities was 53.1%, slightly overweight to benchmark by 3.1% as were absolute returns bonds at 2.9%, and property was underweight to its target allocation by 3.9% (compared with 2.2% at 31 March 2019). All were well within the agreed tolerances.

Allocations for sustainable infrastructure are moving prudently towards the 5% target. However, COVID-19 has impacted on acquisition opportunities for these investments and it is expected that further capital calls will be made during 2020-21. As part of the ongoing investment strategy review, the Fund will continue to be rebalanced back to the strategically agreed benchmarks.

### **Commitment to reducing fossil fuel exposure**

In December 2016, the Fund's investment strategy explicitly committed to reduce over time its investment exposure to fossil fuels. Southwark was one of the first LGPS funds to make such a commitment and placed the Fund at the forefront of sustainable fossil fuel aware investment.

Since then, the Fund has made significant progress toward this long-term ambition, as set out below. In September 2017, the Fund agreed a long-term plan for the reduction of investment exposure to fossil fuels. This plan set out the goals and objectives for the Fund over the long-term.

The Fund's implementation period for fossil fuel reduction is split into three main time horizons, encompassing short, medium and long-term objectives.

- The short term: one-four years (2017-2021);
- The medium term: four-ten years (2021–2027); and
- The long-term: beyond ten years (2027+).

The plan is separated into four key areas of focus and consideration for the Fund:

- Investment Strategy and Actuarial Valuation;
- Fund Management and Implementation;
- Local Authority Collaboration and Pooling; and
- Engagement.

The Fund has made significant progress to date in implementing the plan for a reduction in fossil fuel investment. This includes the decision as part of the investment strategy review, following the 2016 triennial actuarial valuation, to introduce a new 5% target allocation to sustainable infrastructure. The first investment as part of this 5% allocation was agreed in March 2018, with a £30 million commitment to Glennmont Clean Energy Fund Europe III. This Fund invests in a range of on and off shore wind farms, solar farms and bio energy across the UK and Europe.

During 2019-20, the PAP reported that significant progress had been made to reducing investment in fossil fuels- a commitment of £600 million in low carbon or fossil fuel exclusionary equities together with the 5% allocation to the three new renewable energy infrastructure funds, leading to an estimated reduction in carbon footprint of just under 40% since 2017.

As part of the investment strategy review, the PAP considered a refreshed fossil fuel divestment approach during 2019-20. The refreshed strategy set out the principles that underpin the Fund's approach to divestment from fossil fuels; the action already taken by the Fund to analyse, understand and reduce fossil fuel investment exposure across the entire portfolio and future targets for reducing and ultimately eliminating carbon and fossil fuel exposure for the Fund.

It is important that the Fund allows time for these substantial changes to the investment portfolio to be monitored and assessed in terms of their impact upon return and volatility implications, risk profile as well as the carbon footprint for the Fund.

As part of this strategy, the Fund is fully committed to collaboration with other local authority partners and in 2015 invested in the London Collective Investment Vehicle (LCIV). The LCIV is a collaborative venture between local authorities to deliver benefits of investment scale and efficiency to the participating Funds. Southwark is committed to engaging with the LCIV to move it forward in relation to fossil fuel divestment. The Fund will continue to support the development of the LCIV as an investment vehicle and as at 31 March 2020, 52% of the assets of the Fund were under the oversight of the LCIV.

### **Carbon footprint measurement**

A comprehensive carbon footprinting review of all assets in the fund was undertaken as at 31 December 2019. The Fund has elected to measure fossil fuel exposure through carbon footprinting, which is the most commonly used metric for assessment. This metric seeks to assess the carbon footprint of an underlying investment, which can be attributable to the Fund's specific investments. For example, the greenhouse gas (GHG) emissions of a particular company can be apportioned to equity investors based upon their proportional equity share of that company.

This assessment is easier to perform for listed equities, due to the wide availability of company specific data, but has been extended to analyse other asset classes within the portfolio. The exception to this assessment is for the 10% allocation to UK Government index linked bonds.

In order to carry out this specialist portfolio assessment, the Fund initially engaged TruCost and then subsequently Sustainalytics. Both companies have significant experience in climate change and investment portfolio data. The initial assessment was calculated as at 30 September 2017. This provided the Fund with a starting point for this journey, such that over the long-term the Fund can monitor the incremental progress made to reduce the overall portfolio exposure. An updated portfolio assessment was carried out by Sustainalytics as at 31 December 2019 and this confirmed that the carbon footprint of the Fund had reduced by 38% since the initial assessment.

The Fund will continue to develop and enhance the accuracy of this portfolio assessment over time. For example it will be possible to gain greater clarity over the Fund's property portfolio with the provision of more detailed energy and water usage. Due to the Fund's investment strategy of developing and renovating property to high standards of energy efficiency it is likely that this assessment will provide further evidence

of the benefit of the Fund's significant property allocation as a mitigation of the fossil fuel risk in other areas of the portfolio.

The Fund's carbon footprint will be further reduced as the commitments to the three sustainable infrastructure funds are drawn down. The operational assets of these funds will benefit from carbon dioxide offsets. This is based on the assumption that clean energy is carbon dioxide emission-free and when compared to the relevant grid's carbon intensity, carbon offset value can be calculated.

One of the changes agreed in the investment strategy is a new 5% allocation to blended alternatives. Suitable investments will be identified which meet the Fund's objective of further reducing fossil fuel exposure over time. This new allocation will be funded by the overweight position in equities.

## **Investment environment and performance**

At the start of the financial year global equity markets were returning around 6% with US equities returns at 7%. Europe performed best at 9% whilst Japan and emerging markets lagged. The UK returned just 3.3% primarily due to political uncertainty and the prospect of a no-deal Brexit at the end of October. Bond returns were low, and sterling continued to depreciate. The longer term outlook was also positive with expected one year returns of 7% and three year returns approximately 10% per year.

During the quarter to September 2019, global equity markets were returning 3.5% in sterling, and US equities returned 4.9% in sterling terms; fiscal easing continued and there were some signs of the US and China keeping trade negotiations going which reassured investors and markets. By the end of Q4 2019, all three quarters of the financial year had seen stock markets rise.

At the start of 2020, stock markets were continuing to rise. But this soon changed as the fears of the impact of COVID-19 saw world stock markets falling. With the world's major economies entering 'lockdown' at differing stages, fears of a severe recession saw markets hit lows last seen during the financial crisis in 2008.

Global equity markets fell sharply by around 16%, the worst quarterly returns in over a decade. US equities returns fell by 14% as monetary and fiscal stimulus could not offset investors' concerns about sudden collapse in economic activity and earnings.

European equities fell by 17.5% as the region in the early stages of the pandemic had been worst affected by COVID-19. Emerging markets fell by 19% in sterling terms, as there was market nervousness over how emerging market companies would cope with the pandemic as well as oil price shock on oil producing countries.

All bond benchmark yield curves shifted down significantly following the central banks loosening monetary policy. Yields for all durations were now below 1%. This was a reaction to the Bank of England cutting short dated rates close to zero as well as low to negative growth expectation.

Although governments have intervened and initiated emergency fiscal measures to reduce the impact of the pandemic, it is difficult to predict the pace of recovery in the markets. What can be predicted is that a level of volatility has returned. Equity and bond markets rise and fall driven by short-term influences but also longer-term outlooks, as well as how governments intervene in the markets. The range of potential economic outcomes is huge.

## **Southwark Fund performance**

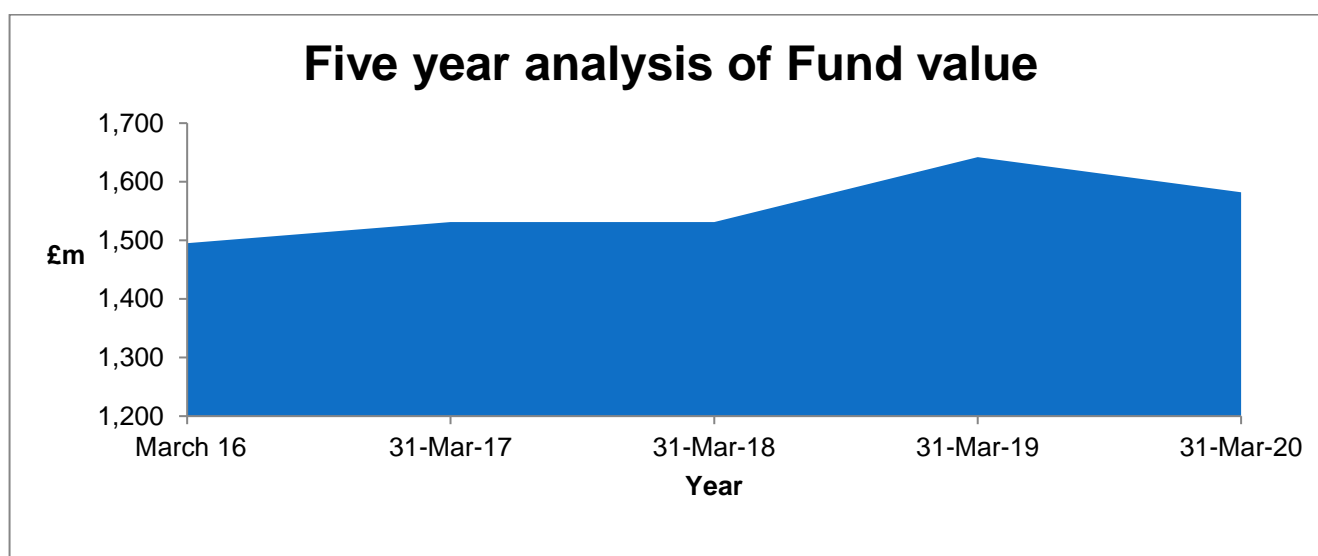
The year to March 2020 has been unprecedented due to the impact of the pandemic which has affected all aspects of normal life. Similarly, COVID-19 has impacted on the financial markets and on pension fund returns. The quarter to March 2020 experienced returns retreating sharply for all LGPS pension funds.

Prior to the quarter to 31 March 2020, the Fund was performing well. The Fund returned 4.4% over the quarter to June 2019 and the one year average performance to December 2019 was showing a return of 15.4%, 1.4% over the strategic benchmark and returning between 8% and 10% over the three and five year periods.

By the end of December 2019, the Fund was valued at £1,753 million, an increase of 7% from the start of the year. But against a global fall in investment markets in the final quarter to March 2020, the Southwark Fund fell by 11.8% to £1,557 million.

This global event had a significant impact on the Fund's return over the 2019-20 financial year, with a negative return of 2.8% for the year to March 2020. However, the medium term performance for the Fund is steady at between 3% per year and 6% per year and over 10 years delivered close to 8% per year.

Markets have shown strong signs of recovery since March 2020. But it is likely this will be subject to volatility in the short term, given worldwide economic uncertainty.



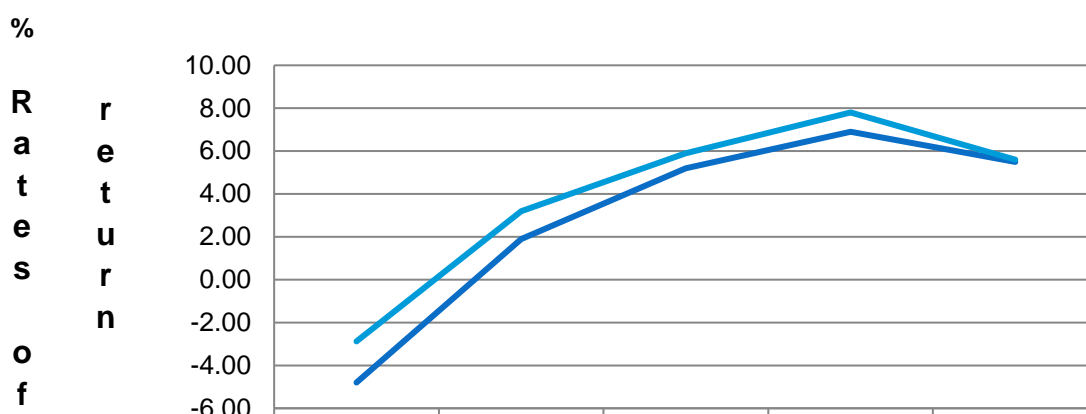
## Performance relative to other LGPS funds

Asset class	Return 2019-20 (Fund) %	Local authority average return (*) %	Over/(Under) performance %	Ranking (percentile)
Total Fund	-2.8	-4.8	2.0	25
Equities	-4.9	-12.5	7.6	10
Property	1.2	1.7	(0.5)	38

Source: Local Authority Pension Performance Analytics (LAPPA) July 2020

The LAPPA LGPS Universe comprised of 63 funds at the end of March 2020. The LGPS universe was valued at £180 billion.

## Pension fund rates of return over 20 years



	1 year	3 year	5 year	10 year	20 year
— Average LA fund return (63 funds)	-4.80	1.90	5.20	6.90	5.50
— Southwark average fund return	-2.88	3.20	5.90	7.80	5.60

LGPS funds averaged a 4.8% fall over the 2019-20 financial year, due to the market falls in March 2020. Returns over the longer term are better than perhaps could be expected at an average return of 6.9%. Relative to other LGPS funds, the Southwark Fund performed above the one year local authority average with a return of -2.8%. The Fund has consistently outperformed other local authority pension funds over a 20 year period.

Asset class	Rank - percentile				
	1 year	3 years	5 years	10 years	20 years
Total Fund	25	13	17	10	26
Equities	10	19	15	15	30
Property	38	6	20	19	25

Source: Local Authority Pension Performance Analytics (LAPPA) July 2020

The LAPPA LGPS Universe comprised of 63 funds at the end of March 2020. The LGPS Universe was valued at £180 billion.

The Fund's performance was ranked in the top third of results over every period. The Fund achieved well above average results in equities, ranking at the 10<sup>th</sup> percentile as a result of its prudence and good governance, driven by strong manager performance within equities and property.

The Southwark Fund has historically been a big investor in equity, adopting a balanced structure that targets growth but stability and future proofing through investments in real assets and a broad mix of investments. Property showed a small increase over the year of 1.2%, which, although below the 1.7% mean average, was still within the top 40% quartile.

## Investment performance – fund manager performance

The benchmarks used to measure performance and the targets set are as follows:

Asset class	Manager	Manager allocations as at 31 March 2020	Strategic benchmark	Target return
		%	%	
Global Equity	BlackRock	20.7	20	Track the relevant index
	Legal & General	21.2	20	Track the relevant index
	Newton	10.9	10	FTSE All World +3% net of fees
<b>Total Global Equity</b>		<b>52.8</b>	<b>50</b>	
Diversified Growth	BlackRock	10.5	10	LIBOR +3.5%
<b>Total Diversified Growth</b>		<b>10.5</b>	<b>10</b>	
Absolute Return Bonds	BlackRock	7.8	5	LIBOR +4%
<b>Total Absolute Return Bonds</b>		<b>7.8</b>	<b>5</b>	
Property	Nuveen	13.7	15	7% on a rolling basis
	M&G	1.4	1.5	6%-8%
	Invesco	1	1.5	7%-9% net of fees
	Frogmore	0.6	1	15%-18% gross IRR
	Brockton	0.3	1	18.8% (gross), 15% (Net)
<b>Total Property</b>		<b>17</b>	<b>20</b>	
Sustainable Infrastructure	Glennmont	0.8	2	10%-11%
	BlackRock	0	1.5	12%-13% IRR (9-10% net)
	Temporis	1.1	1.5	9% ( or higher) net of fees
<b>Total Sustainable Infrastructure</b>		<b>1.9</b>	<b>5</b>	
Index-Linked Gilts	BlackRock	4.4	5	Track the relevant index
	Legal & General	5.5	5	Track the relevant index
<b>Total Index Linked Gilts</b>		<b>9.9</b>	<b>10</b>	



The table below sets out the performance of each investment manager against benchmark over one, three and five year periods to 31March 2020.

<b>Investment manager</b>		<b>1 YEAR</b>	<b>3 YEARS</b>	<b>5 YEARS</b>
		<b>%</b>	<b>%</b>	<b>%</b>
BlackRock Balanced	Portfolio	-13.5	1.9	6.5
	Benchmark	-13.5	1.7	6.4
	<b>Relative</b>	<b>0.0</b>	<b>0.2</b>	<b>0.2</b>
Newton Equities	Portfolio	-4.3	3.0	7.5
	Benchmark	-3.9	4.7	9.3
	<b>Relative</b>	<b>-0.4</b>	<b>-1.7</b>	<b>-1.8</b>
Nuveen	Portfolio	-2.5	8.5	7.8
	Benchmark	-1.2	6.9	7.4
	<b>Relative</b>	<b>-1.3</b>	<b>1.6</b>	<b>0.4</b>
Legal & General	Portfolio	-3.2	3.0	7.5
	Benchmark	-4.8	2.0	6.8
	<b>Relative</b>	<b>1.6</b>	<b>1.0</b>	<b>0.7</b>
BlackRock Dynamic Diversified Growth Fund	Portfolio	-2.9	0.8	N/A
	Benchmark	3.8	4.0	N/A
	<b>Relative</b>	<b>-6.7</b>	<b>-3.2</b>	<b>-</b>
BlackRock Absolute Return Bond Fund	Portfolio	-3.2	N/A	N/A
	Benchmark	4.8	N/A	N/A
	<b>Relative</b>	<b>-8.0</b>	<b>-</b>	<b>-</b>
Brockton Capital	Portfolio	2.8	8.3	N/A
	Benchmark	15.0	15.0	N/A
	<b>Relative</b>	<b>-12.2</b>	<b>-6.7</b>	<b>-</b>
Invesco Real Estate	Portfolio	2.4	0.1	N/A
	Benchmark	8.0	8.0	N/A
	<b>Relative</b>	<b>-5.7</b>	<b>-7.9</b>	<b>-</b>
M&G Investments	Portfolio	2.8	3.8	N/A
	Benchmark	8.0	8.0	N/A
	<b>Relative</b>	<b>-5.2</b>	<b>-4.2</b>	<b>-</b>

Frogmore	Portfolio	11.9	0.6	N/A
	Benchmark	16.5	16.5	N/A
	<b>Relative</b>	<b>-4.6</b>	<b>-15.9</b>	<b>-</b>
BlackRock Global Renewable Power	Portfolio	N/A	N/A	N/A
	Benchmark	N/A	N/A	N/A
	<b>Relative</b>	<b>-</b>	<b>-</b>	<b>-</b>
Glennmont Clean Energy Fund III	Portfolio	-43.8	N/A	N/A
	Benchmark	11.5	N/A	N/A
	<b>Relative</b>	<b>-55.3</b>	<b>-</b>	<b>-</b>
Temporis Operational Renewable Energy fund	Portfolio	N/A	N/A	N/A
	Benchmark	N/A	N/A	N/A
	<b>Relative</b>	<b>-</b>	<b>-</b>	<b>-</b>
Total Fund	Portfolio	-2.8	3.2	5.9
	Benchmark	-1.8	3.5	6.6
	<b>Relative</b>	<b>-1.0</b>	<b>-0.3</b>	<b>-0.7</b>

*N/A-Performance figures are shown where the manager has been invested for the relevant period.*

Prior to the quarter to 31 March 2020, the Fund was performing well and above benchmark and returns were improving overall with an outperformance of 0.7%. Newton produced the best absolute return whilst the fund's real estate assets delivered in the region of 2%. But positive returns globally were wiped out in the quarter to March 2020. Global equities retreated by approximately 16% and inevitably this is reflected in the fund managers' one year performance figures.

The fund's equity managers, Newton, Legal and General and BlackRock, were all subject to negative returns over the year, mirroring the downward trend in global markets, but performing broadly in line with their benchmark. At the start of 2019-20, in the quarter to June 2019, Newton outperformed the benchmark with returns of 7%, and a full year return of 14%. BlackRock and Legal and General also delivered strong performance in this quarter.

The Fund's segregated property mandate at the start of the year was positive and showing a 1.4% return above the rolling target of 7% over seven years. Nuveen returns in the final quarter were negative, driven by falls in capital value but achieved over the full year a positive return, and outperforming benchmark over the three and five year periods.

Frogmore, M&G and Invesco property pooled fund investments have underperformed their benchmarks over one year. However, these funds are progressing in their acquisition of assets. This current phase of growth will lead to the implementation of asset management initiatives as the primary means of increasing fund values.

BlackRock's dynamic diversified growth fund outperformed its target in the quarter to June 2019. By September performance was muted amid global uncertainty driving down government bond yields. It outperformed its benchmark over the quarter to 31 December, and outperformed over one and three years. In the final quarter to 31 March 2020, the Fund value fell due to a drop in equities and exposure to corporate

bonds, but achieved outperformance over a three year period. Similarly BlackRock's absolute return bond fund outperformed its target in all three quarters to December 2019 but by the end of the financial year had underperformed its benchmark.

The Fund's large commitment to property, as well as its holdings in absolute return bonds and diversified growth, has been effective at reducing volatility, which moving forward to recovery will become increasingly important. A large proportion of the Fund being in property has helped preserve overall fund value.

### **Total Fund performance relative to liabilities**

The Fund has slightly outperformed compared with index-linked gilts over a three year period but showed an expected underperformance over the one year period (-5.2%) and in the final quarter (-12%).

