Pension Fund Committee

Date **Monday 28 February 2011**

Time **10.00 am**

Venue **Committee Room 2 - County Hall, Durham**

Business

Part A

1. Declarations of Interest (if any)

2. Minutes of the Meeting held on 13 September 2010 (Pages 1 - 4)

3. Graphs showing recent movements of the Stock and Share Indices (Pages 5 - 14)

4. Graphs showing recent movements of the major currencies against sterling (Pages 15 - 20)

5. Performance Measurement Report (Pages 21 - 28)

6. Pension Fund Investments (Pages 29 - 32)

7. Provisional Valuation Results (Pages 33 - 40)

8. Update on Annual Governance Report Recommendations for the Year Ended 31 March 2010 (Pages 41 - 48)

9. Pension Fund Policy Documents - Funding Strategy Statement and Statement of Investment Principles (Pages 49 - 94)

10. Such other business as, in the opinion of the Chairman of the meeting, is of sufficient urgency to warrant consideration

11. Any resolution relating to the exclusion of the public during the discussion of items containing exempt information

Part B

Items during which it is considered the meeting will not be open to the public (consideration of exempt or confidential information)

12. Minutes of the Meeting held on 13 September 2010 (Pages 95 - 100)

13. Verbal Report of Pension Fund Advisor

14. Report of Blackrock (Pages 101 - 112)

15. Report of Alliance Bernstein (Pages 113 - 150)

16. Report of CB Richard Ellis (Pages 151 - 182)

17. Report of Edinburgh Partners (Pages 183 - 226)

18. Report of Royal London Asset Management (Pages 227 - 278)

19. Report of Barings Asset Management Ltd (Pages 279 - 284)

20. Internal Audit Assurance (Pages 285 - 290)

21. Review of Pension Fund Arrangements (Pages 291 - 308)

22. Such other business as, in the opinion of the Chairman of the meeting, is of sufficient urgency to warrant consideration

Colette Longbottom
Head of Legal and Democratic Services

County Hall
Durham
18 February 2011

To: The Members of the Pension Fund Committee

County Council Members:
Councillors Andy Turner, N Martin, J Bailey, C Carr, J Chaplow, A Hopgood, J Lethbridge, P May, D Morgan and R Todd

Darlington Borough Council Members:
Councillor I G Haszeldine
Councillor C P McEwan

Scheduled Bodies Representative:
Mr D Sanders

Admitted Bodies Representative:
Mr K Tallintire

Pensioner Representative:
Mrs O Brown

Active Members Representative:
(vacancy)

Further Education Colleges Representative:
(vacancy)

Advisors:
County Council Officers

Chief Executive	G Garlick
Corporate Director of Resources	D McLure
Head of Legal and Democratic Services	C Longbottom
Principal Finance Officer – Strategic Finance	H Appleton

Independent Advisors:

P J Williams	Mr P J Williams
P Solve Asset Solution	Mr T Pike

Investment Managers:

Alliance Bernstein	Mr D Stewart Mr A Husain
Barings Asset Management	Mr N Davidson Mr P Stanion
Blackrock	Mr C Moore Ms F Ellard
CBRE	Mr K Farrelly Mr A Baum
Edinburgh Partners	Ms J Price Mr D Robertson

Royal London	Mr S Pierce Mr J Stoddart

Staff Observers:

UNISON	Mr N Hancock
GMB	

Contact: Jill Errington **Email: jill.errington@durham.gov.uk**
Tel: 0191 3706250

Durham County Council

At a Meeting of the **Pension Fund Committee** held at the **County Hall, Durham** on **Monday 13 September 2010** at **10.00 am in Committee Room 2**

Present:

Councillor N Martin in the Chair

Members:
Councillors C Carr, J Chaplow, A Hopgood, J Lethbridge, R Ord and R Todd

Admitted Bodies Representative:
Mr K Tallintire

Advisers:

Durham County Council Officers:

Principal Finance Officer – Strategic Finance:	H Appleton
Payroll and Pensions Manager:	N Orton

Independent Advisers:

P J Williams	Mr P J Williams
P Solve Asset Solution	Mr T Pike

Staff Observer:

Mr