Performance	3 months %	1 year %	3 years (% p.a.)
Total Fund	-10.1	-2.8	3.2
Index Linked Gilts	1.9	2.4	2.9
<b>Relative</b>	<b>-12</b>	<b>-5.2</b>	<b>0.3</b>
Liability Target - Aon Hewitt	1	4.1	4.1
<b>Relative</b>	<b>-11.1</b>	<b>-6.9</b>	<b>-0.9</b>

Source: Mercer Investment performance report quarter to 31 March 2020

The target liability return shown is the 4.1% per year required as per the 2019 valuation. As at 31 March 2020, the Fund produced a return below that assumed by the Actuary. However, this is a snapshot at 31 March 2020, when global markets had plummeted in response to the impact of the pandemic.

Fund performance as at 31 December 2019

Performance	3 months %	1 year %	3 years (% p.a.)
Total Fund	0.7	15.4	8.4
Index Linked Gilts	-9.4	6.8	2.9
<b>Relative</b>	<b>10.1</b>	<b>8.6</b>	<b>5.5</b>
Liability Target - Aon Hewitt	1	4.1	4.1
<b>Relative</b>	<b>-0.3</b>	<b>11.3</b>	<b>4.3</b>

Source: Mercer Investment performance report quarter to 31 December 2019

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The picture at 31 December 2019, prior to the pandemic demonstrates strong performance in the first three quarters of the year. At this point, the Fund outperformed index-linked gilts over the final quarter of 2019 by 10%, and over the one and three year periods to 31 December 2019 by almost 9% and 6% respectively.

Global markets have started to recover from the position at 31 March 2020. Given the uncertainty and volatility in the markets, the position on the target rate of return will be reviewed together with a renewed investment strategy to ensure that the Fund will meet its liabilities over the longer term.

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## SCHEME ADMINISTRATION

### Value for money statement

Southwark Pension Services has finished its restructure, with only one or two posts still to be filled. With the majority of staff in-post the section is moving away from the outdated and outmoded systems and processes it has been using for the last two decades.

A new website has been created that will, over the next year, be expanding to allow employers and members greater access to pensions information.

The roll out of i-Connect (a system that allows employers to interface pensions data to the pensions system) has been a huge success, with data on 96% of relevant employees now being routinely received.

Engagement has begun with Southwark Councils telephone contact centre to roll out the same first point of contact system for anyone ringing into the pensions section. This ensures that all calls are answered speedily with operators either resolving the query immediately, or escalating the enquiry back to the pensions team.

It is planned to bring pensioner payroll back under Fund control in 2021.

Additionally, we are moving to a remote scan and post solution. This will allow us to accurately measure the amount of paper that we use and our aim is to reduce the amount of paper used significantly.

### Summary of activity

#### Data quality

Work commenced in early 2017 to implement i-Connect software and roll it out to schools and other external employers, enabling them to submit their monthly pension returns online.

The system is now fully rolled out with 96% of relevant employees having their data submitted electronically. This allows the data team to aggressively interrogate data to identify and raise anomalies or data gaps with schools and other employers.

Higher levels of data quality allow the pension administration team to progress casework significantly faster than before with less need to contact employers directly.

#### Technology/security

The pensions system used by Southwark Council has now moved into its new cloud hosted environment which provides a higher level of security for the data held there. Our software provider fully complies with the government backed Cyber Essentials Scheme.

The new website has been penetration tested where two minor issues were identified that have now been resolved. The new website is only the beginning of our digital journey where we plan to communicate and engage more effectively with all members and employers.

#### Staffing/structure

The main restructure has now been completed and the section is fully functional again.

The new structure broadly consists of three specialist teams - pension administration, projects/technical and data management.

More details can be seen at [www.southwarkpensions.co.uk/organisation-structure](http://www.southwarkpensions.co.uk/organisation-structure).

The new Data Manager has been instrumental in the roll out of i-Connect with the main council payroll also making submissions through the system.

With all pension data now arriving electronically, the data team are able to interrogate the data, identifying and raising any problems immediately.

On data management, The Pensions Regulator (TPR) has stated:

***'Failure to maintain complete and accurate records means you are at risk of not meeting your legal obligations. Poor record-keeping can have a huge impact on members and can be very expensive for your scheme if things go wrong due to bad or missing data.'***

It is extremely important that records are as complete as possible. TPR has provided guidance at [www.thepensionsregulator.gov.uk/en/trustees/managing-db-benefits/governance-and-administration/record-keeping](http://www.thepensionsregulator.gov.uk/en/trustees/managing-db-benefits/governance-and-administration/record-keeping)

The new members of the pension administration team have now been trained and this has enabled the team to cover all business as usual work. Some minor backlogs of work had built up but in-house training means that any backlogs will be fully resolved within the next few months.

## **Member communication**

A new website ([www.southwarkpensions.co.uk](http://www.southwarkpensions.co.uk)) has been built in conjunction with Concert, a Buck company. This website looks cleaner and more professional than the majority of other LGPS fund websites and is now live.

Phase two of the website build will bring more functionality to include a news feed so members and employers can see real time changes within the pensions industry.

Phase three will be an employer's section of the website where employers will be able to complete online forms securely (rather than submitting paper forms to us) which will further smooth the transition of information from employers.

Phase four will be an employee section of the website which will allow members to complete online forms securely to once again reduce the amount of paper forms that come in.

All scheme members will have received a postcard or launch email inviting them to visit the new website.

Phase one went live on 22 July 2020 and phase two is due for completion at the end of 2020.

Annual Benefit statements for active and deferred members, up to 31 March 2020, were issued to all members by August 2020. A pensioner newsletter was also issued in April 2020.

## **The McCloud judgement**

The LGPS is going to change for some people as a result of The Court of Appeal ruling known as, the McCloud judgement. The ruling, made on 20 December 2018, found that when public service pension schemes changed in 2014 and 2015, they had discriminated on the grounds of age, by only providing protection for older members.

In the LGPS, these protections were applied in 2014 when the scheme changed from a final salary scheme to a CARE scheme. All members were automatically moved across to the new scheme, but older members, closer to retirement, were given additional protections, called the 'Underpin'. These protections were set up to ensure members did not receive less pension in the new scheme, than they would have in the old scheme. As the protections were only applied to members of a certain age, the Court decided that it was 'unlawful on the grounds of age discrimination'.

The Government made [a statement to the treasury](#) on 15 July 2019, announcing that, as a result of the McCloud judgement, it would 'take steps to remove the discrimination.' Although the original ruling only directly involved two schemes, the Government has confirmed it will be applied to all public service pension schemes. These protections in the LGPS will need to be revised. As a result, if members are affected by the changes the amount of pension they get may change.

A Government consultation was released on 16 July 2020 with proposals on changes that could be made to the scheme to remove the discrimination. The consultation closed on 8 October 2020.

More information about this judgment and next steps will appear on the pensions website at [www.southwarkpensions.co.uk](http://www.southwarkpensions.co.uk)

## Key performance data

### Performance indicators

Although the LGPS is a national scheme, it is administered in-house.

Southwark Council has a statutory responsibility to administer pension benefits payable from the Fund on behalf of participating employers, and past and present members and their dependants.

Pension Services work to an agreed set of statutory targets and the following table sets out performance against those statutory targets for each of the key tasks for the period 1 January 2020 to 31 March 2020.

Over time, Pension Services will benchmark in line with guidance set out by CIPFA, but for the time being, ongoing change and business transformation within Southwark Council is impacting on pension administration, hence the administration team is working alongside HR on developing new end-to-end processes.

For these reasons, only a three month snap shot is shown in the table :

Process	Legal requirement (from notification)	No. of cases completed	Within target	% achieved in legal deadline
Notify retirement benefits	Within one month from date of retirement	92	87	95%
Provide retirement estimate/quote on request	Within two months of request (unless earlier request issued in last 12 months)	83	83	100%
New starter notification to member joining LGPS	Within two months of joining scheme, subject to	26	24	92%

	notification received from employer			
Inform member who left scheme of leaver rights and options	Within two months of notification of leaving, from employer	74	51	69%
Obtain transfer details for transfer in, calculate and provide quote	Two months from date of request	52	29	56%
Provide transfer out (CETV) request	Three months from date of request	79	43	54%
Calculate and notify dependants about death benefits	As soon as is practicable, but within two months from date of death notification	87	81	93%
Divorce quote – letter dealing CETV and other benefits	Three months from date of request	1	1	100%

The source of key performance data included in this report comes from the pension system used by Southwark Council.

### Financial indicators

The cost of administering the Fund in 2019-20 was £8.881 million, representing £320 per scheme member.

During 2019-20 the Fund did not undertake any activity with regard to the National Fraud Initiative scheme.

### Other information

#### Membership of the Fund

The Fund provides pensions for:

- Employees of Southwark Council;
- Employees of a number of admitted bodies, i.e. organisations that participate in the scheme via an admission agreement. Examples of admitted bodies are not for profit organisations with a link to the council and contractors who have taken on the council's services and therefore staff have been transferred; and
- Employees of scheduled bodies, i.e. organisations which have the right to be a member of the LGPS under the regulations (e.g. academies).

Overall membership has increased by approximately 10.5% over the last twelve months. The Fund has matured over the last five years, with deferred and pensioner members increasing gradually.



Membership	2015	2016	2017	2018	2019	2020
Active	7,210	7,117	6,914	6,291	6,753	6,888
Pensioner	6,913	7,212	7,483	7,620	7,594	7,887
Deferred	7,705	7,858	9,063	10,269	10,723	10,932*
<b>Total</b>	<b>21,828</b>	<b>22,187</b>	<b>23,460</b>	<b>24,180</b>	<b>25,070</b>	<b>25,707</b>

\* included in this figure is 2,899 undecided leavers.

During 2019-20 there were 125 new pensioners, split as follows:

- 23 late retirements ;
- 8 ill-health early retirements;
- 48 early retirements through redundancy;
- 33 early retirements; and
- 13 flexible retirements.

## Employers in Fund

The table below summarises the number of active employers in the Fund analysed by scheduled bodies and admitted bodies during the financial year. During the year, two admitted bodies exited the scheme.

There are no ceased employers who have outstanding liabilities. The Fund has a policy in place which provides that all ceasing employers' liabilities are subsumed into the Council's share of the Fund. As part of this policy, each admitted employer is given a fixed employer contribution rate on commencement in the Fund. Any variances in the rate over time are either treated as a saving or a cost to the contracting department. The purpose of this policy is to ensure that the full cost of pensions is reflected in contracts and those uncertainties around pension costs do not influence the contract price quoted by providers.

	Active
Scheduled body	30
Admitted body	20
<b>Total</b>	<b>50</b>

## Participating employers

Appendix 1 lists the admitted and scheduled bodies participating in the Fund at 31 March 2020 and sets out the contributions paid by employees and employers during the year for each employer.

## How the service is delivered

### Key services provided

Development of the Member Self-Service portal as a 'one stop shop' for members looking to find out more about their pension, and to check and update the information held about them has been paused while a new hosting infrastructure for the pension system is implemented.

A newsletter for pensioners was sent out in April 2020 which updated members about pension increases and provided other relevant information, for example about planning ahead, the State Pension, protecting personal data and keeping personal data up-to-date. It also made members aware that greater use will be made in the future of electronic communications. Other members will receive a newsletter with this year's Annual Benefit statements. This will cover a range of relevant topics.

A number of information sessions were provided to targeted groups of staff. Work continues to improve pensions information on Southwark Council's website, to make it easier for members, prospective members and employers to find relevant information. The content has also been further reviewed and updated where appropriate with use being made of the website to broadcast important alerts to members.

### Key information sources

	Member Self-Service Portal	Helpdesk/Mailbox	Website/Intranet
Active	Yes <a href="https://pensions.southwark.gov.uk/">https://pensions.southwark.gov.uk/</a>	<b>020 7525 4924</b> <a href="mailto:lbspensions@southwark.gov.uk">lbspensions@southwark.gov.uk</a>	<a href="http://www.southwark.gov.uk/council-and-democracy/pensions">www.southwark.gov.uk/council-and-democracy/pensions</a>  The source: <a href="http://www.lgpsmember.org/">www.lgpsmember.org/</a> <a href="http://www.southwarkpensions.co.uk/">www.southwarkpensions.co.uk/</a>
Deferred	Yes <a href="https://pensions.southwark.gov.uk/">https://pensions.southwark.gov.uk/</a>	<b>020 7525 4924</b> <a href="mailto:lbspensions@southwark.gov.uk">lbspensions@southwark.gov.uk</a>	<a href="http://www.southwark.gov.uk/council-and-democracy/pensions">www.southwark.gov.uk/council-and-democracy/pensions</a>  <a href="http://www.lgpsmember.org/">www.lgpsmember.org/</a> <a href="http://www.southwarkpensions.co.uk/">www.southwarkpensions.co.uk/</a>
Pensioner	Yes <a href="https://pensions.southwark.gov.uk/">https://pensions.southwark.gov.uk/</a>	<b>020 7525 4924</b> <a href="mailto:lbspensions@southwark.gov.uk">lbspensions@southwark.gov.uk</a>	<a href="http://www.southwark.gov.uk/council-and-democracy/pensions">www.southwark.gov.uk/council-and-democracy/pensions</a>  <a href="http://www.lgpsmember.org/">www.lgpsmember.org/</a>
Employing bodies	N/A	<b>020 7525 4924</b> <a href="mailto:lbspensions@southwark.gov.uk">lbspensions@southwark.gov.uk</a>	<a href="http://www.southwark.gov.uk/council-and-democracy/pensions">www.southwark.gov.uk/council-and-democracy/pensions</a>  The source: <a href="http://www.lgpsmember.org/">www.lgpsmember.org/</a> <a href="http://www.southwarkpensions.co.uk/">www.southwarkpensions.co.uk/</a>

### Internal Dispute Resolution Procedure (IDRP)

Occasionally, a disagreement over a decision that Southwark Council has made about a pension will be made. The IDRP gives members the right to apply to an adjudicator who will consider the case and decide if the original decision was correct or overturn that decision.

IDRP can be a two stage process.

Under stage one the adjudicator will consider all the points raised in determining a decision. A member will need to carefully consider why in their view the LGPS Regulations were not applied. If a member disagrees with the stage one decision, the matter can be appealed and the decision and case will pass to a different adjudicator under stage two, who will assess any new information afresh and make a final decision on behalf of Southwark Council.

## The Pensions Ombudsman (TPO)

TPO deals with complaints and disputes. If The Pensions Advisory Service (TPAS) guidance cannot resolve a problem, a formal complaint application can be made. Anyone using TPO's 'Early Resolution Service' will not be expected to have first used the LGPS' IDRPs if the parties are happy with that.

TPO is impartial and looks at all the facts without taking sides. It has legal powers to make decisions that are final, and binding and enforceable in Court. There is no charge for using TPO as it is funded by grant-in-aid, paid by the DWP.

TPO can be contacted on 0800 917 4487  
Address: 10 South Colonnade, Canary Wharf, E14 4PU  
Website: [www.pensions-ombudsman.org.uk](http://www.pensions-ombudsman.org.uk)

## The Pensions Advisory Service (TPAS)

TPAS is the Department for Work and Pensions (DWP) arm's length body for delivering personal information and guidance on pension matters. It can help resolve problems an individual may be having with their pension and they can write on your behalf to obtain further information if you have been unable to do so.

TPAS can be contacted on 0800 011 3797  
Address: 120 Holborn, London, EC1N 2TD  
Website: [www.pensionsadvisoryservice.org.uk](http://www.pensionsadvisoryservice.org.uk)

## Local Government Pension Scheme (LGPS) Regulations

All LGPS Regulations are held within Pension Services, 2<sup>nd</sup> Floor, 160 Tooley Street, London, SE1 2QH and are available for inspection upon request.

## FURTHER INFORMATION

### Queries regarding benefits or cost of membership

[lbspensions@southwark.gov.uk](mailto:lbspensions@southwark.gov.uk)

0207 525 4924

### Queries regarding Fund investments and accounts

Caroline Watson  
Senior Finance Manager – Treasury and Pensions  
Telephone: 020 7525 4379  
Email: [caroline.watson@southwark.gov.uk](mailto:caroline.watson@southwark.gov.uk)

Or you can write to us at:

London Borough of Southwark Pension Fund  
Finance and Governance

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Treasury and Pensions  
Second Floor Hub 1  
PO BOX 64529  
London SE1P 5LX

### **External sources of information**

The Pensions Regulator  
Napier House  
Trafalgar Place  
Brighton  
East Sussex  
BN1 4DW  
Telephone: 0345 600 5666 Website: [www.thepensionsregulator.gov.uk](http://www.thepensionsregulator.gov.uk)

Website: [www.gov.uk/contact-pension-service](http://www.gov.uk/contact-pension-service)

To find out about State Pension eligibility, payments and complaints and to find your local pension centre.

Website: [www.gov.uk/find-pension-contact-details](http://www.gov.uk/find-pension-contact-details)

The Pensions Tracing Service can help ex-members of pension schemes who may have lost touch with previous employers, to trace their pension entitlements.

Telephone: 0800 731 0193

## GLOSSARY

### **Absolute return fund**

A fund that aims to deliver positive returns in all market conditions, with low volatility. This is achieved through the use of financial instruments such as derivatives to protect against downside risk and generate higher returns.

### **Actuary**

An independent consultant who advises the Fund and reviews the financial position of the Fund every three years. The Actuary then produces a report, known as the actuarial valuation report, which compares the Fund's assets with its liabilities and prescribes the rates at which the employing bodies must contribute.

### **Added Years**

Additional service that a member of the Fund can buy by paying extra contributions to the Fund providing that HMRC limits on pension and contributions are not exceeded.

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

An option available to individual members to secure additional pension benefits by making regular payments to the Fund's AVC provider up to a maximum of 15% of total earnings.

### **Admitted body**

An organisation whose staff can become members of the Fund by virtue of an admission made between the Council and the organisation. It enables contractors who take on the Council's services with employees transferring, to offer those staff continued membership of the Fund.

### **Asset allocation**

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

### **Asset class**

A collective term for investments of a similar type. The main asset classes are equities (shares), bonds, cash and property.

### **Basis point**

One hundredth of 1% (i.e. 0.01%).

### **Benchmark**

A standard against which the performance of an investment can be compared. Asset allocation benchmarks vary from peer group to customized benchmarks tailored to a particular fund's requirements.

### **CARE scheme**

Career Average Revalued Earnings - where pension is built up as a proportion of pensionable pay - 1/49th for each year in the LGPS 2014. Therefore, instead of calculating pension with reference to final salary on retirement, the LGPS 2014 uses the average of annual earnings over membership of the LGPS. Earlier years are revalued by inflation (CPI) to ensure that each year's salary is of equivalent real value.

### **Cash transfer values**

The capital value of a benefit entitlement paid into or withdrawn from the Fund when an employee joins or leaves the scheme with a pension transfer.

### **Corporate bond**

Corporate bonds are when an investor loans money to an entity for a defined period for either a fixed or a variable interest rate.

### **Custody**

Administering of securities by a financial institution. The custodian bank keeps a record of a client's investments and may also collect

income; process tax reclaims and provide other services, according to client instructions. The custodian physically holds the securities for safe-keeping

### **Deferred pension**

The pension benefit payable from Normal Retirement Age to a member of the Fund who has ceased to contribute as a result of leaving employment or opting out of the pension scheme before retirement age.

### **Defined benefit scheme**

A type of pension scheme where the pension that will ultimately be paid to the employee is fixed, usually as a percentage of final salary. It is the responsibility of the sponsoring organisation to ensure that sufficient assets are set aside to meet the pension promised.

### **Diversification**

The spreading of investment funds among different types of assets, markets and geographical areas in order to reduce risk.

### **Diversified growth funds**

Investment products that utilise a variety of liquid assets, strategies and investment horizons in order to deliver real capital appreciation over the medium to long-term

### **Emerging markets**

Stock markets in developing countries (as defined by the World Bank).

### **Equities**

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

### **Final Pensionable Pay**

Pensionable Pay earned in the last 12 months before retirement (or any one of the previous two

years if annual earnings in either of these years are higher).

### **Final salary scheme**

A pension scheme that provides a pension and a lump sum benefit calculated as a proportion of a member's pay in their last year of membership depending on the length of membership in the scheme.

### **Fixed interest**

An income stream which remains constant during the life of the asset, such as income derived from bonds, annuities and preference shares.

### **Index**

A calculation of the average price of shares, bonds, or other assets in a specified market to provide an indication of the average performance and general trends in the market.

### **Index-linked gilts**

Gilts where the principal is indexed to inflation on a daily basis in terms of the Consumer Price Index (CPI).

### **Mandate**

The agreement between a client and investment manager laying down how the fund is to be managed. May include performance targets by reference to a benchmark.

### **Market value**

The price at which an investment can be bought or sold at a given date.

### **Pensionable Pay**

Basic pay excluding non-contractual overtime, bonus and shift payments.

### **Pooled funds**

Pooled funds are funds which manage the investments of more than one investor on a collective basis. Each investor is allocated units

which are revalued at regular intervals. Income from these investments is normally returned to the pooled fund and increases the value of the units.

### **Return**

The value received (income plus capital) annually from an investment, usually expressed as a percentage.

### **Scheduled body**

An organisation that has the right to become a member of the Local Government pension Scheme under the scheme regulations. Such an organisation does not need to be admitted as its right to membership is automatic.

### **Unconstrained equity investing**

Mandates where the investment manager is expected to construct and manage their portfolio of stocks in a way that reflects their judgment, without being hindered by limits sets relative to a benchmark index. The manager may also be free to invest a high proportion in cash if they have a negative view on equity markets. Generally, there would be few investment restrictions, although a mandate would rarely be totally unconstrained.

### **Unlisted securities**

Holdings in companies which do not form part of the main stock market. They may be developing companies or smaller companies whose shares are not frequently traded. Unlisted securities are usually less liquid than those traded in the main markets.

### **Valuation**

A summary of an investment portfolio showing the holdings and their value as at a certain date.

## APPENDIX 1 - Contributing employers and amounts received in 2019-20

Name	Total employee Contributions (£000)	Total employer Contributions (£000)	Total contributions (£000)
<b>Administering authority</b>			
London Borough of Southwark	11,904.00	38,308.00	50,212.00
<b>Scheduled Bodies</b>			
Ark All Saints Academy	75.74	149.54	225.28
Ark Globe Academy	84.95	128.58	213.53
Ark Walworth Academy	67.39	172.68	240.07
Bacons College	82.53	214.76	297.29
Compass Free School	20.03	53.15	73.17
Dulwich Hamlet	23.51	66.87	90.38
The Belham School (part of Dulwich Hamlet)	30.76	85.72	116.48
Goose Green	31.39	81.07	112.47
Galley Wall Primary School	17.78	48.00	65.78
Harris Academy Bermondsey	42.17	68.30	110.47
Harris Academy at Peckham	49.53	119.93	169.46
Harris Peckham Free School	17.00	36.08	53.08
Harris Primary Academy Peckham Park	24.60	58.04	82.65
Harris Boys Academy	41.41	101.45	142.85
Harris Girls Academy	37.47	87.48	124.96
Harris Primary East Dulwich	19.50	49.65	69.15
Harris PAPP Nursery Hub	3.81	8.35	12.16
John Donne	45.28	105.54	150.82
John Keats	12.13	25.09	37.22
Judith Kerr Free School	20.58	52.59	73.16
Kingsdale Foundation School	33.83	94.27	128.10
Newlands Academy (AET)	29.30	79.09	108.39
Redriff Primary Academy	59.08	162.41	221.49
Spa Academy	40.21	110.64	150.86
St. Paul's CE Primary	30.49	95.31	125.80
The Angel Oak Academy (Gloucester)	29.46	109.55	139.01
The Charter School Educational Trust (ED)	31.57	64.26	95.83
The Charter School Educational Trust 2	83.69	170.10	253.79
The Dulwich Hamlet Educational Trust	4.74	9.14	13.88
University Academy Engineering South Bank (UAESB)	37.81	116.48	154.29
<b>Scheduled bodies total</b>	<b>1,127.76</b>	<b>2,724.11</b>	<b>3,851.86</b>



Name	Total employee Contributions (£000)	Total employer Contributions (£000)	Total contributions (£000)
<b>Admitted bodies</b>			
AiP	2.47	10.54	13.01
APCOA - School Crossing	0.29	0.97	1.26
Brandon Trust	22.58	69.59	92.17
Browning Tenant Management	5.27	13.65	18.92
Centre for Literacy (CLPE)	3.41	13.19	16.60
D Brice & Co Ltd	0.89	3.21	4.10
Energy Kidz	1.55	6.19	7.74
HATS	0.39	1.44	1.84
Interserve (MacLelans)	1.65	7.01	8.66
Leather Market AdBod	12.01	16.56	28.57
Pabulum	0.89	2.89	3.78
PFI VEOLIA ES	138.06	430.97	569.03
Principles Catering	0.68	2.29	2.98
Sherman & Waterman Associates	0.06	0.22	0.28
South London Gallery - SLG	9.94	16.29	26.23
Southwark Diocesan B of E	12.07	14.67	26.74
Southwark Law Centre	45.54	149.89	195.43
Sports and Leisure Management	7.37	27.99	35.36
Westgate Cleaning - Camelot	0.90	3.02	3.91
WestGate Cleaning - Goose Green	0.88	3.94	4.83
<b>Admitted bodies total</b>	<b>266.90</b>	<b>794.5</b>	<b>1,061.4</b>
<b>Total pension contributions 2019-20*</b>	<b>13,298.66</b>	<b>41,826.61</b>	<b>55,125.26</b>

*\*Total contributions represents employee and employer contributions excluding Early Retirement contributions of £356,104. Total contributions are as per the Statement of Accounts of £55.151 million includes all contributions and any adjustments.*

The Fund did not levy any interest on the late payment of any contributions during 2019-20.

## APPENDIX 2 – Pension Fund Statement of Accounts

**Independent auditor's report to the members of Southwark Council on the consistency of the pension fund financial statements of the London Borough of Southwark Pension Fund included in the Pension Fund Annual Report (the Report).**

### **Opinion**

The pension fund financial statements of the London Borough of Southwark Pension Fund (the Fund) administered by the Southwark Council (the Authority) for the year ended 31 March 2020 which comprises of the Fund Account, the Net Assets Statement and the notes to the Fund financial statements, including a summary of significant accounting policies are derived from the audited Fund financial statements for the year ended 31 March 2020 included in the Authority's Statement of Accounts (the Statement of Accounts).

In our opinion, the accompanying Fund financial statements are consistent, in all material respects, with the audited financial statements in accordance with proper practices as defined in the CIPFA/LASAAC code of practice on local authority accounting in the United Kingdom 2019/20 and applicable law.

### **Pension Fund Annual Report – Fund financial statements**

The Report and the Fund financial statements do not reflect the effects of events that occurred subsequent to the date of our report on the Statement of Accounts. Reading the Fund financial statements and the auditor's report thereon is not a substitute for reading the audited Statement of Accounts and the auditor's report thereon.

### **The audited financial statements and our Report thereon**

We expressed an unmodified audit opinion on the Fund financial statements in the Statement of Accounts in our report dated 30 November 2020.

That report also includes an Emphasis of Matter - effects of COVID-19 on the valuation of property and infrastructure investments section that draws attention to *Note 5* in the audited Fund financial statements, which is replicated in *Note 5* of the Fund financial statements. *Note 5* describes the effects of the COVID-19 pandemic on the valuation of the Fund's property and infrastructure investments as at 31 March 2020. *Note 5* indicates that the ongoing impact of the COVID-19 pandemic has created an unprecedented set of circumstances on which to base judgement. As such, the Fund property and infrastructure allocations as at 31 March 2020 are difficult to value according to the preferred accounting policy. Valuations are therefore reported on the basis of 'material valuation uncertainty'. Consequently, less certainty and a higher degree of caution should be attached to the valuation than would normally be the case. As stated in our report dated 30 November 2020, our opinion is not modified in respect of this matter.

### **Strategic Director of Finance and Governance's responsibilities for the Fund financial statements in the Report**

Under the Local Government Pension Scheme Regulations 2013 the Strategic Director of Finance and Governance of the Authority is responsible for the preparation of the Fund financial statements, which must include the Fund Account, the Net Asset Statement and supporting notes and disclosures prepared in accordance with proper practices. Proper practices for the Fund financial statements in both the Statement of Accounts and the Report are set out in the CIPFA/LASAAC code of practice on local authority accounting in the United Kingdom 2019/20.

## Auditor's responsibility

Our responsibility is to express an opinion on whether the Fund financial statements in the Report are consistent, in all material respects, with the audited Fund financial statements in the Statement of Accounts based on our procedures, which were conducted in accordance with International Standard on Auditing 810 (Revised), Engagements to Report on Summary Financial Statements.

## Use of our report

This report is made solely to the members of the Authority, as a body, in accordance with Part 5 paragraph 20(5) of the Local Audit and Accountability Act 2014 and as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our audit work has been undertaken so that we might state to the Authority's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

*Ciaran McLaughlin, Key Audit Partner for and on behalf of Grant Thornton UK LLP, Local Auditor, London, 30 November 2020.*

## LONDON BOROUGH OF SOUTHWARK PENSION FUND

### FUND ACCOUNT

	Note	2019-20		2018-19	
		£000	£000	£000	£000
<b>Dealings with members, employers and others directly involved in the Fund</b>					
Contributions	6	(55,151)		(56,129)	
Transfers in from other pension funds	7	(10,636)		(2,762)	
<b>Sub total</b>			<b>(65,787)</b>		<b>(58,891)</b>
Benefits	8	59,692		59,112	
Payments to and on account of leavers	9	11,692		4,964	
<b>Sub total</b>			<b>71,384</b>		<b>64,076</b>
<b>Net reduction/(addition) from dealing with members of the Fund</b>			<b>5,597</b>		<b>5,185</b>
<b>Management expenses</b>	10		<b>8,881</b>		<b>7,508</b>
<b>Returns on investments</b>					
Investment income	11	(15,578)		(15,814)	
Taxes on income	11	291		382	

Profit and losses on disposal of investments and changes in market value of investments	12	61,254	(108,300)
<b>Net return on investments</b>		<b>45,967</b>	<b>(123,732)</b>
<b>Net (increase)/decrease in the net assets available for benefits during the year</b>		<b>60,445</b>	<b>(111,039)</b>
Opening net assets of the Fund		(1,641,986)	(1,530,947)
<b>Net assets of the Fund available to fund benefits at 31 March</b>		<b>(1,581,541)</b>	<b>(1,641,986)</b>

## NET ASSETS STATEMENT

		<b>31 March</b>	<b>31 March</b>
	<b>Note</b>	<b>2020</b>	<b>2019</b>
		<b>£000</b>	<b>£000</b>
Investment assets	12	1,542,755	1,631,245
Current assets	13	44,238	14,195
Current liabilities	13	(5,452)	(3,454)
<b>Net assets of the Fund available to fund benefits at 31 March</b>		<b>1,581,541</b>	<b>1,641,986</b>

The Fund's financial statements do not take account of liabilities to pay pensions and other benefits after the period end.

The estimated actuarial present value of promised retirement benefits is disclosed at note 19.

## NOTES TO THE PENSION FUND STATEMENTS

### 1. INTRODUCTION

The Pension Fund (the Fund) is part of the Local Government Pension Scheme (LGPS) and is administered by Southwark Council (the Council).

The following description of the Fund is a summary only. For more detail, reference should be made to the Pension Fund Annual Report 2019-20 and the underlying statutory powers underpinning the scheme, namely the Public Service Pension Act 2013 and the LGPS Regulations.

#### a) General

The scheme is governed by the Public Service Pension Act 2013. The Fund is administered in accordance with the following secondary legislation:

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

It is a contributory defined benefit scheme that provides pensions and other benefits for former employees of the Council and other admitted organisations.

The overall investment strategy is the responsibility of the Council. This responsibility is delegated to the Strategic Director of Finance and Governance, taking account of the advice of the Pensions Advisory Panel (PAP). In line with the provisions of the Public Services Pensions Act 2013, the Council has set up a Local Pension Board to assist the Council in its role as scheme manager of the Fund. The Board meets on a quarterly basis and has its own terms of reference. Board members are independent of the PAP.

#### b) Membership

Membership of LGPS is voluntary and employees are free to choose whether to join the scheme, remain in the scheme or make their own personal arrangements outside of the scheme.

Organisations participating in the Fund include:

- Scheduled bodies, which are largely academies and similar bodies whose staff are automatically entitled to be members of the Fund; and
- Admitted bodies, which are other organisations that participate in the Fund under an admission agreement between the Fund and the relevant organisation. Admitted bodies include voluntary, charitable and similar bodies or private contractors undertaking a local authority function following outsourcing to the private sector.

A list of participating organisations and their contributions for the financial year 2019-20 is included within the Pension Fund Annual Report 2019-20. This is available on the Council website.

	31 March 2020	31 March 2019
Number of contributors to the Fund	6,888	6,753
Number of contributors and dependants receiving allowances	7,887	7,594
Number of contributors who have deferred their pensions	10,932	10,723

#### c) Funding

Benefits are funded by contributions and investment earnings. Contributions are made by active members of the Fund in accordance with the LGPS Regulations 2013 and range from 5.5% to 12.5% of pensionable pay for the financial year ending 31 March 2020. Employee contributions are matched by employers' contributions, which are set in accordance with the triennial actuarial funding valuations, the last being at 31 March 2019. For the 2019-20 financial year primary employer contribution rates ranged from 7.3% to 17.8% of pensionable pay, plus additional deficit payments where appropriate.

#### d) Benefits

Prior to 1 April 2014, pension benefits under the LGPS were based on final pensionable pay and length of pensionable service, summarised in the following table:

	Service pre- 1 April 2008	Service post- 31 March 2008	Service pre- 1 April 2008
<b>Pension</b>	Each year worked is worth 1/80 x final pensionable salary.	Each year worked is worth 1/60 x final pensionable salary.	Each year worked is worth 1/49 career average revalued earnings salary.
<b>Lump Sum</b>	Automatic lump sum of 3x pension. In addition, part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up.	No automatic lump sum. Part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up.	

## 2. BASIS OF PREPARATION

The Statement of Accounts summarises the Fund's transactions for the 2019-20 financial year and its position at year-end as at 31 March 2020. The accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2019-20, which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

The accounts summarise the transactions of the Fund and report on the net assets available to pay pension benefits. The accounts do not take into consideration the obligations to pay pensions and benefits which fall due after the end of the financial year.

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fund account – revenue recognition

#### a) Contributions income

Normal contributions, both from the members and from the employers, are accounted for on an accruals basis at the percentage rate recommended by the Fund Actuary in the payroll period to which they relate.

Employers' augmentation contributions and pension strain contributions are accounted for in the period in which the liability arises. Any amount due in year but unpaid will be classed as a current financial asset.

#### b) Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the Local Government Scheme Regulations. Individual transfers in or out are accounted for when received or paid, which is normally when the member liability is accepted or discharged.

Transfers in from members wishing to use the proceeds of their Additional Voluntary Contributions to purchase scheme benefits are accounted for on a receipts basis and are included in transfers in. Bulk group transfers are accounted for on an accruals basis in accordance with the terms of the transfer agreement.

#### c) Investment income

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

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

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the net assets statement as a current investment asset. Property related income consists primarily of rental income. Rental income from operating leases on properties owned by the fund is recognised on a straight-line basis over the term of the lease. Any lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

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

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

d) Fund account – benefits payable

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

e) Fund account – taxation

The fund is a registered public service scheme under section 1(1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK Income Tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin unless exemption is permitted. Irrecoverable tax is accounted for as a Fund expense as it arises.

f) Management expenses

The Code does not require any breakdown of Fund administrative expenses. However, in the interests of greater transparency, the Council discloses its Fund management expenses in accordance with the CIPFA guidance Accounting for Local Government Pension Scheme Management Costs.

Administrative expenses

All administrative expenses are accounted for on an accruals basis. All staff costs of pension administration are charged directly to the Fund. Management, accommodation and other overheads are apportioned to the Fund in accordance with Council policy

Oversight and governance costs

All oversight and governance expenses are accounted for on an accruals basis. All staff costs associated with governance and oversight are charged directly to the Fund. Management, accommodation and other overheads are apportioned to the fund in accordance with Council policy.

Investment management expenses

All investment management expenses are accounted for on an accruals basis. Fees for the fund managers and custodian are agreed in the respective mandates governing their appointments and are based broadly on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.

Net Asset Statement

g) Financial assets

Financial assets are included in the net assets statement on a fair value basis in accordance with the Code and with the requirements of IFRS 13 as at the reporting date. A financial asset is recognised in the net assets statement on the date the Fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in the fair value of assets are recognised by the fund. The values of investments as shown in the net assets statement have been determined as follows:

- Equity investments, unit trusts and unitised insurance policies at their market bid price on 31 March each year;



- Foreign currency transactions have been brought into the accounts at the exchange rate that was in force when the transaction took place;
- End of year balances on foreign currency transactions have been translated at the exchange rate on 31 March each year;
- Investment assets have been valued and included in the accounts at bid price except for derivative contracts which are valued on the basis of unrealised gains and losses; and
- Property unit trusts have been included at net asset price.

#### h) Freehold and leasehold property

Property assets have been included in the accounts at fair value as at 31 March each year. The valuation of direct property managed by Nuveen is carried out annually by an independent valuer.

#### i) Derivatives

The Fund uses derivative financial instruments to manage its exposure to specific risks arising from its investment activities. The Fund does not hold derivatives for speculative purposes. The future value of forward currency contracts is based on market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year-end with an equal and opposite contract.

#### j) Cash and cash equivalents

Cash comprises cash in hand and demand deposits. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal risk of changes in value.

#### k) Financial liabilities

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

#### l) Actuarial present value of promised retirement benefits

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

#### m) Additional Voluntary Contributions (AVCs)

The Fund provides an AVC scheme for its members, the assets of which are invested separately from those of the Fund. AVCs are not included in the accounts but are disclosed as note 6.

#### 4. CRITICAL JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Fund liability is calculated every three years by the appointed Actuary, with annual updates in the intervening years. The methodology used is in line with accepted guidelines and in accordance with IAS 19. Assumptions underpinning the valuations are agreed with the Actuary and are summarised in note 19. This estimate is subject to significant variances based on changes to underlying assumptions.

#### 5. ASSUMPTIONS MADE ABOUT THE FUTURE AND OTHER MAJOR SOURCES OF ESTIMATION UNCERTAINTY

The statements contain estimated figures that are based on assumptions made by the council about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, as balances cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of retirement benefits	<p>This applies to the estimation of the net liability to pay pensions, which depends upon a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets.</p> <p>Valuation techniques are used to determine the carrying amount of pooled property funds and directly held freehold and leasehold property. Where possible these valuation techniques are based on observable data, but where this is not possible, management uses the best available data. Changes in the valuation assumptions used, together with significant changes in rental growth, vacancy levels or the discount rate could affect the fair value of property.</p>	A 1.0% change in the discount rate is estimated to change the present value of pension liability by £271 million.
Freehold and leasehold, property pooled, property and infrastructure funds	<p>The ongoing impact of the COVID-19 pandemic has created an unprecedented set of circumstances on which to base judgement. As such, the Fund property and infrastructure allocations as at 31 March 2020, are difficult to value according to preferred accounting policy. Valuations are therefore reported on the basis of 'material valuation uncertainty'.</p> <p>Consequently, less certainty and a higher degree of caution should be attached to the valuation than would normally be the case.</p>	The effect of variations in the factors supporting the valuation, estimated to be 7%, would be an increase or decrease in the value of property of £17 million, on a fair value of £246 million.

## 6. CONTRIBUTIONS RECEIVABLE

Contributions represent the total amount receivable from employees and employers of the scheme.

	2019-20			2018-19		
	Employees	Employers	Total	Employees	Employers	Total
	£000	£000	£000	£000	£000	£000
Southwark council	(11,904)	(38,308)	(50,212)	(11,358)	(39,932)	(51,290)
Admitted bodies	(270)	(805)	(1,075)	(273)	(921)	(1,194)
Scheduled bodies	(1,128)	(2,736)	(3,864)	(1,020)	(2,625)	(3,645)
<b>Total contributions</b>	<b>(13,302)</b>	<b>(41,849)</b>	<b>(55,151)</b>	<b>(12,651)</b>	<b>(43,478)</b>	<b>(56,129)</b>

Contributions receivable from employers are shown below:

	2019-20	2018-19
	£000	£000
Normal	(29,475)	(28,092)
Early retirement strain	(356)	(3,730)
Deficit funding	(12,018)	(11,656)
<b>Total contributions from employers</b>	<b>(41,849)</b>	<b>(43,478)</b>
<b>Contributions from employees</b>	<b>(13,302)</b>	<b>(12,651)</b>
<b>Total contributions</b>	<b>(55,151)</b>	<b>(56,129)</b>

During 2019-20 employees made AVCs of £258k (£214k in 2018-19).

The value of the AVCs at 31 March 2020 was £2.8 million (£2.9 million at 31 March 2019).

## 7. TRANSFERS IN FROM OTHER PENSION FUNDS

Transfers in from other pension funds were as follows:

	2019-20	2018-19
	£000	£000
Individual transfers	(10,636)	(2,762)
<b>Total transfers in from other pension funds</b>	<b>(10,636)</b>	<b>(2,762)</b>

## 8. BENEFITS PAYABLE

The table below shows the total benefits payable grouped by entities:

	2019-20	2018-19
	£000	£000
Pensions	50,347	51,418
Commutation of pensions and lump sum retirement benefits	8,108	6,571
Lump sums - death benefits	1,237	1,123
<b>Total benefits payable</b>	<b>59,692</b>	<b>59,112</b>

The table below shows the total benefits payable grouped by entities:

	2019-20	2018-19
	£000	£000
Southwark council	56,682	56,703
Admitted bodies	2,049	1,766
Scheduled bodies	961	643
<b>Total benefits payable</b>	<b>59,692</b>	<b>59,112</b>

## 9. PAYMENTS TO AND ON ACCOUNT OF LEAVERS

	2019-20	2018-19
	£000	£000
Refund of contributions	430	246
Individual transfers out to other schemes	11,262	4,718
<b>Total payments</b>	<b>11,692</b>	<b>4,964</b>

## 10. MANAGEMENT EXPENSES

	2019-20	2018-19
	£000	£000
Administrative costs	2,677	2,059
Investment and management expenses	5,632	4,820
Oversight and governance costs	572	629
<b>Total management expenses</b>	<b>8,881</b>	<b>7,508</b>

The 2019-20 fee for external audit services for the pension fund was £28k (£21k in 2018-19).

The table below shows the total investment and management expenses:

	2019-20	2018-19
	£000	£000
Management fees	3,931	3,019
Property management expenses	1,618	1,700
Custody fees	83	101
<b>Total investment expenses</b>	<b>5,632</b>	<b>4,820</b>

The Fund incurred expenses of £0.9 million in relation to services provided by the Council during 2019-20 (£0.8 million during 2018-19).

## 11. INVESTMENT INCOME

	<b>2019-20</b>	<b>2018-19</b>
	<b>£000</b>	<b>£000</b>
Dividends from equities	(4,533)	(3,783)
Income from pooled investment vehicles	(1,963)	(2,465)
Rent from properties	(9,069)	(9,559)
Interest on cash deposits	(13)	(7)
<b>Total investment income before taxes</b>	<b>(15,578)</b>	<b>(15,814)</b>
Taxes on income	291	382
<b>Total investment income after taxes</b>	<b>(15,287)</b>	<b>(15,432)</b>

## 12. INVESTMENT ASSETS

	31 March 2020 £000	31 March 2019 £000
<b>Bonds</b>		
Quoted Overseas	6,177	7,700
<b>Equity</b>		
Quoted UK	25,195	23,275
Quoted Overseas	140,725	149,126
<b>Pooled Funds</b>		
Fixed Income Overseas	120,788	124,768
Index-Linked Gilts UK	153,575	149,613
Multi Asset Overseas	163,023	167,475
<b>Unitised Insurance Policy</b>		
Equity Overseas	651,416	716,671
<b>Property</b>		
Direct Property UK	189,550	222,470
Property Unit Trust UK	56,420	67,659
Infrastructure	31,803	-
<b>Derivatives</b>		
Forward currency contracts	222	90
<b>London Collective Investment Vehicle</b>	150	150
<b>Other investment balances</b>	3,711	2,248
<b>Investment assets</b>	<b>1,542,755</b>	<b>1,631,245</b>

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 the sale of investments during the year. The table on the next page shows the movement in investment assets and the change in market value for the year:

	Value at 31 March 2019	Purchases	Sales	Change in market value	Cash movement	Value at 31 March 2020
	£000	£000	£000	£000	£000	£000
Bonds	7,700	32,410	(34,393)	460	-	6,177
Equity	172,401	52,712	(47,120)	(12,073)	-	165,920
Pooled funds	441,856	383	-	(4,853)	-	437,386
Unitised insurance policy	716,671	122,200	(151,564)	(35,891)	-	651,416
Property	290,129	6,182	(41,289)	(9,052)	-	245,970
Infrastructure	-	32,454	(426)	(225)	-	31,803
Derivatives	90	3,101	(3,349)	380	-	222
Cash deposits	-	-	-	-	-	-
London Collective Investment Vehicle	150	-	-	-	-	150
Other investment balances	2,248	-	-	-	1,463	3,711
<b>Investment assets</b>	<b>1,631,245</b>	<b>249,442</b>	<b>(278,141)</b>	<b>(61,254)</b>	<b>1,463</b>	<b>1,542,755</b>



	Value at 31 March 2018	Purchase	Sales	Change in market value	Cash movement	Value at 31 March 2019
	£000	£000	£000	£000	£000	£000
Bonds	8,582	34,253	(36,136)	1,001	-	7,700
Equity	147,756	83,057	(78,180)	19,768	-	172,401
Pooled funds	409,056	36,375	(17,511)	13,936	-	441,856
Unitised insurance policy	686,592	210,946	(249,884)	69,017	-	716,671
Property	266,190	27,563	(7,757)	4,133	-	290,129
Derivatives	103	1,269	(1,727)	445	-	90
Cash deposits	1,000	-	-	-	(1,000)	-
London Collective Investment Vehicle	150	-	-	-	-	150
Other investment balances	2,298	-	-	-	(50)	2,248
<b>Investment assets</b>	<b>1,521,727</b>	<b>393,463</b>	<b>(391,195)</b>	<b>108,300</b>	<b>(1,050)</b>	<b>1,631,245</b>

The Fund does not hold derivatives as a main asset class, but they are used by Newton Investment Management, our active equity fund manager, to hedge the currency risk of holding global equities. The currency forward contracts are traded over the counter.

The valuation of direct property managed by Nuveen is carried out by Knight Frank LLP. The valuer is RICS qualified and the valuation took place on 31 March 2020. All properties have been valued at market value.

The Investment Strategy Statement can be accessed through the Council's website. The following investments represent more than 5% of investment assets.

Name of investment	Fund manager	31 March 2020	% of investment assets	31 March 2019	% of investment assets
		£000	%	£000	%
Diversified Growth Fund	BlackRock	163,023	11%	167,474	10%
Low Carbon Target	Legal and General	263,047	17%	158,330	10%
North America Equity	Legal and General	43,000	3%	132,081	8%
Low Carbon Target	BlackRock	123,200	8%	131,087	8%
Absolute Return Bond Fund	BlackRock	120,788	8%	124,768	8%
+5 Year Index Linked Gilt Fund	Legal and General	85,426	6%	83,423	5%
US Equity Fund	BlackRock	77,284	5%	79,777	5%

The market value of assets (excluding cash and accruals) managed by the investment managers at the balance sheet date 31 March 2020 has been set out in the table below.

	31 March 2020		31 March 2019	
	£000	%	£000	%
BlackRock	673,584	44%	707,797	43%
Legal and General Investment Managers	415,217	27%	450,730	28%
Nuveen	195,651	13%	242,973	15%
Newton Investment Management	172,320	11%	180,191	11%
M and G Real Estate	22,358	1%	21,745	1%
Invesco Real Estate	14,953	1%	14,611	1%
Glennmont	11,700	1%	-	0%
Temporis	20,103	1%	-	0%
Frogmore Real Estate Partners	8,822	1%	7,734	1%
Brockton Capital LLP	4,186	0%	3,066	0%
London Collective Investment Vehicle	150	0%	150	0%
<b>Total</b>	<b>1,539,044</b>	<b>100%</b>	<b>1,628,997</b>	<b>100%</b>

### 13. CURRENT ASSETS AND LIABILITIES

The current assets of the Fund are analysed as follows:

	31 March 2020 £000	31 March 2019 £000
Contribution due from employers	1,116	3,175
Other current assets	2,717	2,352
Cash at managers	18,448	3,825
Cash and bank	21,957	4,843
<b>Total</b>	<b>44,238</b>	<b>14,195</b>

The current liabilities of the Fund are analysed as follows:

	31 March 2020 £000	31 March 2019 £000
Benefits	(15)	(3)
Professional fees	(2,283)	(842)
Investment	(2,072)	(2,006)
Taxes	(604)	(602)
Other	(478)	(1)
<b>Total</b>	<b>(5,452)</b>	<b>(3,454)</b>

### 14. RELATED PARTY TRANSACTIONS

The Fund is required to disclose details of its financial relationship with related third parties. This has been defined as where the related party has, or is perceived to have, real influence over any transaction between the parties.

Through its administration of the Fund, the Council has a related party interest with the Fund, and the costs charged by the Council are disclosed in note 31.

Management of the Fund is the responsibility of the Council's Strategic Director of Finance and Governance (SDFG). No officers' remuneration is paid directly by the Fund; costs are instead recovered as part of the costs disclosed in note 10. The SDFG remuneration is disclosed in note 29 of the Council's Statement of Accounts.

The Pension Advisory Panel (PAP) offers advice to the SDFG. Councillor members of the PAP make an annual declaration of their interests which is available on the Council's website.

The Council is also the single largest employer of members of the Fund and contributed £38.3 million to the Fund in 2019-20 (£39.9 million in 2018-19).

## 15. FAIR VALUE HIERARCHY

The valuation of financial instruments has been classified into three levels in accordance with IFRS 13, according to the quality and reliability of information used to determine fair values.

Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprises of quoted equities, quoted fixed securities, quoted index linked securities and unit trusts. Listed investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data. They comprise property unit trusts.

Level 3 are those where at least one input that could have a significant effect on the instruments valuation is not based on observable market data.

Description of asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivities affecting valuations provided
Market quoted investments	Level 1	Published bid market price ruling on the final day of the accounting period	Not required	Not required
Quoted bonds	Level 1	Fixed interest securities are valued at a market value based on current yields	Not required	Not required
Futures and options in UK bonds	Level 1	Published exchange prices at the year-end	Not required	Not required
Exchange traded pooled investments	Level 1	Closing bid value on published exchanges	Not required	Not required
Unquoted bonds	Level 2	Average of broker prices	Evaluated price feeds	Not required
Forward foreign exchange derivatives	Level 2	Market forward exchange rates at the year-end	Exchange rate risk	Not required
Overseas bond options	Level 2	Option pricing model	Annualised volatility of counterparty credit risk	Not required
Pooled investments – overseas unit trusts and some property funds	Level 2	Closing bid price where bid and offer prices are published Closing single price where single price published	NAV-based pricing set on a forward pricing basis	Not required
Freehold, leasehold properties	Level 3	Valued at fair value at the year-end by independent valuers	Existing lease terms and rentals; Independent market research; Nature of tenancies; Covenant strength for existing tenants; Assumed vacancy levels; Estimated rental growth; Discount rate	Significant changes in rental growth, vacancy levels or the discount rate could affect valuations as could more general changes to market prices
Infrastructure funds	Level 3	Valued by fund manager at the lower of fair value and cost	Purchase price at acquisition for newer or non-operational assets, estimated cash flows, government price support	Market prices and cash yields, government policies on energy subsidies, pace of shift to renewable and clean energy, discount rates

The following table shows the fair value valuation hierarchy of fund assets and liabilities.

Value as at 31 March 2020	Quoted market price	Using observable inputs	With significant un-Observable inputs	Total
	Level 1	Level 2	Level 3	
	£000	£000	£000	
Financial assets at fair value through profit and loss	977,310	283,961	88,223	1,349,494
Non-financial assets at fair value through profit and loss	-	-	189,550	189,550
<b>Total</b>	<b>977,310</b>	<b>283,961</b>	<b>277,773</b>	<b>1,539,044</b>

Value as at 31 March 2019	Quoted market price	Using observable inputs	With significant un-Observable inputs	Total
	Level 1	Level 2	Level 3	
	£000	£000	£000	
Financial assets at fair value through profit and loss	1,046,474	292,393	67,658	1,406,525
Non-financial assets at fair value through profit and loss	-	-	222,470	222,470
<b>Total</b>	<b>1,046,474</b>	<b>292,393</b>	<b>290,128</b>	<b>1,628,995</b>

The following table shows the reconciliation of fair value measurements within level three:

Value as at 31 March 2020	Value at 31 March 2019	Purchase	Realised Sales gain/(loss)	Unrealised gain/(loss)	Value at 31 March 2020	
	£000	£000	£000	£000	£000	
Property	290,129	6,182	(41,289)	5,001	(14,053)	245,970
Infrastructure	-	32,454	(426)	-	(225)	31,803
<b>Total</b>	<b>290,129</b>	<b>38,636</b>	<b>(41,715)</b>	<b>5,001</b>	<b>(14,278)</b>	<b>277,773</b>

Value as at 31 March 2019	Value at 31 March 2018	Purchase	Sales	Realised gain/(loss)	Unrealised gain/(loss)	Value at 31 March 2019
	£000	£000	£000	£000	£000	£000
Property	266,190	27,563	(7,757)	1,097	3,036	290,129
<b>Total</b>	266,190	27,563	(7,757)	1,097	3,036	290,129

The sensitivity of pricing methodology for property assets within fair value level three is considered to be +/-7%.

This equates to a pricing volatility of +/- £17 million for property assets as at 31 March 2020 (£16 million as at 31 March 2019).

## 16. FINANCIAL INSTRUMENTS

The following table shows the classification of the Fund's financial instruments:

	31 March 2020	31 March 2019
	£000	£000
<b>Financial assets</b>		
Fair value through profit and loss	1,349,494	1,431,416
Amortised cost	46,833	13,268
<b>Financial liabilities</b>		
Amortised cost	(5,452)	(3,454)
<b>Total</b>	<b>1,390,875</b>	<b>1,441,230</b>

## 17. CONTINGENT LIABILITIES AND CONTRACTUAL ARRANGEMENTS

Outstanding capital commitments (investments) at 31 March 2020 totalled £76.8 million (31 March 2019: £21.2 million).

These commitments relate to outstanding call payments due on property and infrastructure funds. The amounts 'called' by these funds are irregular in both size and timing over a number of years from the date of each original commitment.

## 18. NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS

### Risk and risk management

The Fund's primary long-term risk is that the Fund's assets will fall short of its liabilities (i.e. promised benefits payable to members). Therefore the aim of investment risk management is to minimise the risk of an overall reduction in the value of the Fund and to maximise the opportunity for gains across the whole portfolio. The Fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) and credit risk to an acceptable level. In addition, the Fund manages its liquidity risk to ensure there is sufficient liquidity to meet the Fund's forecast cash flows. The Council manages these investment risks as part of its overall pension Fund risk management programme.

Responsibility for the Fund's risk management strategy rests with the Strategic Director of Finance and Governance advised by the Pensions Advisory Panel. Risk management policies are established to identify and analyse the risks faced by the Council's pensions operations. Policies are reviewed regularly to reflect changes in activity and in market conditions.

### Market risk

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.

The objective of the Fund's risk management strategy is to identify, manage and control market risk exposure within acceptable parameters, whilst optimising the return on risk.

In general, excessive volatility in market risk is managed through the diversification of the portfolio in terms of geographical and industry sectors and individual securities. To mitigate market risk, the council and its investment advisers undertake appropriate monitoring of market conditions and benchmark analysis.

### Price risk

Price risk represents the risk that the value of a financial instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate risk or foreign exchange risk), whether those changes are caused by factors specific to the individual instrument or its issuer or factors affecting all such instruments in the market.

The Fund is exposed to share price risk. This arises from investments held by the Fund for which the future price is uncertain. All security investments present a risk of a loss of capital. The maximum risk resulting from financial instruments is determined by the fair value of the financial instruments.

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

Potential price changes are determined based on historical data and volatility of asset class returns. For example, 'riskier' assets such as equities will display greater potential volatility than bonds. The following table demonstrates the change in the net assets available to pay benefits if the market price had increased or decreased. In consultation with the Fund's investment advisers, the Council has determined that the following movements in market price risk are reasonably possible for 2019-20 reporting period:

2019-20 - asset type	31 March	Change	Value on	Value on
	2020		increase	decrease
	£000	%	£000	£000
Total equities	817,707	11%	904,377	731,079
Total bonds and index-linked	280,541	5%	294,894	266,188
Multi-asset	163,023	5%	171,686	154,361
Alternatives	31,803	3%	32,672	30,933
Property	245,970	3%	253,766	238,172
Other assets	3,711	0%	3,711	3,711
<b>Total investment assets</b>	<b>1,542,755</b>			

2018-19 - asset type	31 March	Change	Value on	Value on
	2019		increase	decrease
	£000	%	£000	£000
Total equities	889,072	9%	969,088	809,056
Total bonds and index-linked	282,081	7%	301,827	262,335
Multi-asset	167,475	4%	174,174	160,776
Property	290,129	3%	298,833	281,425
Other assets	2,488	0%	2,488	2,488
<b>Total investment assets</b>	<b>1,631,245</b>			

The potential changes disclosed above are broadly consistent with a one-standard deviation movement in the value of the assets. The sensitivities are consistent with the assumptions contained in the investment advisers' most recent review. The analysis assumes that all other variables, in particular foreign currency exchange rates and interest rates, remain the same.

Had the market price of the Fund's investments increased/decreased in line with the above, the change in the net assets available to pay benefits in the market price would have been as shown in the table above.

### Interest rate risk

The Fund invests in financial assets for the primary purpose of obtaining a return on investments. Fixed interest securities and cash are subject to interest rate risks, which represent the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Fund's interest rate risk is routinely monitored by the council and its investment advisers in accordance with the fund's risk management strategy, including monitoring the exposure to interest rates and assessment of actual interest rates against the relevant benchmarks.



Fixed interest securities are exposed to interest rate risk. The table below demonstrates the change in value of these assets had the interest rate increased or decreased by 1%:

Assets exposed to interest rate risks	Market value		
	£000	Value on 1% rate increase £000	Value on 1% rate decrease £000
As at 31 March 2020	126,966	128,236	125,696
As at 31 March 2019	124,768	126,016	123,520

### Currency risk

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than sterling. A strengthening/weakening of the pound against the various currencies in which the Fund holds investments would increase/decrease the net assets available to pay benefits.

The Fund's currency risk is routinely monitored by the Council and its investment advisers in accordance with the Fund's risk management strategy, including monitoring the range of exposure to currency fluctuations.

Overseas equities, fixed interest securities and futures, cash in foreign currencies and some elements of pooled investment vehicles are exposed to currency risk. The following table demonstrates the change in value of assets exposed to currency risk had there been a 10% strengthening or weakening of the pound against foreign currencies.

Assets exposed to currency risk	Value £000	Change %	Value on foreign exchange rate increase	Value on foreign exchange rate decrease
			£000	£000
As at 31 March 2020	912,962	10	1,004,258	821,666
As at 31 March 2019	982,765	10	1,081,042	884,489

### Credit risk

This is the risk the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. For example, a stock may lose value or a dividend due may not be paid. The market values of investments generally reflect an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the Fund's financial assets and liabilities.

The Fund has set out a series of restrictions in each investment manager's agreement. These restrictions are intended to limit the risks from each individual investment and prevent unsuitable investment activity. The Fund also employs a global custodian to ensure that all transactions are settled in a timely manner.

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## Liquidity risk

This is the risk that the Fund may not have the funds available to meet payments as they fall due. Historically the Fund has been cash positive (i.e. contributions received have been greater than benefits paid out). However, in recent years this has reversed with benefits paid now surpassing contributions received. The reduction in active members and a resulting change in the membership profile have increased the liquidity risk of the Fund going forward.

The Fund currently has two bank accounts. One is held by the global custodian and holds cash relating to investment activities, the other is the Fund bank account, which holds the cash relating to member activities.

There is a strategy in place to forecast all income and expenditure for the Fund to ensure that sufficient funds will be made available to meet short-term commitments. In the event that there are insufficient available assets to meet liabilities when they fall due, the Fund would be able to redeem investment assets and recall cash resources from investment managers at short notice to meet this requirement.

## 19. ACTUARIAL POSITION OF THE FUND

### Introduction

The Scheme Regulations require that a full actuarial valuation be carried out every third year. The purpose of this is to establish that the London Borough of Southwark Pension Fund (the Fund) is able to meet its liabilities to past and present contributors and to review employer contribution rates. The last full actuarial investigation into the financial position of the Fund was completed as at 31 March 2019 by Aon, in accordance with Regulation 62 of the Local Government Pension Scheme Regulations 2013.

### Actuarial position

1. The valuation as at 31 March 2019 showed that the funding level of the Fund had increased since the previous valuation with the market value of the Fund's assets as at 31 March 2019 (of £1,642.0 million) covering 103% of the liabilities allowing, in the case of pre-1 April 2014 membership for current contributors to the Fund, for future increases in pensionable pay, and for other membership for future pension revaluation and increases.
  
2. The valuation also showed that the aggregate level of contributions required to be paid by participating employers with effect from 1 April 2020 was:
  - 18.3% per year of pensionable pay. This is the rate calculated as being sufficient, together with contributions paid by members, to meet the liabilities arising in respect of service after the valuation date (the primary rate),
  
  - Plus**
  - An allowance of 1.5% per year of pensionable pay for McCloud and cost management – see paragraph 9,
  
  - Less**
  - 1.5% per year of pensionable pay to remove surplus, over a recovery period of 20 years from 1 April 2020 (which together with the allowance above for McCloud and cost management comprises the secondary rate).
  
3. In practice, each individual employer's or group of employers' position is assessed separately taking into account other factors (see note 4) and contributions are set out in Aon's report dated 30 March 2020 (the actuarial valuation report). In addition to the contributions certified, payments to cover additional liabilities such as those arising from early retirements and ill-health retirements will be made to the Fund by the employers.

Year from 1 April	% of pensionable pay	Plus total contribution amount (£m)
2020	21.8	0.3
2021	21.6	-
2022	21.1	-

4. The funding plan adopted in assessing the contributions for each employer is in accordance with the Funding Strategy Statement. Different approaches were adopted in relation to the calculation of the primary contribution rate and stepping of contribution changes and grouping of employer contributions as agreed with the administering authority and reflected in the Funding Strategy Statement, reflecting the employers' circumstances. This included an agreement that where employers are in surplus, this has only led to an adjustment in contributions to the extent that this surplus is in excess of 10% of the value of that employer's liabilities (i.e. to the extent that the employer's funding level is greater than 110%).
5. The valuation was carried out using the projected unit actuarial method for most employers and the main financial actuarial assumptions used for assessing the funding target and the contribution rates were as follows:

Discount rate for periods in service	4.05% per year
Discount rate for periods after leaving service	4.05% per year
Rate of pay increases	3.60% per year
Rate of increase to pension accounts	2.10% per year
Rate of increases in pensions in payment (in excess of GMP)	2.10% per year

The assets were valued at market value. Further details of the assumptions adopted for the valuation, including the demographic assumptions, are set out in the actuarial valuation report.

6. The key demographic assumption was the allowance made for longevity. The post retirement mortality assumption adopted for the actuarial valuation was in line with standard self-administered pension scheme (SAPS) S2 Heavy mortality tables with appropriate scaling factors applied based on an analysis of the Fund's pensioner mortality experience and a Fund membership postcode analysis using Aon's Demographic Horizons™ longevity model, and included an allowance for improvements based on the 2018 Continuous Mortality Investigation (CMI) Core Projections Model (CMI2018), with a long-term annual rate of improvement in mortality rates of 1.5% per year. The resulting average future life expectancies at age 65 (for normal health retirements) were:

	Men	Women

Current pensioners aged 65 at the valuation date	20.7	23.5
Future pensioners aged 45 at the valuation date	22.5	25.4

7. The valuation results summarised in paragraphs 1 and 2 are based on the financial position and market levels at the valuation date, 31 March 2019. As such the results do not make allowance for changes which have occurred subsequent to the valuation date, although we comment on changes in market conditions to 31 March 2020 in paragraph 10.
8. The formal actuarial valuation report and the Rates and Adjustments Certificate setting out the employer contribution rates for the period from 1 April 2020 to 31 March 2023 were signed on 30 March 2020. Other than as agreed or otherwise permitted or required by the Regulations, employer contribution rates will be reviewed at the next actuarial valuation of the Fund as at 31 March 2022 in accordance with Regulation 62 of the Local Government Pension Scheme Regulations 2013.
9. There are a number of uncertainties regarding the Fund benefits and hence liabilities:

- **Increases to Guaranteed Minimum Pensions (GMPs):**

The 2019 valuation allows for the extension of the 'interim solution' for public service schemes to pay full inflationary increases on GMPs for those reaching State Pension Age (SPA) between 6 April 2016 and 5 April 2021. However, the Government is still exploring various options, including conversion of GMPs to Scheme benefits, in order to achieve equalisation for GMPs as required by the High Court judgement in the Lloyds Bank case.

The results of the 2019 valuation do not allow for the impact of potentially extending this interim solution indefinitely, providing full pension increases on GMPs for members reaching SPA after 5 April 2021 nor for conversion of GMPs to Scheme benefits. Based on approximate calculations, at a whole of fund level, the impact of providing full pension increases on GMPs for those members reaching SPA after 5 April 2021 is an increase in past service liabilities of between 0.1% to 0.2% across the Fund as a whole.

- **Cost management process and McCloud judgement:**

Initial results from the Scheme Advisory Board cost management process indicated that benefit improvements/member contribution reductions equivalent to 0.9% of pay would be required. However, the cost management process was paused following the Court of Appeal ruling that the transitional arrangements in both the Judges' Pension Scheme (McCloud) and Firefighters' Pension Scheme (Sargeant) constituted illegal age discrimination. Government confirmed that the judgement would be treated as applying to all public service schemes including the LGPS (where the transitional arrangements were in the form of a final salary underpin) and a consultation on changes to the LGPS is expected in June 2020.

The employer contributions certified from 1 April 2020 as part of the 2019 valuation include an allowance of 1.5% of pay in relation to the potential additional costs following the McCloud judgement/cost management process. This was a simplified approach which didn't take account of different employer membership profiles or funding targets and may be more or less than the assessed cost once the LGPS changes have been agreed depending upon the precise nature of the new final salary underpin, the members in scope, and how this affects the cost management process.

10. Since the valuation date, Fund asset returns have fallen short of the assumed return of 4.05% over the year to 31 March 2020, on its own leading to a reduction in the funding level. In addition, reduced expectations of future asset returns and have led to a decrease in the discount rates, and expected future inflation linked benefit increases have increased, further reducing funding levels and increasing the primary rate. The Actuary, in conjunction with the administering authority, will monitor the position on a regular basis and the administering authority will take action if it believes necessary.
11. This Statement has been prepared by the Actuary to the Fund, Aon, for inclusion in the accounts of the Fund. It provides a summary of the results of the actuarial valuation which was carried out as at 31 March 2019. 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 does not accept any responsibility or liability to any party other than our client, the London Borough of Southwark, the administering authority of the Fund, in respect of this Statement.

The report on the actuarial valuation as at 31 March 2019 is available on request from the London Borough of Southwark, the administering authority of the Fund.

## Aon Hewitt Limited

### May 2020

IAS 26 (retirement benefit plans) requires the 'actuarial present value of promised retirement benefits' to be disclosed in the Fund Accounts using the most recent actuarial valuation. The Fund was last valued as at 31 March 2019.

	<b>31 March</b>	<b>31 March</b>
	<b>2019</b>	<b>2016</b>
	<b>£m</b>	<b>£m</b>
Fair value of net assets	1,642	1,256
Actuarial present value of promised retirement benefits	(2,192)	(1,671)
Surplus/(deficit) in the fund as measured for IAS 26	<b>(550)</b>	<b>(415)</b>

## **McCloud Judgement**

In December 2018, the Court of Appeal ruled against the Government in the 'McCloud /Sargeant' judgement which found that the transitional protection arrangements put in place when the firefighters' and judges' pension schemes were reformed amounted to illegal age discrimination. The ruling potentially has implications for all public sector schemes which were reformed around the same time and could lead to members who were discriminated against being compensated.

The Government applied to the Supreme Court for permission to appeal this judgement, but the Supreme Court rejected the Government's request on 27 June 2019, and on 15 July the Chief Secretary to the Treasury announced in a written statement confirming that the Government believes that the difference in treatment will need to be remedied across all public service schemes, including the LGPS. The next stage is for the case to be referred to the Employment Tribunal to agree the remedy, following appropriate consultation. Whilst the remedy is uncertain, a prudent approach would be to assume it is equivalent to extending the 'best of both' underpin to all members.

The Government Actuary's Department (GAD), under instruction of the LGPS Scheme Advisory Board (England and Wales) was asked to calculate the worst case scenario impact at Scheme level, and in their paper titled 'Local Government Pension Scheme Potential impact of McCloud/Sargeant ruling on pension accounts disclosures' dated 10 June 2019, they state, that using an effective date of 31 March 2019, financial assumptions appropriate for accounting purposes and a salary increase assumption of CPI + 1.5% (as used for the London Borough of Southwark Pension Fund), the estimated worst case scenario impact will be a 3.2% increase in the active liabilities. This was very much an estimate, is based on the Scheme as a whole and made no allowance for 'high fliers' who could distort these figures. The figures for London Borough of Southwark could be different to this GAD assessment but we feel gives a reasonable indication of the increase in liabilities.

## **GMP equalisation and indexation**

On 26 October 2018, the High Court ruled in the Lloyds Bank case that equalisation for the effect of unequal Guaranteed Minimum Pensions (GMPs) is required. The ruling confirmed that trustees have a duty 'to equalise benefits for men and women so as to alter the result which is at present produced in relation to GMPs.'

In March 2016, the Government introduced an interim solution for members in public sector schemes with GMPs who were set to lose out from the removal of the Additional State Pension (AP). This was done by paying full increases on GMP pensions for individuals reaching State Pension Age (SPA) from 5 April 2016 through 5 December 2018 (GMP Rules do not require schemes to pay any increases on GMPs earned before April 1988, and cap increases at 3% per year on GMPs earned after April 1988). This additional liability was included in the liabilities disclosed.

## **20. POST BALANCE SHEET EVENTS**

No such material events have occurred.

## **GLOSSARY**

### **ACCOUNTING STANDARDS**

These are the 'proper accounting practices' that the council must follow. They comprise laws and regulations, which are set out in Acts of Parliament and in codes of practice recommended by professional bodies.

### **ACCRUAL**

An accounting principle where income and expenditure is recognised as it is earned or spent rather than when money is received or paid. This concept is reflected in the accounts by the inclusion of debtors and creditors.

### **ACTUARIAL GAINS AND LOSSES**

These arise where actual events have not coincided with the actuarial assumptions made for the last valuations or the actuarial assumptions have changed.

### **ASSET**

An item having value to the council in monetary terms. Assets are categorised as either current or non-current:

- A current asset will be consumed or cease to have material value within the next financial year (e.g. cash and stock); and
- A non-current asset provides benefits to the council and to the services it provides for a period of more than one year and may be tangible e.g. a community centre, or intangible, e.g. computer software licences.

### **CASH EQUIVALENTS**

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

### **CONTINGENT ASSET**

A contingent asset is a possible asset arising from past events whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the Council's control.



## **CONTINGENT LIABILITY**

- A possible obligation arising from past events whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the Council's control; or
- A present obligation arising from past events where it is not probable that a transfer of economic benefits will be required, or the amount of the obligation cannot be measured with sufficient reliability.

## **CREDITORS**

Amounts owed by the Council for goods and services received but not paid for as at 31 March.

## **DEBTORS**

Amounts owed to the Council for goods and services provided but where the associated income was not received as at 31 March.

## **EVENTS AFTER THE BALANCE SHEET DATE**

Events after the balance sheet date are those events, favourable or unfavourable.

## **FAIR VALUE**

The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

## **IAS 19**

International Accounting Standard 19 is based on the principle that an organisation should account for retirement benefits when it is committed to give them, even if the actual giving will be many years into the future.

## **INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)**

The Accounting standards adopted by the International Accounting Standards Board (IASB). Local Authorities are required to produce full accounts using IFRS.

## **NET BOOK VALUE**

The amount at which non-current assets are included in the balance sheet, i.e. their historical cost or current value less the cumulative amount provided for depreciation.

## **NET REALISABLE VALUE**

The open market value of the asset in its existing use (or open market value in the case of non-operational assets), less the expenses to be incurred in realising the asset.

## **RELATED PARTIES**

Two or more parties are related parties when at any time during the financial period:

- One party has direct or indirect control of the other party; or
- The parties are subject to common control from the same source; or  
One party has influence over the financial and operational policies of the other party to an extent that the other party might be inhibited from pursuing at all times its own separate interests; or
- The parties, in entering a transaction, are subject to influence from the same source to such an extent that one of the parties to the transaction has subordinated its own separate interest; or
- The parties, or any member of a group of which it is a part, provides key management personnel services to the other, or to the parent of the other, reporting entity.

## **RELATED PARTY TRANSACTION**

A related party transaction is the transfer of assets or liabilities or the performance of services by, to or for a related party, irrespective of whether a charge is made.

# APPENDIX 3 – Funding Strategy Statement

## SECTION 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 58 of the Local Government Pension Scheme Regulations 2013 (as amended) (the Regulations). The Statement describes the London Borough of Southwark's strategy, in its capacity as Administering Authority, for the funding of the London Borough of Southwark Pension Fund (the Fund).

As required by Regulation 58, the Statement has been reviewed (and where appropriate revised) having regard to guidance published by CIPFA. The statement has also been reviewed having regard to updated guidance published by CIPFA in September 2016, and not the original guidance issued in October 2012 as referred to in the LGPS Regulations at time of writing this Statement.

#### Consultation

In accordance with Regulation 58, the administering authority has consulted such persons as it considers appropriate 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 Investment Strategy Statement published under Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the Investment Regulations).

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

#### Policy purpose

The purpose of this Funding Strategy Statement is to document the processes by which the administering authority:

- Establishes a clear and transparent fund-specific strategy that will identify how employer's pension liabilities are best met going forward;
- Supports the regulatory requirement in relation to the desirability of maintaining as nearly constant primary employer contribution rates as possible;
- Ensures that the regulatory requirements to set contributions as to ensure the solvency and long-term cost efficiency of the Fund are met; and
- Takes a prudent longer-term view of funding the Fund's liabilities.

**Links to investment policy set out in the Statement of Investment Principles (SIP)**

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 Investment Strategy Statement 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 Investment Strategy Statement 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 this Statement**

The administering authority undertook its latest substantive review of this Statement in January 2020.

The administering authority will formally review this Statement as part of the triennial valuation following the 31 March 2019 valuation, currently expected to be as at 31 March 2022, 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 valuations, and will discuss with the Fund Actuary whether any significant changes have arisen that require action.

## SECTION 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 in order to:

- Produce a Fund to pay Scheme benefits, transfer values, costs, charges and expenses as defined in the LGPS Regulations and as required in the Investment Regulations over the long term and in so doing; and
- To smooth out the contributions required from employers over the long term.

#### Aims of the Fund

The main aims of the Fund are:

**a) To comply with Regulation 62 of the Regulations** and specifically to:

- Adequately fund benefits to secure the Fund's solvency and long-term cost efficiency, which should be assessed in light of the risk profile of the Fund and employers;
- Take account of the desirability of maintaining as nearly constant primary employer contribution rates as possible (and subject to the administering authority not taking undue risks) at reasonable cost to the taxpayers, scheduled (as defined in Part 1 or deemed employers as per Part 4 of Schedule 2 of the LGPS Regulations), resolution (as defined in Part 2 of Schedule 2 of the LGPS Regulations), and admitted bodies; and
- Enable overall employer contributions to be kept as constant as possible (and subject to the administering authority not taking undue risks) at reasonable cost to the taxpayers, scheduled, resolution and admitted bodies.

The administering authority recognises that the requirement to keep employer total contribution levels 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 bodies, admission bodies, other bodies and to taxpayers (subject to not taking undue risks); and
- Maximising income from investments within reasonable risk parameters (see later).

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

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 riskier in nature, and that risk can manifest itself in volatile returns over short-term periods, and a failure to deliver 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 on 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 on a monthly basis 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 properly 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 stocks are sought through investment in other asset classes such as stocks and property. The administering authority ensures that risk parameters are reasonable by:

- Complying with any restrictions set out in the Investment Regulations;
- Restricting investment to asset classes generally recognised as appropriate for UK pension funds;
- Analysing the potential volatility and absolute return risks, and funding risk represented by those asset classes in collaboration with Investment Advisors and Fund Managers, the Fund Actuary and the LCIV 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 that the investments do not move in line with the Fund's liabilities.

## SECTION 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:

#### **Administering authority**

The administering authority will:

- Administer the Fund;
- Collect employer and employee contributions, investment income and other amounts due to the Fund as stipulated in LGPS regulations and, as far as the Administering Authority is able to, ensure these contributions are paid by the due date;
- Pay from the Fund the relevant entitlements as stipulated by the Regulations;
- Invest surplus monies in accordance with the Investment Regulations;
- Ensure that cash is available to meet liabilities as and when they fall due;
- Manage the valuation process in consultation with the Fund's Actuary;
- Ensure 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 relevant guidance and Regulations.
- Prepare and maintain an Investment Strategy Statement and a Funding Strategy Statement after due consultation with persons the Administering Authority considers appropriate, and amend these two documents if required.
- Monitor all aspects of the Fund's performance and funding.
- Effectively manage any potential conflicts of interest arising from its dual role as both Administering Authority and Scheme employer; and
- Enable the Local Pension Board to review the valuation process as set out in their terms of reference.

#### **Individual employers**

Individual employers will:

- Deduct contributions from employees' pay;
- Pay all ongoing contributions, including their employer's contribution as determined by the Fund Actuary and where relevant set out in the rates and adjustment certificate, promptly by the due date;
- Develop a policy on certain discretions and exercise those discretions as permitted within the regulatory framework;

- Pay for additional membership or pension, augmentation, early release of benefits or other one off strain costs in accordance with agreed arrangements;
- 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 Investment Strategy Statement or other policies and
- Pay any exit payments as required in the event of their ceasing participation in the Fund.

## **Fund Actuary**

The Fund Actuary will prepare advice and calculations and provide advice on:

- Funding strategy and the preparation of the Funding Strategy Statement;
- Actuarial valuations including the setting of employers' contribution rates and issue of a Rates and Adjustments Certificate, after agreeing assumptions with the Administering Authority and having regard to the Funding Strategy Statement and the LGPS Regulations;
- Bulk transfers and individual benefit-related matters such as pension strain costs, compensatory added years costs, etc;
- Valuations of exiting employers; and
- Bonds and other forms of security for the Administering Authority against the financial effect on the Fund of employers' default.

Such advice will take account of the funding position and Funding Strategy Statement of the Fund, along with other relevant matters.

The Fund Actuary will assist the Administering Authority in assessing whether employer contributions need to be revised between actuarial valuations as required by the Regulations.

The Fund Actuary will ensure that the Administering Authority is aware of any professional guidance requirements which may be of relevance to his or her role in advising the Administering Authority.



## SECTION 4

### FUNDING TARGET, SOLVENCY AND NOTIONAL SUB FUNDS

#### 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:

- What the Solvency Target should be (the funding objective - where the Administering Authority wants the Fund to get to);
- The Trajectory Period (how quickly the Administering Authority wants the Fund wants to get there); and
- The Probability of Funding Success (how likely the Administering Authority wants it to be now that the Fund will actually achieve the Solvency Target by the end of the Trajectory Period).

These three choices, supported by risk modelling carried out by the Fund's 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 and Funding Target

##### Solvency and 'funding success'

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, using appropriate actuarial assumptions. The Solvency Target is the amount of assets which the Fund, having taken advice from the Fund Actuary, wishes 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 methods and assumptions.

The Administering Authority believes that its funding strategy will ensure the solvency of the Fund because employers collectively have the financial capacity to increase employer contributions should future circumstances require, in order to continue to target a funding level of 100%.

For secure tax raising scheduled bodies and admission bodies with Guarantors of sound covenant agreeing to subsume assets and liabilities following exit, the Solvency Target will use appropriate actuarial methods and assumptions that are believed appropriate in the long term for those bodies. For the 2019 valuation the Solvency Target will be set using an assumed rate of return of 2% in excess of the assumed long term annual increase in the Consumer Prices Index, which is intended to be a prudent outperformance assumption based on assumed future asset holdings.

For admission bodies and other bodies whose liabilities are expected to be orphaned following exit, the required Solvency Target 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 exit.

##### 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, and asset-liability modelling carried out by the Fund Actuary.

Consistent with the Administering Authority's aim of enabling employers' contribution levels to be kept as nearly constant as possible, the required chance of achieving the Solvency Target at the end of the relevant Trajectory Period for each employer or employer group can be altered at successive valuations within an overall envelope of acceptable risk.

The Administering Authority will not permit contributions to be set following a valuation that have an unacceptably low chance of achieving the Solvency Target at the end of the relevant Trajectory Period.

### **Trajectory 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.

Maintaining a stable Trajectory Period avoids undue volatility when setting long-term assumptions for the Fund, where the Administering Authority would in ideal circumstances look to reduce the Recovery Period over time in order to achieve full funding. A Trajectory Period of 25 years will be used for the valuation at 31 March 2019.

### **Funding Target**

The Funding Target is the amount of assets which the Fund needs to hold at the valuation date to pay the liabilities at that date as indicated by the chosen valuation method and assumptions. It is a product of the actuarial valuation exercise and is not 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 serves 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 discount rate, and hence the overall required level of employer contributions, has been set at the valuation at 31 March 2019 such that the Fund Actuary estimates there a 78% chance that the Fund would reach or exceed its Solvency Target after 25 years.

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

- Primary 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; and
- For admission bodies the Administering Authority will take into account the potential for participation to cease, the potential timing of such exit, and any likely change in investment strategy regarding the assets held in respect of the admission body's liabilities at the date of exit.

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

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

### **Scheduled bodies and certain other bodies of sound covenant**

The Administering Authority will adopt a general approach in this regard of assuming indefinite investment in a broad range of assets of higher risk than low risk assets for secure tax raising Scheduled Bodies whose participation in the Fund is considered by the Administering Authority to be indefinite and certain other bodies which are long-term in nature i.e. admission bodies with a subsumption commitment from such scheduled bodies. This is known as the scheduled and subsumption body funding target.

For other scheduled bodies, the Administering Authority may without limitation, take into account the following factors when setting the funding target for such bodies:

- The type/group of the employer;
- The business plans of the employer;
- An assessment of the financial covenant of the employer; and
- Any contingent security available to the Fund or offered by the employer such as a Guarantor or bond arrangements, charge over assets, etc.

### **Admission bodies falling under London Borough of Southwark policy**

The London Borough of Southwark, as an employer, introduced an admissions policy following the actuarial valuation at 31 March 2010 whereby the pensions risk of new admission bodies is underwritten by London Borough of Southwark, and in return the employer's contribution is fixed at the rate at initial entry to the Fund (potentially subject to certain provisos). The Administering Authority has agreed that these contribution rates can be reflected in the actuarial valuation and set out in the Rates and Adjustment Certificate.

The London Borough of Southwark subsequently extended this approach to admission bodies joined the Fund prior to the introduction of this admissions policy with contributions payable at a fixed rate as determined as part of the 31 March 2013 valuation process.

The above policies affect all admission bodies participating in the Fund at the 2019 valuation.

### **Admission bodies and certain other bodies whose participation is limited and not subject to a guarantee**

For admission bodies, bodies closed to new entrants and other bodies whose participation in the Fund is believed to be of limited duration through known constraints or reduced covenant, and for which no access to further funding would be available to the Fund after exit the Administering Authority will have specific regard to the potential for participation to cease (or to have no contributing members), the potential timing of such exit, and any likely change in notional or actual investment strategy as regards the assets held in respect of the body's liabilities at the date of exit (i.e. whether the liabilities will become 'orphaned' or whether a Guarantor exists to subsume the notional assets and liabilities). This is known as the (ongoing) orphan admission bodies funding target. It is not the same as the exit basis.

At the 2019 valuation no employers fell into this category.

## Full funding

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

## Other aspects of the Funding Strategy

### Recovery Periods

Where a valuation reveals that the Fund is in surplus or deficiency against the Funding Target, employers' contribution rates will be adjusted to target restoration of fully funding the solvent position over a period of years (the Recovery Period). The Recovery Period to an employer or group of employers is therefore the 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.

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, and whether the employer is in surplus or deficit on the appropriate Funding Target.

Where an employer is in surplus, and where an employer's expected exit date is unknown or expected to be later than the date the revised rates and adjustments certificate will come into force following the next valuation, this surplus will only lead to an adjustment in an employer's contributions to the extent that this surplus is in excess of 10% of the value of that employer's liabilities valued relative to the appropriate Funding Target (i.e. to the extent that the employer's funding level is greater than 110%).

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, and where the employer is in deficit, the Administering Authority may be prepared to agree to Recovery Periods which are longer than the average future working lifetime of the membership of that employer. The Administering Authority recognises that such an approach is consistent with the aim of keeping employer contribution levels as nearly constant as possible. However, the Administering Authority also recognises the risk in relying on long Recovery Periods and has agreed with the Fund Actuary a limit of 30 years, for employers which are assessed by the Administering Authority as being a long term secure employer.

Where employers are in deficit, the Administering Authority's policy is to agree Recovery Periods with each employer which are as short as possible within the above framework. 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.

A period of 20 years has been used for the London Borough of Southwark, at the valuation at 31 March 2019 which is the largest employer in the Fund.

## Grouping

In some circumstances it may be desirable to group employers within the Fund together for funding purposes (i.e. to calculate employer contribution requirements). 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 the initial grouping and at each valuation and to notify each employer that is grouped which other employers it is grouped with and details of the grouping method used. If the employer objects to this grouping, it will be set its own contribution rate. For employers with more than 50 contributing members, the Administering Authority would look for evidence of homogeneity between employers before considering grouping. For employers, whose participation is for a fixed period grouping is unlikely to be permitted, unless the grouping is with the letting authority for the purpose of risk sharing arrangements.

Where employers are grouped together for funding purposes, this will only occur with the consent of the employers involved.

All employers in the Fund are grouped together in respect of the risks associated with payment of lump sum benefits on death in service – in other words, the cost of such benefits is shared across the employers in the Fund. Such lump sum benefits can cause funding strains which could be significant for some of the smaller employers without insurance or sharing of risks. The Fund, in view of its size, does not see it as cost effective or necessary to insure these benefits externally and this is seen as a pragmatic and low cost approach to spreading the risk.

### **Stepping**

Again, consistent with the desirability of keeping primary (and overall) employer contribution levels as nearly constant as possible, the Administering Authority will consider, at each valuation, whether new contribution rates should be payable immediately, or should be reached by a series of steps over future years. The Administering Authority will discuss with the Fund Actuary the risks inherent in such an approach, and will examine the financial impact and risks associated with each employer. The Administering Authority's policy is that in the normal course of events no more than three annual steps will be permitted. Further steps may be permitted in extreme cases in consultation with the Fund Actuary, but the total is very unlikely to exceed six steps.

### **Inter-valuation funding calculations**

In order to monitor developments, the Administering Authority may from time to time request informal valuations or other calculations. Generally, in such cases the calculations will be based on an approximate roll forward of asset and liability values, and 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 funding valuations.

## Asset shares notionally allocated to individual employers

### Notional asset shares

In order to establish contribution requirements for individual employers or groups of employers it is convenient to notionally subdivide the Fund as a whole between the employers (or group of employers where grouping operates), as if each employer had its own notional asset share within the Fund. Admission bodies with fixed contribution rates are grouped with the London Borough of Southwark for this purpose.

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 notional asset shares

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

Further adjustments are made for:

- A notional deduction to meet the expenses paid from the Fund in line with the assumption used at the previous valuation;
- Allowance for any known material internal transfers in the Fund (cash flows will not exist for these transfers). The Fund Actuary will assume an estimated cash flow equal to the value of the liabilities determined consistent with the Funding Target transferred from one employer to the other unless some other approach has been agreed between the two employers;
- Allowance for lump sum death in service and any other benefits shared across all employers (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 cash flow calculations. In such a circumstance:

- Where, in the opinion of the Fund Actuary, the cash flow data which is unavailable is of low materiality, or where estimated cashflows can be produced with reasonable accuracy, estimated cash flows will be used;
- Where, in the opinion of the Fund Actuary, the cash flow data which is unavailable is material, or difficult to estimate with necessary accuracy, the Fund Actuary may 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 cash flows and involve calculation of gains and losses relative to the surplus or deficiency exhibited at the previous valuation. Having established an expected surplus or deficiency at this valuation, comparison of this with the liabilities evaluated at this valuation leads to an implied notional asset holding; or
- Analysis of gains and losses methods will also be used where the results of the cash flow approach appears to give unreliable results perhaps because of unknown internal transfers.

## **Fund maturity**

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 consider requiring top up payments where deficit contributions fall below a minimum level, or further alternative approaches as it deems appropriate.

## **Long-term cost efficiency**

In order to ensure that measures taken to maintain stability of employer contributions are not inconsistent with the statutory objective for employer contributions to be set so as to ensure the long-term cost efficiency of the Fund, the Administering Authority has assessed the actual contributions payable by considering:

- The implied average deficit recovery period, allowing for the stepping of employer contribution changes;
- The investment return required to achieve full funding over the recovery period; and
- How the investment return compares to the Administering Authority's view of the expected future return being targeted by the Fund's investment strategy.

## SECTION 5

### SPECIAL CIRCUMSTANCES RELATED TO CERTAIN EMPLOYERS

#### Interim reviews

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

The Administering Authority's overriding objective at all times in relation to employers is that, where possible, there is clarity over the Funding Target for that employer, and that contribution rates payable are appropriate for that Funding Target. However, this is not always possible as any date of exit 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 exit is known, and is more than three years hence, or is unknown and participation is assumed to be indefinite, the Administering Authority will generally not deem it necessary to carry out an interim valuation;
- For admission bodies admitted under paragraph 1(d) of Part 3 Schedule 2 of the Regulations falling into the above category, the Administering Authority sees it as the responsibility of the relevant Scheme Employer to instruct it if an interim valuation is required. Such an exercise would be at the expense of the relevant Scheme Employer unless otherwise agreed;
- A material change in circumstances, such as the date of exit becoming known, material membership movements or material financial information coming to light may cause the Administering Authority to informally review the situation and subsequently formally request an interim valuation;
- For an employer, whose participation is due to cease within the next three years, the Administering Authority will keep an eye on 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 64(4) applies.

#### Guarantors

Some employer 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, and monitors the exposure of the 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; and
- During the period of participation of the employer a Guarantor can at any time agree to the future subsumption of any residual liabilities of an employer. The



effect of that action would be to reduce the Funding and Solvency Targets for the employer, which would probably lead to reduced contribution requirements.

## **New employers**

### **Initial rate**

When a new employer joins the Fund, the Fund's Actuary determines the initial employer contribution rate payable.

An interim contribution rate may be set pending a more accurate calculation by the Fund's Actuary of the employer contribution rate payable. The Administering Authority will determine these interim contribution rates following each Actuarial Valuation and at any other time at its discretion.

The employer contribution rate will be set in accordance with the Funding Strategy Statement, taking into consideration elements such as:

- Any past service or transferred liabilities;
- Whether the new employer is open or closed to new entrants;
- The funding target that applies to the employer;
- The funding level on commencement and, where there is a surplus or deficit, whether the admission agreement is fixed term or not, whether open or closed and the period of any fixed term contract period or average future working lifetime of the employee membership (as appropriate); and
- Other relevant circumstances as determined by the Administering Authority on the advice of the Fund Actuary.

### **New admission bodies**

Where the Administering Authority makes an admission agreement with a body (the new body), the default stance of the Fund is that the relevant Scheme employer, as defined in Part 3 of Schedule 2 of the LGPS Regulation 2013, will be required to retain ultimate responsibility for funding the liabilities of new admission body, with the admission body paying contributions in accordance with terms of the Admission Agreement or side agreement. This applies to both the liabilities of the initial transferring membership and, in the case of an open admission agreement, any liabilities of the new body relating to members that commence participation after the initial transfer under the terms of the Admission Agreement.

### **Bonds and other securitization**

Paragraph 6 of Part 3, Schedule 2 of the Regulations creates a requirement for a new admission body to carry out, to the satisfaction of the Administering Authority (and Scheme employer in the case of an admission body admitted under paragraph 1(d)(i) of that Part ), an assessment taking account of actuarial advice, of the level of risk arising on premature termination of the provision of service or assets 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 for any reason it is not desirable for an admission body to enter into an indemnity bond, the admission body is required to secure a guarantee in a form satisfactory to the Administering Authority from an organisation who either funds, owns or controls the functions of that admission body.

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

- In the case of admission bodies admitted under Paragraph 1(d) of Part 3, Schedule 2 of the Regulations and other admission bodies with a Guarantor, and so long as the Administering Authority judges the relevant Scheme employer or Guarantor to be of sufficiently sound covenant, any bond exists purely to protect the relevant Scheme employer 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 bond required from the admission body, if any. In this case, 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. Once the Scheme employer or Guarantor confirms their agreement to the level of bond cover proposed, the Administering Authority will be happy to provide a separate document to the admission body setting out the level of cover which the Administering Authority and Scheme employer/Guarantor consider suitable, but this should not be constructed as advice relevant to the admission body on this matter.
- In the case of:
  - Admission bodies admitted under paragraph 1(e) of Part 3, Schedule 2;
  - Admission bodies admitted under paragraph 1(d) of Part 3, Schedule 2 where the Administering Authority does not judge the Scheme employer to be of sufficiently strong covenant; and
  - Other admission bodies with no Guarantor or where the Administering Authority does not judge the Guarantor to be of sufficiently strong covenant; and
  - The admission will only be able to proceed once the Administering Authority has agreed the level of bond cover. As such, the Administering Authority will obtain some 'standard' calculations from the Fund Actuary to assist them to form a view on what level of bond would be satisfactory. The Administering Authority will be pleased to supply this calculation to the Scheme employer or Guarantor, where relevant, but this should not be construed as advice to the relevant Scheme employer or Guarantor on this matter. Once the Scheme employer or Guarantor, where relevant, confirms their agreement to the level of bond proposed, the Administering Authority will be happy to provide a separate document to the admission body setting out the level of cover which the Administering Authority and Scheme employer/Guarantor, where relevant, consider suitable but this should not be constructed as advice relevant to the admission body on this matter.
- The Administering Authority notes that levels of required bond cover can fluctuate and will review, or recommend that the 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 agrees 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 a mix of growth and matching assets.

### **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 will act on the basis that it will have no further access for funding from that employer once any exit valuation, carried out in accordance with Regulation 64, 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 arises on the orphan liabilities such that this creates a cost for those other employers to make good the deficiency. To give effect to this, the Administering Authority will seek funding from the outgoing employer sufficient to enable it to match the liabilities with low risk investments, generally Government fixed interest and index-linked bonds.

To the extent that the Administering Authority decides not to match these liabilities with Government bonds of appropriate term then any excess or deficient returns will be added to or deducted from the investment return to be attributed to the other employers' notional assets between the exit date of the employer and each subsequent funding valuation of the Fund. Assets will then be reallocated within the Fund to ensure the orphan liabilities remain 100% funded on a low risk basis after taking account of any outstanding exit payments payable to, or due from the exiting employer, with any investment profit or loss allocated to the contributing employers in proportion to their notional asset share.

### **Cessation of participation (i.e. exiting the Fund)**

Where an employer becomes an exiting employer, an exit valuation will be carried out in accordance with Regulation 64. That valuation will take account of any activity as a consequence of exit 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. When employees do not transfer to another employer they will retain pension rights within the Fund, i.e. either as a deferred pensioner or immediately taking retirement benefits.

The assumptions adopted to value the departing employer's liabilities for the exit valuation will depend upon the circumstances. In particular, the exit valuation will distinguish between residual liabilities which will become orphan liabilities, and liabilities which will be subsumed by other employers and will take account of any contractual guarantees where possible and notified to the Administering Authority. For example London Borough of Southwark's admission policy generally includes a guarantee that it will take on all the assets and liabilities with no exit payment falling on the exiting employer. For clarity, no exit credit will be payable to such employers on exit.

For orphan liabilities the Funding Target in the exit valuation will anticipate investment in low risk investments such as Government bonds. This is to protect the other employers in the Fund, as upon exit, the employer's liabilities will become 'orphan' liabilities within the Fund, and there is no recourse to that (former) employer if a shortfall emerges in relation to these liabilities after the exit date.

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

In addition, the Administering Authority may, at its discretion, include additional margins for prudence compared to the approach used for determining ongoing contributions, for

example in relation to regulatory uncertainty (which at the date of this Statement includes uncertainty associated with the McCloud case, cost management process and indexation and equalisation of GMP).

Regardless of whether the residual liabilities are orphan liabilities or subsumed liabilities, the exit valuation will determine final payments required to make good the funding position revealed unless a contractual agreement sets out that another employer will take responsibility for all the assets and liabilities relating to the exiting employer. In other words, the fact that liabilities may become subsumed liabilities does not necessarily remove the possibility of an exit payment being required.

Any deficit or surplus in the Fund in respect of the employer will generally be due to the Fund as a termination contribution, or payable by the Fund to the employer as an exit credit respectively, where the exit date is on or after 14 May 2018.

## **Academies**

Academies are scheduled bodies and, as such, have an automatic right to join the LGPS. Guidance has been issued by the Secretaries of State for Education and Communities and Local Government but in practice differing approaches are being taken when setting the funding strategy for academies.

Where a new academy joins an existing Multi Academy Trust which has been certified a contribution rate in the Fund, the Fund will require that the Multi Academy Trust ensures that contributions are paid in respect of this academies membership of the Fund.

If the relevant Multi Academy Trust has not previously been certified a contribution rate in the Fund an initial rate will be calculated by the Fund Actuary as set out in the section above.

In future for a new academy conversion while the London Borough of Southwark's asset share is in deficit, the Administering Authority's standard approach will be to:

- Allocate liabilities to the academy in relation to its current employees only, with the London Borough of Southwark asset share retaining liability for former employees; and
- Allocate a notional share of assets from the London Borough of Southwark's asset share to the new academy's asset share based on what is known as a 'capped prioritised share of fund' approach. This means that the academy will inherit an appropriate share of any deficit attributable at conversion to the London Borough of Southwark's former employees as well as the academy's own employees. Where the prioritised share of Fund is greater than the value of the transferring membership, calculated using the appropriate Funding Target, the notional asset share to be transferred will be capped at 100% of the value of the transferring membership.

Where an academy transfers from one Multi Academy Trust participating in the Fund to another Multi Academy Trust participating in the Fund the notional reallocation of assets between the relevant Multi Academy Trusts will be calculated using the capped prioritised share of fund" approach set out above, unless the transfer of the academy results in cessation of participation in the Fund of a Multi Academy Trust, in which case additional considerations will apply and the method for determining the notional reallocation of assets will be determined by the Administering Authority in consultation with the Fund Actuary.

## SECTION 6

### IDENTIFICATION OF RISKS AND COUNTER MEASURES

#### Approach

The Administering Authority seeks 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 before, and after they emerge, wherever possible. The main risks to the Fund are considered below:

#### Investment risk

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 would be:

- Assets not delivering the required return (for whatever reason, including manager underperformance);
- Systematic 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 risks, duration risks and market risks;
- Alternative assets – liquidity risks, property risks, alpha risk;
- Money market – credit risk and liquidity risk;
- Currency risk;
- Macroeconomic risks; and
- Environmental; social and corporate governance risks.

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

#### **Choice of Solvency and Funding Targets**

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

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

The Administering Authority's policy will be to monitor an underlying 'low risk' position (making no allowance for returns in excess of those available on Government stocks) to ensure that the Funding Target remains realistic.

### Employer risk

The 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 admitted) and other pension fund stakeholders.

The Administering Authority will maintain a knowledge base on their admitted bodies and their legal status (charities, companies limited by guarantee, group/subsidiary arrangements) and use this information to inform the Funding Strategy Statement.

### Climate change

The systemic risks posed by climate change and the policies implemented to tackle them will fundamentally change economic, political and social systems and the global financial system. They will impact every asset class, sector, industry and market in varying ways and at different times, creating both risks and opportunities for investors. The Administering Authority and Investment Advisory Panel keeps the effect of climate change on future returns under review and will commission modelling or advice from the Fund Actuary on the potential effect on funding as required.

### Liquidity and maturity risk

This is the risk of a reduction in cash flows into the Fund (including investment income – e.g. potentially resulting from changes in investment holdings), or an increase in cash flows out of the Fund, or both, which can be linked to changes in the membership and, in particular, a shift in the balance from contributing members to members drawing their pensions. Changes in the funding position and hence (secondary) employer contributions can also affect the cashflow position since it is not always possible to deliver complete stability of contributions. Timing of contribution payments by employers can also impact on liquidity requirements were flexibility is granted by the Administering Authority. Changes within the public sector and to the LGPS itself may affect the maturity profile of the LGPS and have potential cash flow implications. For example:

- Budget cuts and headcount reductions could reduce the active (contributing) membership and increase the number of pensioners through early retirements;
- An increased emphasis on outsourcing and other alternative models for service delivery may result in falling active membership (e.g. where new admissions are closed);
- Public sector reorganisations may lead to a transfer of responsibility between different public sector bodies, (e.g. to bodies which do not participate in the LGPS);
- Scheme changes, for example, lower member contributions as provisionally agreed as part of the Scheme Advisory Board cost management process will lead to lower member contributions which may not be immediately matched by higher employer contributions; and
- An increase in the take-up of the 50/50 option (whether on affordability grounds or to avoid tax charges) will reduce member contributions to the Fund.

The Administering Authority seeks to maintain regular contact with employers to mitigate against the risk of unexpected or unforeseen changes in maturity or other changes leading to cashflow or liquidity issues. The Administering Authority also commissions the Fund Actuary to provide projections of benefit payments and contributions based at each valuation and monitors the cashflow position on a regular basis.

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), or establishment of a wholly owned company which does not participate in the Fund, or only partially participates, 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 of risk mitigation are set out below:

- **Early retirement and ill-health strain payments** - no allowance is made in actuarial valuations of the Fund for the additional value of the benefits when a member is made redundant, is in ill-health or leaves on the grounds of efficiency. To counter the potential 'strain' (or cost) emerging at the next valuation early retirement strain payments are required from the employer to the Fund to meet this additional cost over a period of no longer than three years.
- **Bodies ceasing to exist with unpaid deficiency** - some employers can cease to exist and become insolvent leaving the employers in the Fund open to the risk of an unpaid deficit. For admission bodies admitted under paragraph 1(d) of Part 3, Schedule 2, any such deficit will be met by the relevant Scheme employer and there is therefore little risk to other employers in the Fund (provided of course that the relevant Scheme employer is itself regarded to be of good covenant).

Other employers are more problematic and the Administering Authority will as far as practicable look to reduce risks by:

- Use of bond arrangements; or
- Ensuring there is a guarantor to back the liabilities of the body; or
- Monitoring other employers with small or declining membership to ensure that funding is close to 100% on the solvency measure by the time the last member leaves service and this may affect the funding strategy accordingly.

#### Statistical/financial risk

This covers such items such as the performances of markets, Fund investment managers, asset reallocation in volatile markets, pay and/or price inflation varying from anticipated levels or the effect of possible increases in employer contribution rate on service delivery and on Fund employers. The Administering Authority policy will regularly assess such aspects to ensure that all assumptions used are still justified.

#### Liability risk

The main risks include discount rates, pay and price inflation, life expectancy, changing retirement pattern and other demographic changes.

The Administering Authority will ensure that the Fund Actuary investigates demographic, pay and pension increase experience at each valuation and reports on developments. The demographic assumptions are intended to be best estimate, informed by Fund experience and wider evidence where needed, e.g. the mortality assumptions are informed by a postcode analysis carried out by the Fund Actuary's specialist longevity team and the projections model released by the Continuous Mortality Investigation of the Institute and Faculty of Actuaries. If the Administering Authority becomes aware of any material changes in population mortality which may also be reflected in the Fund's experience it will ask the Fund Actuary to report on the effect on the funding position and employer contributions.

The Fund Actuary will also provide quarterly funding updates to assist the Administering Authority in its monitoring of the financial liability risks. The Administering Authority will, as far as practical, monitor changes in the age profile of the Fund membership, early retirements and redundancies and, if any changes are considered to be material, ask the Fund Actuary to report on their effect on the funding position and employer contributions.

If significant liability changes become apparent between valuations, the Administering Authority will notify the affected employers of the anticipated impact on costs that will emerge at the next valuation and consider whether any bonds that are in place for admission bodies require review. It will also consider the extent to which such changes can or should be allowed for in exit valuations, taking advice from the Fund Actuary.

#### Regulatory and compliance risk

The risks relate to changes to both general and LGPS specific regulations, national pension requirements or HM Revenue and Customs' rules.

The Administering Authority will keep abreast of all proposed changes. If any change potentially affects the costs of the Fund, the Administering Authority will ask the Fund Actuary to assess the possible impact on costs of the change. Where significant, the Administering Authority will notify employers of the possible impact and the timing of any change.

There are a number of consultations which have been issued in recent years, some of which represent proposed changes which were first raised a number of years ago, including a cap on exit payments by public sector employers, new Fair Deal arrangements and greater flexibility on employer exit from the LGPS. Some of these may affect funding and pose a risk to the Fund. The Government has also consulted on changes to the valuation cycle although the Administering Authority understands that the 2022 valuation is going ahead as previously planned.

There are a number additional uncertainties associated with the benefit structure at the time of the latest formal review of this Statement, including:

- How the Government will address the issues of GMP indexation and equalisation beyond expiry of the current interim solution from 6 April 2021;
- The outcome of the McCloud/Sargeant cases which ruled that the transitional protections implemented in the Firefighters' and Judges' Pension Schemes were illegal age discrimination, and what the remedy might be in the LGPS in terms of its scope and form; and
- The outcome of the cost management process and whether the agreement reached in relation to the Scheme Advisory Board (SAB) process for member contributions to be reduced and benefits enhanced to achieve an additional cost of 0.9% of pay.

Details of the allowance made for these uncertainties in the 2019 valuation are as follows:



## **McCloud/cost cap**

1.5% of pay has been added to employer contributions based on Fund-specific calculations carried out by the Fund Actuary. This figure has been calculated across the Fund as a whole on the scheduled and subsumption body funding target assuming the following remedy:

- Compensation will apply to members who joined the LGPS before 1 April 2014 (see below);
- Benefits will be the better of those accrued in the 2014 Scheme or those accrued in the 2008 Scheme, backdated to 1 April 2014 (i.e. an 'underpin' approach);
- Compensation will apply to members who retire from active service with immediate pension benefits, through normal health or ill-health retirement (this is because transitional protections only applied to members retiring from active service with immediate pension); and
- The remedy will not apply to spouses' or dependants' benefits. This is because transitional protections only applied to members' benefits.

The cost is split 0.4% of pay in respect of past service and 1.1% of pay in respect of future service where the past service cost has been spread over a recovery period of 19 years.

## **GMP indexation/equalisation**

There is no allowance for GMP equalisation beyond the extended 'interim' solution announced in January 2018, i.e. for full inflationary increases on GMP to be paid from the Fund for members reaching State Pension Age by 5 April 2021.

### Smoothing risk

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. Where such an adjustment is used, the Administering Authority will review the impact of this adjustment at each valuation to ensure that it remains within acceptable limits to ensure that it does not alter the disclosed solvency level by more than 5%.

### Recovery period risk

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

### Stepping risk

The Administering Authority recognises that permitting contribution rate changes to be introduced by annual steps rather than immediately introduces a risk that action to restore solvency is insufficient in the early years of the process. The Administering Authority will limit the number of permitted steps as appropriate. Details of the Administering Authority's policy are set out earlier in this Statement.

## APPENDIX 4 – Investment Strategy Statement

### 1. Introduction

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

This ISS has been designed to be a living document and is an important governance tool for the London borough of Southwark Pension Fund (the Fund). This document sets out the investment strategy of the Fund, provides transparency in relation to how the Fund investments are managed, outlines the Fund's approach to managing risk, how environmental, social and governance issues are taken into account and the approach with regard to pooling of investments. This document replaces the Fund's Statement of Investment Principles (SIP).

This Statement will be reviewed by the Pensions Advisory Panel (PAP) annually, or more frequently should any significant change occur, with any resulting recommendations made to the Strategic Director of Finance and Governance.

Southwark Council is the Administering Authority for the Fund and bears ultimate responsibility for the funding of member pensions. The management and strategic direction of the Fund, whilst separate from the Council, will always take into consideration the Council's long-term objectives.

In this regard the Fund's investment principles are aligned with the Council's fairer future principles as defined in the Council Plan, in particular, the fairer future value of 'spending money as if it were from our own pocket' and the 'fit for the future' principles to ensure financial sustainability.

The Fund is fully committed to collaboration with other local authority partners and in 2015 invested, and is an active shareholder, in the London Collective Investment Vehicle (LCIV). The LCIV is a collaborative venture between local authorities to deliver benefits of investment scale and efficiency to the participating Funds. The Fund will continue to support the development of the LCIV as an investment vehicle.

## 2. Investment objectives and principles

The Fund is an open, defined benefit pension fund as part of the national LGPS. The Scheme rules are determined at national level and cover many elements of the Fund, such as employee benefits and employee contributions. The nature of the Fund and scheme design means that payment of pensions will extend over the very long term.

In setting the investment strategy the Fund seeks to balance twin objectives: first, to achieve sufficient long-term returns for the Fund to be affordable and second, to keep the employers' contribution rate as stable as possible.

The Fund will seek to operate a long-term, sustainable strategy; one which does not rely upon the pursuit of short-term returns or adherence to asset management trends, but utilises a well-structured asset and Fund manager investment allocation to target long-term socially responsible investment performance. The Fund's uncomplicated investment structure provides significant flexibility and adaptability if required.

To achieve the twin objectives, the Fund needs to invest in a diverse range of assets which provide higher returns relative to the growth of pension liabilities whilst taking account of the volatility inherent in investment markets. The principles set out below provide high level guidance on how the Fund seeks to meet these objectives and manage the associated risks.

### Governance

- The Fund seeks at all times to adopt best practice governance standards within a structured framework, compliant with regulatory requirements and with expert independent advice taken throughout the decision making process;
- The Fund will operate with transparency and be accountable for decision making to stakeholders and scrutiny bodies; and
- The Fund will ensure that officers and members of the PAP and Local Pension Board have the necessary skills, expertise and resources to ensure effective and evidence based decision making regarding the Fund's investment strategy.

### Investment structure and risk management

- The Fund is a long-term investor and as such the Fund invests in a wide range of investment assets, which may be volatile or illiquid, such as equity or property, but that over the long term can generate a sufficient return to meet the Fund's pension obligations;
- The Fund operates an evidenced and research based approach to investment; continually utilising research and guidance from investment professionals and peers, and seeking continual development in the understanding of investment;
- The Fund recognises the importance of having the right asset allocation, but also the value of developing the right structure and appointing suitable investment managers. The Fund will take account of markets and the economic background in decision making, but will avoid making decisions on a purely short-term basis;

- The Fund will be comprehensive in the consideration of risks; the Fund will base assessments of risk on future pension liabilities and contributions, will consider financial and non-financial risks, diversify investment assets in an appropriate manner, but also recognise the limits of that diversification. As a long-term investor the Fund understands that investment success depends significantly on the sustainable growth of the economy;
- The Fund will seek the most efficient and cost-effective solutions to achieving the Fund's objectives. This may involve active management and other services where additional costs are justified. Fees will always be considered in the context of overall performance and it is recognised that higher performance may be associated with higher fees; and
- The Fund is an active shareholder in the LCIV, with the Fund making regular contributions to the LCIV to assist in the development and expansion of the collaborative venture. Any future investments within the LCIV will be dependent upon the satisfactory completion of detailed due diligence and review to the same high standard that would be undertaken outside the investment pool.

### **Responsible investment and stewardship**

- The Fund is a responsible investor; holding the belief that well governed companies that manage their business in a responsible and sustainable manner will generate better returns over the long term;
- The Fund is prepared to be innovative and demonstrate thought leadership in investment, within a framework of prudence and fiduciary duty;
- The Fund will actively exercise responsible stewardship of the assets held and act as a responsible voice in the broader investment community; and
- The Fund will collaborate with others whenever possible to share ideas and best practice, and to improve effectiveness and to reduce costs.

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

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

Asset class	Target allocation %	Investment style %	Maximum allocation %	Role (s) within the strategy
<b>Equity</b>	50.0	Passive 40.0	65.0	Expected long-term growth in capital and income in excess of inflation over the long term.
		Active 10.0		
<b>Diversified Growth</b>	10.0	Active 10.0	20.0	Primarily for diversification from equities. Equity like returns over time with a lower level of risk.
<b>Absolute Return Fixed Income</b>	5.0	Active 5.0	10.0	Diversified approach to fixed income investing which is not dependent on the direction of interest rates.
<b>Index Linked Gilts</b>	10.0	Passive 10.0	40.0	Low risk (relative to the liabilities) asset that provides inflation linked income and protection from falling interest rates.
<b>Property</b>	20.0	Direct 14.0	30.0	Provides diversification from equities and fixed income. Generates investment income and provides some inflation protection.
		Pooled Fund 6.0		
<b>Sustainable Infrastructure</b>	5.0	Limited Partnership 5.0	10.0	Asset class provides additional diversification from traditional asset classes. Generates sustainable, reliable income with significant linkage to inflation. Provides risk mitigation from declining fossil fuel usage.

The above table sets out the Fund's asset allocation strategy with a target allocation to each asset class. If the actual asset allocation as at a reporting quarter end moves outside a target range for a particular asset class, (plus or minus 5% of total investment assets) the Strategic Director of Finance and Governance will review the portfolio and prevailing market conditions to determine if a corrective rebalancing action is required. A breach of the target range will not necessitate a portfolio rebalance.

Under Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, the Fund is required to set maximum investment limits pertaining to different asset classes so that actual allocation to those asset classes will not breach this maximum limit. The limits as applied to the Fund are set out in the above table.

Appendix A shows the Fund's current investment manager appointments and mandates.

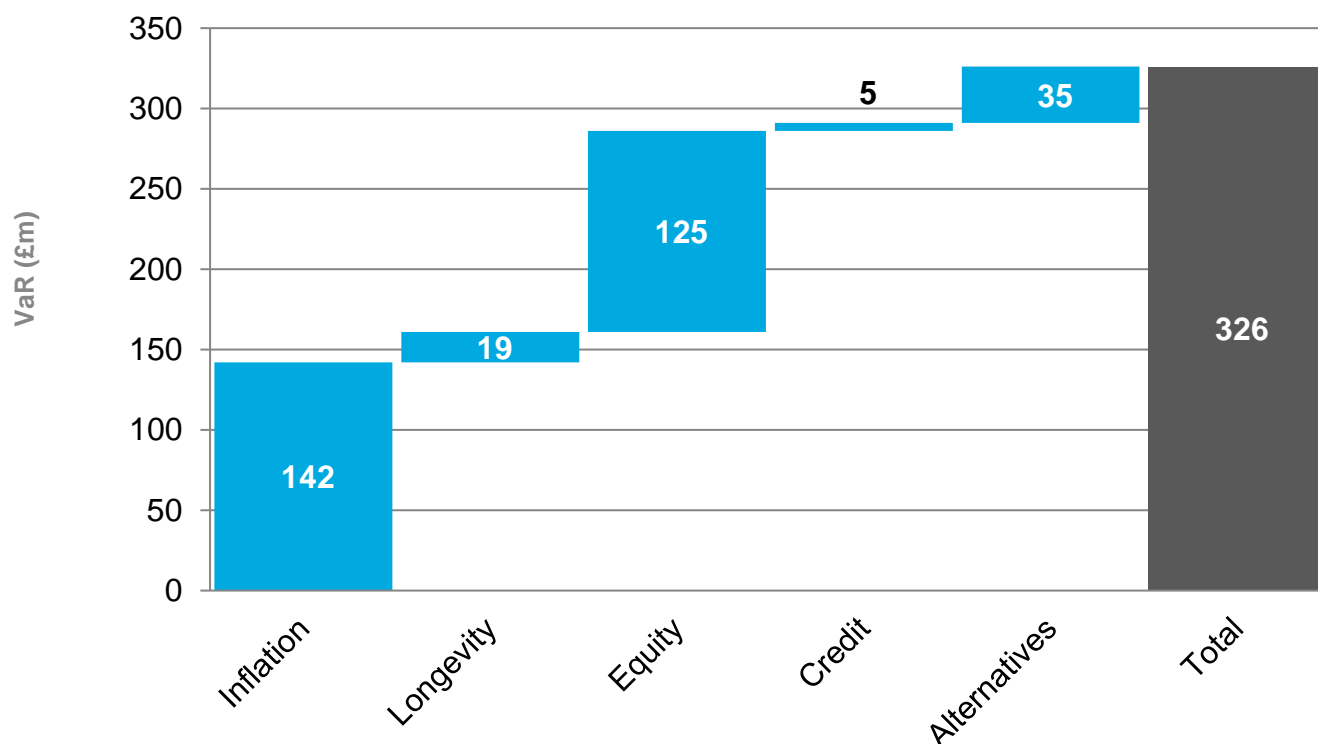
The Fund's asset allocation is reviewed on an ongoing basis and undergoes a triennial strategy review as part of the actuarial valuation process. The triennial review looks at both qualitative and quantitative analysis, covering:

- 
- The required level of return that will mean the Fund is able to meet its future benefit obligations as they fall due;
  - The level of risk that the Fund can tolerate in absolute terms, and in relation to its funding level and deficit;
  - An analysis of the order of magnitude of the various risks facing the Fund, so that the Fund can focus upon the most significant risks and
  - The desire for diversification across asset class, region, sector, and type of security.

## 4. Risk measurement and management

The risks inherent within the portfolio are assessed both qualitatively and quantitatively as part of regular investment strategy reviews by the Strategy Director of Finance and Governance and the PAP. The Fund uses specialist external investment advisers under contract, to support these reviews and on an ongoing basis. The Fund highly values the use of specialist support in the management of performance and risk.

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



As an additional illustration of risk, the table below, based on the 31 March 2016 Actuarial Valuation results and estimates, shows how a range of events could impact on the Fund:

Event	Event movement	Impact on the Fund
Fall in equity markets	25% fall in equities	£175m
Rise in inflation	1% increase in inflation	£286m
Fall in interest rates	1% fall in interest rates	£286m
Underperformance by the active managers	3% collective underperformance	£20m

The Fund's overall investment strategy is designed to mitigate much of the underlying risk through the holding of a variety of different, diverse asset classes (e.g. long-term directly held property investments).

## Equity risk

The largest asset risk to the Fund is in relation to its equity holdings. Should equity markets deteriorate significantly this will have a large negative impact on the Fund's assets. The Fund invests in equities in order to provide the necessary long-term expected returns to help ensure that the Fund remains affordable. The Fund believes that the extra returns that are expected to be generated by equities compensate for the level of risk equities bring to the Fund. However, the Fund is aware of the need for diversification in growth assets, and the Fund's strategy reflects this via allocations to absolute return investment mandates and property.

## Inflation

Consumer Price Index (CPI) inflation will increase the value of pension benefits accrued by active and deferred members of the Fund as well as increasing the value of pensions in payment. The Fund has an allocation to index-linked gilts for explicit inflation protection and other investment assets, such as property and equities, in the expectation that these will achieve returns in excess of inflation over time.

## Active manager risk

Active investment managers are appointed to manage a portion of the Fund's assets. This brings with it the risk of underperformance relative to the market but also brings the chance of additional returns and diversification. The additional risk is small relative to other risks. Extensive due diligence is undertaken before managers are selected and investment managers are also monitored regularly by Fund officers, the PAP, and by the Fund's investment advisers.

## Liquidity risk

The Fund recognises that there is liquidity risk in holding assets that are not readily marketable and realisable. Given the long-term investment horizon and the potential for an illiquidity premium in investment returns, the degree of liquidity risk within the portfolio is considered as acceptable. The Fund has a large allocation to property but the majority of the Fund's assets are realisable at short notice.

The table below sets out a summarised cash flow position of the Fund over the last five financial years.

	2012-13 £000	2013-14 £000	2014-15 £000	2015-16 £000	2016-17 £000	2017-18 £000
Contributions and transfers in	49,364	51,288	54,569	61,181	55,789	54,711
Benefits and transfers out	(50,956)	(51,949)	(51,801)	(61,755)	(60,269)	(59,400)
Investment income	14,104	12,345	12,903	12,717	14,324	14,743
<b>Net position</b>	<b>12,512</b>	<b>11,684</b>	<b>15,671</b>	<b>12,143</b>	<b>9,844</b>	<b>10,054</b>



## Exchange rate risk

This risk arises from investing in unhedged overseas (non-GBP denominated) assets, with all pension benefits due to be paid in sterling. As a long-term investor, the Fund takes the view that currency volatility can be tolerated. The Fund's portfolio is well diversified across asset classes, geography and investment managers.

## Demographic risks

The Fund is subject to a range of demographic risks, but with particular importance to the investment strategy is the possibility of a maturing Fund membership profile. This would involve a change in the ratio between active members contributing into the Fund and pensioner members drawing pension benefits from the Fund. The more mature a pension fund, the more likely it is that disinvestments would need to be made to pay benefits. The Fund is not in that situation at present as income from contributions and investments is greater than benefit payments. However, this situation is monitored regularly and formally as part of the actuarial valuation and strategy review.

## Environmental, social and governance risks

The Fund believes that environmental, social and governance (ESG) factors should be taken into account on an ongoing basis and are an integral part of the Fund's objective to be a long-term sustainable investor.

The Fund has committed to a long-term process of cutting fossil fuel investments. More information on this policy is set out in section 6.

Fund engagement is crucial in relation to improving standards of corporate governance, which over the long term is expected to enhance investment returns. Details of the Fund's approach are set out in sections 6 and 7 as well as the Fund's initial approach for the implementation of a reduction in fossil fuel exposure as Appendix C.

## 5. Approach to asset pooling

The Fund is a shareholder of the London Collective Investment Vehicle (LCIV). The LCIV was created in 2015 and is in the process of opening a range of sub-funds for potential investment. As part of any future changes to investment strategy, the Fund will look first to the availability of appropriate investment products within the LCIV.

The transition of any assets into the pool will follow the normal due diligence process with consideration of: transition costs, fees (direct and indirect), reporting arrangements, socially responsible investment requirements and, most importantly, expectations for future performance.

The Fund currently benefits from lower fees for passive investments arising from collective fee arrangements with the CIV, although these are not assets under management of the LCIV (value as at 30 September 2017 £848 million, approximately 56% of the Fund).

The Fund has a target allocation of 20% of the Fund to illiquid property assets and the cost of exiting these strategies early would have a significant negative financial impact on the Fund.

## 6. Environmental, social and corporate governance policy

The Fund is a long-term investor that aims to deliver a truly sustainable pension fund; ensuring that it is affordable, delivers financially to meet the objectives of the Fund employers, and is invested responsibly.

The fiduciary duty of the Fund is to act in the best long-term interests of Fund members. To do so properly requires the Fund to recognise that environmental, social and governance issues can impact on the Fund's financial performance and that they should be taken into account in funding and investment strategies, and throughout the funding and investment decision making process.

The Fund recognises the growing financial risks associated with investment in traditional energy sources and is fully committed to the continued reduction in exposure to fossil fuel. The Fund commits to transferring over time any current investments in these traditional energy sources in a way that is both structured and affordable and also meets the Fund's fiduciary duties.

Appendix C outlines the initial approach by which the Fund will achieve this divestment, how the risks and other considerations associated with such a commitment will be managed and how the divestment over time will be incorporated into the asset allocation strategy for the Fund.

The Fund will seek to incorporate ESG considerations at all stages in the investment process; from the overall asset allocation, to individual investment selections, and continued engagement and responsible stewardship of Fund assets.

The Fund will continue to explore new opportunities in sustainable energy and infrastructure. Where possible, these opportunities should be pursued through arrangements entered into with the LCIV, although it is recognised at this time that there is no such plan for these facilities to be accessible through this route.

The responsible investment objectives of the Fund are promoted through membership of the Local Authority Pension Fund Forum (LAPFF). As a LAPFF member the Fund allies itself with 71 other shareholders with combined assets of over £175 billion to influence key areas of responsible investment interest.

The Fund's key responsible investment principles are set out below:

- Apply long-term thinking to deliver long term sustainable returns;
- Seek sustainable returns from well governed and sustainable assets;
- Apply a robust approach to effective stewardship;
- Engagement through voting, meetings, and the LAPFF is a valuable tool to influence organisations in areas of responsible investment interest;
- Ensure that responsible investment is a core competency and skill to support decision making;
- Seek to innovate, demonstrate and promote responsible investment leadership and ESG best practice;
- Apply evidence based decision making in the implementation of responsible investment;
- Achieve improvements in ESG through effective partnerships with the London CIV and LAPFF;
- Share ideas and best practice to achieve wider and more valuable responsible investment outcomes;
- Be transparent and accountable in all Fund activities;
- Consider the costs of responsible investment decisions alongside fiduciary responsibilities; and
- To continue with a structured, measured process of reducing and ultimately eliminating investments in fossil fuels.

## **7. Policy of the exercise of rights (including voting rights) attaching to investments**

The Fund follows the principles of the UK Stewardship Code and exercises the voting rights attached to its investments wherever it is possible and cost effective to do so. The Fund intends to formally sign up to the UK Stewardship Code.

The aim is to promote and support good corporate governance principles and best practice. Voting rights should be exercised in accordance with the best financial interests of both the beneficiaries and contributors to the Fund. Environmental, social and ethical considerations may be taken into account when exercising votes where this acts in these parties' best interests.

Fund managers have been instructed to vote in accordance with their house policies and practices, whilst also taking into account the Combined Code on Corporate Governance. Where practical, managers should vote in line with the council's priority themes.

Fund managers report in advance of all voting rights they intend to exercise on behalf of the Fund. They provide details of their house view and on how they intend to vote. They ensure that this is consistent with the council's key themes and also with the LAPFF principles.

Fund managers' views are compared with the voting recommendations of LAPFF. Where the fund managers' house views are not consistent with those of LAPFF, the fund manager is instructed by the Fund to vote in line with the recommendations of the LAPFF.

Fund managers provide a quarterly report on corporate governance activity. This lists all votes which have been exercised and all engagement with companies which has taken place. It allows for checks to be carried out in order to ensure all the Fund's voting rights have been exercised in accordance with policy. Summary reports outlining voting and engagement activity are provided at quarterly Pensions Advisory Panel meetings.

### **Myners Principles**

The Government introduced a code in October 2001 based on the results of HM Treasury's review of institutional investment in the UK, carried out by Paul Myners. This code set out ten principles that were intended to improve the investment management of pension funds. These were updated in October 2008 and previously LGPS administering authorities were required to prepare, publish and maintain statements of compliance against a set of six principles within the Statement of Investment Principles. Although not specifically required by the Regulations the Fund sees the Myners Principles as a relevant governance tool and will continue to report on compliance.

The Fund is fully compliant with the six principles and Appendix B sets out the compliance statement.

**Advice taken**

In creating this statement, the Fund has taken advice from its investment consultant. Also, in relation to each of the constituent parts, such as the asset allocation and risk mitigation, advice has been taken from its investment consultant, Mercer, and the Fund Actuary, Aon Hewitt.

## Appendix A – Current investment managers and mandates

Manager	Mandate	Benchmark	Benchmark weight (%)	Outperformance target (% per year)
BlackRock	Balanced	In line with customised benchmarks using monthly mean fund weights	25.0	-
BlackRock	Dynamic Diversified Fund	LIBOR	10.0	+3.0% net of fees
BlackRock	Absolute Return Bonds	LIBOR	10.0	+4.0% net of fees
L&G	Passive Global Equities and Bonds	FTSE All World	25.0	-
Newton	Global Equity	FTSE All World	10.0	+3.0% net of fees
Nuveen Real Estate	Core Property	7.0% per year. absolute return	14.0	
Frogmore	Opportunistic Property	16.5% per year absolute return	1.5	-
Brockton	Opportunistic Property	15.0% per year absolute return	1.5	-
Invesco	PRS Property	8.5% per year absolute return	1.5	-
M&G	PRS Property	8.0% per year absolute return	1.5	-

## Appendix B

### Myners Principles – Assessment of Compliance

#### 1. Effective Decision-Making

##### Principle

Administering authorities should ensure that:

- Decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to make them effectively and monitor their implementation; and
- Those persons or organisations have sufficient expertise to be able to evaluate and challenge the advice they receive and manage conflicts of interest.

##### State of Compliance

The Fund is currently **fully compliant** with this principle:

- The Pensions Advisory Panel (PAP) is supported by suitably qualified officers and external advisers. All members of the PAP are offered training on appropriate topics.

#### 2. Clear Objectives

##### Principle

An overall investment objective(s) should be set out for the Fund that takes 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 advisors and investment managers.

##### State of Compliance

The Fund is currently **fully compliant** with this principle:

- The Fund's objectives are set out in the Investment Strategy Statement and the Funding Strategy Statement. The objective, benchmark and risk parameters are clearly stated in the Investment Management Agreements with each investment manager; and
- Covenants of all Scheme employers are reviewed on an ongoing basis.

### 3. Risk and Liabilities

#### Principle

- In setting and reviewing their investment strategy, Administering Authorities should take account of the form and structure of liabilities; and
- These include the implications for local tax payers, the strength of the covenant for participating employers, the risk of their default and longevity risk.

#### State of Compliance

The Fund is currently **fully compliant** with this principle:

- The asset allocation strategy is reviewed every three years. Mercer Ltd is commissioned to carry out an asset liability study which models the risk/reward characteristics of different investment strategies; and
- The study follows the triennial actuarial valuation and the form and structure of liabilities are fully taken into account.

### 4. Performance Assessment

#### Principle

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

#### State of Compliance

The Fund is currently **fully compliant** with this principle:

- The PAP monitors the performance of the investment managers and the suitability of the investment strategy on a regular basis; and
- Performance measurement is provided by JP Morgan and Mercer Ltd.
- Assessment of the effectiveness of the Administering Authority is reflected through the effectiveness of the decision making in the investment returns achieved. Further, with the establishment of the Local Pensions Board, scrutiny of the PAP is now being undertaken.

- A procurement exercise was carried out in 2014 which resulted in the appointment of Mercer Ltd as the Fund's investment advisers. They were appointed through the National LGPS Frameworks and as such are subject to ongoing review at the framework level. Feedback is provided to the framework on an annual basis.

## 5. Responsible Ownership

### Principle

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; and
- Report periodically to Scheme members on the discharge of such responsibilities.

### State of Compliance

The Fund is currently **fully compliant** with this principle:

- The Fund has adopted the investment managers' policies on activism and each has adopted the Institutional Shareholders' Committee Statement of Principles. All investment managers adopt a policy of engagement with companies;
- The Fund's policy on responsible ownership is set out in its Investment Strategy Statement;
- Investment managers report on the exercise of voting rights and this is monitored by officers and the PAP to ensure consistency with the Fund's policy;
- The Fund is a member of the LAPFF, the UK's leading collaborative shareholder engagement group;
- Responsible ownership is periodically reported to the PAP and states how active fund managers are discharging these responsibilities; and
- A section on responsible ownership is included in the Pension Fund Annual Report and a member survey has been completed. These ensure that members are both provided with the relevant information and are able to input their views into the responsible ownership process going forward.



## 6. Transparency and Reporting

### Principle

Administering Authorities should:

- Act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives; and
- Provide regular communication to scheme members in the form they consider most appropriate.

### State of Compliance

The Fund is currently **fully compliant** with this principle:

- Documents relating to the Fund are published on the Council's website;
- The Annual Report sets out the arrangements during the year for the management of investment, governance and risks and other relevant information;
- Members can also request information directly from the Council; and
- The PAP minutes are published on the Council's website.

## APPENDIX 5 – Communications strategy

### Introduction and regulatory framework

This is the communications strategy for the Local Government Pension Fund administered by Southwark Council.

As at 31 March 2020 the Fund had 25,707 scheme members (10,932 deferred, 6,888 active and 7,887 pensioner members) There were 20 admitted and 30 scheduled bodies.

This document provides an overview of how Southwark Council communicates to these and other interested parties.

A written statement of the strategy is a requirement of the provisions of Regulation 61 of the Local Government Pension Scheme Regulations 2013 which require Southwark Council to prepare and maintain a written statement setting out the policy of communicating with members, representatives of members, prospective members and Scheme employers.

The statement must also set out the Fund's policy on the provision of information and publicity to Scheme members and their representatives, and Scheme employers of member, on the format, frequency and method of distributing that information, and on the promotion of the Scheme to prospective members and their employers.

### Responsibilities and resources

Within the pension administration section, the Pensions Manager has responsibility for preparing communication material and organising communication events with the support of key personnel in the team.

Communication material is produced within the section, supported by Aon Hewitt, the Fund's actuaries, as required.

The communications strategy is approved by the Strategic Director of Finance and Governance, on the advice of the Pensions Advisory Panel (PAP) and following review by the Local Pensions Board.

### Communication with key stakeholders

The key stakeholders that we communicate with and who form part of this communications strategy are:

- Active members;
- Deferred members;
- Pensioner members;
- Prospective members;
- Scheme employers (admitted and scheduled bodies plus schools);
- Senior Managers;
- Union Representatives; and

- Elected members, PAP and Local Pension Board

We seek to utilise an electronic form of communication wherever possible. However, there will always be examples where that is not appropriate, including such factors as member demographic, the need for face-to-face communication and training, and regulatory factors. We will also aim to meet any requests to improve the accessibility of information such as larger font or information in another language.

As Southwark Council administers the Fund, all communication conforms to the Council's branding.

### Active, deferred and pensioner members

We aim to ensure that as far as reasonable, members understand their benefits and rights under the Fund. We also aim to ensure that members receive timely and accurate information.

Key approaches are outlined in the table below.

Information type	Method of Communication	Frequency of Issue	Distribution	Stakeholder
<b>Scheme booklet</b>	Electronic and paper based on intranet	At joining and at major scheme changes	Emailed or posted to employees by employer	Active members
<b>Retirement presentations</b>	Face-to-face	Regularly as required	Advertised on intranet and invitations via HR team	Active members
<b>Pension roadshows and drop in sessions</b>	Face-to-face	On request and at major scheme changes	Advertised on intranet	Active members
<b>Pension Fund Annual Report</b>	Southwark Council website	Annual	On request	All members
<b>Benefit Statements</b>	Via email to active members. Via post to deferred members	Annual	Employee email address for active members, home addresses for deferred	Active and Deferred members
<b>Website information and links, including Member Self-Service (MSS)</b>	Electronic	Continuously available	Advertised on communication	All members
<b>Newsletters</b>	Electronic, via email or by post, as appropriate	Periodically – at least annually	Electronic, via email or by post, as appropriate	All members

## Prospective members and their employers

The objective is to increase take up of the pension and also to use as a means of attracting potential new employees. We support Southwark Council's Human Resources team and Scheme employers to meet these objectives, as we do not have direct access to prospective members.

We support these objectives by making available the LGPS leaflet which is distributed to potential or new employees via the employers.

## Scheme employers plus Southwark Schools

The objective is to ensure that they understand their responsibilities and benefits under the LGPS scheme, particularly the importance of timely and accurate information.

Key approaches are outlined in the table below:

<b>Information Type</b>	<b>Method of Communication</b>	<b>Frequency of Issue</b>	<b>Distribution</b>
<b>Administration strategy</b>	Southwark Council website and electronic	Continuously available and reissued if major change	Initially via email and advertised on other communications
<b>Employer guide</b>	Southwark Council website and electronic		Initially via email and advertised on other communication
<b>System guide</b>	Southwark Council website and electronic		Initially via email and advertised on other communications
<b>Training sessions</b>	Face-to-face	As required	Email to employer contacts with personal invitations
<b>Newsletters/ updates</b>	Email	As required	Email to employers' named contact officers

## Senior Managers

The objective is to ensure that Senior Managers are aware of the benefits of the pension scheme, to enable them to support their staff and, in addition, to help them understand the cost and funding implications so that they can make informed employer decisions.

Over and above the various member communication approaches already outlined above, the team also runs regular senior manager briefings.

## **Union Representatives**

The objective is to provide union member representatives with pension scheme information to support their members. It is also to ensure that they are aware of the Fund policy.

The union representatives are involved in the pension briefing sessions, and ad-hoc face-to-face meetings are held as required.

## **Elected members, PAP and Local Pension Board**

The objective is to ensure that these stakeholders are aware of their responsibilities in relation to the Scheme, to seek their view on discretionary policies and responses to Government consultations.

These objectives are achieved via a training programme for new and existing Panel and Board members. In addition regular briefing papers will be presented to the Panel and the Board on key areas related to the Fund.

## **Performance Measurement and Review**

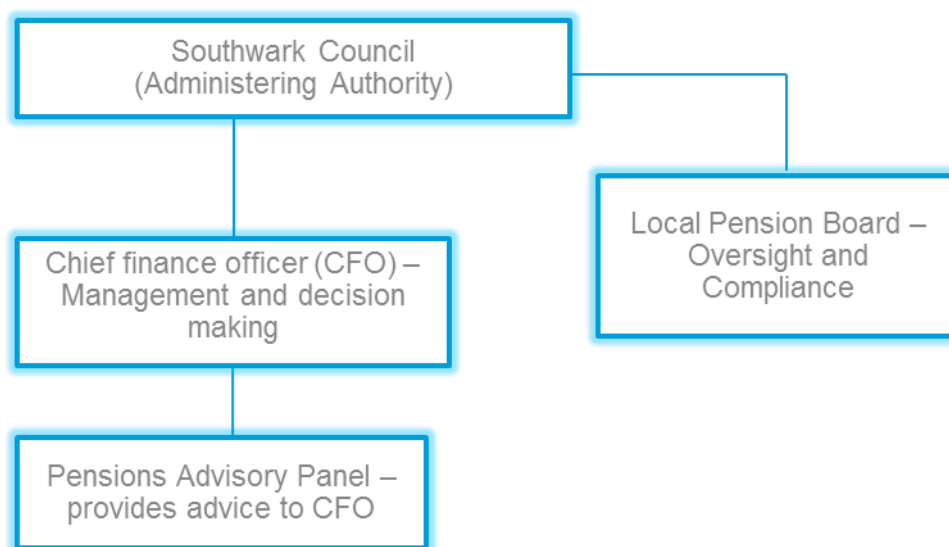
We measure our performance in how effectively we communicate with each of the stakeholder groups. We use a combination of qualitative feedback and measurable targets in order to assess both the effectiveness of the communications strategy and also to measure our performance in meeting the requirements of the strategy.

The strategy is reviewed annually to ensure that it meets stakeholders' needs and regulatory requirements.

As part of that review, we consider any qualitative feedback from stakeholders to identify if revisions are required to either the strategy itself or communication approaches or material.

## APPENDIX 6 – Governance compliance statement

### Background



Regulation 55 of the Local Government Pension Scheme Regulations 2013 requires that an Administering Authority must prepare, maintain and publish a written statement setting out:

- Whether the Administering Authority delegates the function in relation to maintaining a pension fund to a committee, a sub-committee or an officer;
- The frequency of any committee or sub-committee meetings;
- The terms of reference, structure and operational procedures of the delegation; and
- Whether the committee or sub-committee includes representatives of employing authorities or members.

The London Borough of Southwark Pension Fund covers each of these in the following ways:

#### Arrangements for maintaining a pension fund committee

Since 2004 this function has been delegated to the Pensions Advisory Panel (PAP), whose primary objective is to assist the Strategic Director of Finance and Governance in the management of the pensions function within the Council.

## Frequency of meetings

The PAP meets once every quarter. Additional meetings are held where issues requiring urgent attention arise.

## Terms of reference, structure and operational procedures

The primary objective of the PAP is to provide advice to the Strategic Director of Finance and Governance in the management of the Fund. This will include the provision of advice on the following:

## INVESTMENTS

1. Establishing and reviewing the strategic investment objectives;
2. Reviewing the definition of the investment return target most likely to satisfy this investment objective;
3. Considering what constraints, if any, should apply to the invested assets and monitor compliance;
4. Establishing and reviewing the strategic asset allocation (benchmark) that is likely to meet the investment return target;
5. Considering and reviewing the appropriateness of the Fund structure i.e. the delegation of powers to managers, setting boundaries for the managers' discretion and considering which manager return targets are likely to achieve the investment return target;
6. Monitoring the performance of the investment managers at least once every three months, and from time to time consider the desirability of continuing or terminating the appointment of investment managers. In monitoring performance of investment managers, the PAP should consider:
  - i. The investments made by the managers;
  - ii. Their input to the process and the value of their advice;
  - iii. Investment returns and risk against established targets;
  - iv. Manager compliance with the Fund's requirements; and
  - v. Discussion of results with managers.
7. Monitoring risks;
8. Developing a responsible investment strategy;

## FUNDING

9. Carrying out duties set out in the Regulations, in relation to actuarial valuations of the Fund;
10. Ensuring employer contributions are set accordingly and other relevant regulations are adhered to;
11. Considering applications, from external bodies, for membership of the Council's pension scheme;

## GOVERNANCE

12. Monitoring of governance arrangements including regulatory compliance and implementation of audit recommendations;
13. Monitoring costs incurred in administering the Fund, including:
  - i. Management and other direct costs; and
  - ii. Transaction (dealing) costs.

## BENEFITS ADMINISTRATION

14. Considering policy matters in relation to the Fund and the Council's early retirement policy;
15. Monitoring early retirements; and
16. Considering the effectiveness of the administering authorities' management of pension administration.

## Constitution of the Pensions Advisory Panel (PAP)

The PAP will be constituted as follows:

- i. Three members (two members from the majority group and one member of the majority opposition) who have received the appropriate training; one of those members will chair the Panel (voting);
  - ii. Three officers (the Chief Finance Officer (CFO) (non-voting), an officer with specialist knowledge on finance and investments (voting) and an officer with specialist knowledge of pension administration (voting);
  - iii. Two independent advisers (non-voting); and
  - iv. A representative appointed by the constituent trade unions representing beneficiaries (non-voting).
- Decisions should aim to be reached by consensus. Where agreement cannot be reached, then a majority vote will apply. Voting rights are restricted to members and officers (excluding the CFO), with the Chair having the casting vote if required.
  - Decisions of the Panel will be treated as advice to the CFO.
  - To be quorate, at least three voting members of the Panel must be present, plus at least one independent adviser. At least one of the voting members must be an officer.



## Local Pension Board

1. The Panel will work closely with the Local Pension Board (the Board) to ensure the Fund is administered efficiently and effectively and will share with the Board reports and documents to enable the Board to meet its remit; and
2. The Panel will consider any reports the Board may produce in the course of their duties and respond accordingly within a reasonable period of time.

## Conflicts of interest

1. All members of the PAP must declare to the Administering Authority on appointment and at any such time as their circumstances change, any potential conflict of interest arising as a result of their position on the Panel;
2. A conflict of interest is defined as a financial or other interest which is likely to prejudice a person's exercise of functions as a member of the Panel. It does not include a financial or other interest arising merely by virtue of that person being a member of the Fund; and
3. On appointment to the Panel and following any subsequent declaration of potential conflict by a Panel member, the Administering Authority shall ensure that any potential conflict is effectively managed in line with both the internal procedures of the Panel's conflicts policy and the requirements of the Code.

## Representation from employing authorities or members

When deciding on the composition of the PAP, it was decided that as London Borough of Southwark represents the majority of the Fund membership, admitted bodies would not be included on the Panel. There are 23 admitted bodies in the Fund. Although they are not represented on the Panel, they are fully consulted on and kept informed of all decisions made by the Panel.

## The Local Pension Board

The Public Service Pensions Act (2013) required all Administering Authorities to establish a Local Pension Board (the Board) by 1 April 2015.

The Board has the responsibility to assist the Administering Authority to ensure the effective and efficient governance and administration of the Local Government Pension Scheme (LGPS) including:

- (i) Securing compliance with the LGPS regulations and other legislation relating to the governance and administration of the LGPS and any statutory pension scheme that is connected with it;
- (ii) Securing compliance with requirements imposed in relation to the LGPS and any connected scheme by The Pensions Regulator; and
- (iii) Such other matters as the LGPS regulations may specify.

The Administering Authority retains ultimate responsibility for the administration and governance of the Southwark Council LGPS. The role of the Board is to assist the Administering Authority to fulfil that responsibility.

The Board meets quarterly and the membership and work of the Board can be viewed on page 6 in the Annual Report of the Board.

## The principles

Principle	Fully compliant?	Note
<b>Structure</b>		
The management of the administration of benefits and strategic management of the Fund assets clearly rests with the main committee established by the appointed Council.	<b>Yes</b>	
The 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.	<b>See note</b>	<b>1</b>
That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	<b>Not applicable</b>	
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.	<b>Not applicable</b>	
<b>Representation</b>		
That all key stakeholders are afforded the opportunity to be represented, within the main or secondary committee structure. These include: <ul style="list-style-type: none"> <li>Employing authorities (including non-scheme employers, e.g., admitted bodies);</li> <li>Scheme members (including deferred and pensioner scheme members);</li> <li>Where appropriate, independent professional observers; and</li> <li>Expert advisers (on an ad-hoc basis).</li> </ul>	<b>See note</b>	<b>1</b>
That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.	<b>Yes</b>	
<b>Selection and role of lay members</b>		
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.	<b>Yes</b>	
That at the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.	<b>Yes</b>	
<b>Voting</b>		
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.	<b>Yes</b>	
<b>Training/facility time/expenses</b>		
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	<b>See note</b>	<b>2</b>

Principle	Fully compliant?	Note
reimbursement of expenses in respect of members involved in the decision making process.		
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.	Yes	
That the Administering Authority considers the adoption of annual training plans for committee members and maintains a log of all such training undertaken.	Yes	
<b>Meetings (frequency/quorum)</b>		
That an Administering Authority's main committee or committees meet 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.	Not applicable	
That an Administering Authority that does 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.	Not applicable	
<b>Scope</b>		
That Administering Authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Yes	
<b>Publicity</b>		
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.	Yes	

### Note 1

When deciding the composition of the Pensions Advisory Panel, it was decided that as the London Borough Southwark represents over 90% of the Fund membership, admitted bodies would not be included in the Panel. Although they are not represented on the Panel, they are fully consulted on and kept informed of all decisions made by the Panel.

### Note 2

A policy on training exists. It is part of the terms of reference of the Panel that members will have had training and be trained on all matters requiring a decision prior to meetings where these issues are on the agenda. Annual training plans are being considered for the future.

## APPENDIX 7 – Post pool reporting

### Introduction

The Fund is a member of the London Collective Investment Vehicle (LCIV). It does not hold any assets within the LCIV pool directly, however the Fund has passive investments held with Legal & General Investment Management and BlackRock are held in an oversight arrangement and recognised as pooled assets. The Fund is therefore able to benefit from pooled fee savings.

### Pool set up costs

The following table sets out the cumulative set up costs to date incurred by the Fund in its membership of LCIV.

Asset pool	Cumulative
	Direct
Shares subscription costs	150,000
Development fund costs	140,000
	290,000

The cost of purchasing shares in LCIV is included in the set up costs. This cost is treated as an investment in the Fund accounts. However for the purposes of determining the total pool set up costs incurred by the Fund, this has been included above. Development fund costs are invoiced annually and are not broken down into detailed cost categories.

The following table compares the set up costs and annual service charge to actual fee savings achieved. The Fund has achieved net savings of £1.75 million to date.

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Set up costs	150,000	25,000	25,000	25,000	65,000	290,000
Annual service charge	25,000		75,000	65,000	25,000	190,000
Fee savings	-	(535,126)	(601,487)	(384,777)	(534,000)	(2,055,390)
Net savings realised	175,000	(510,126)	(501,487)	(294,777)	(444,000)	(1,575,390)

### Ongoing investment management costs

The following table sets out the investment management costs incurred between 2016-17 and 2019-20. Direct costs are those payable to the investment managers and are based on assets under management. Indirect costs are fees payable to LCIV in relation to its oversight role with regard to the Fund's passive assets held by Legal & General Investment Management and BlackRock.

	Asset pool		Non-asset pool		Fund total
	Direct	Indirect	Direct	Indirect	
<b>Ad Valorem</b>	114,162	45,413	5,472,073		5,631,648

### LCIV – additional information

More information on the London CIV, including contact details, can be found at the London CIV website at [www.londonciv.org.uk](http://www.londonciv.org.uk).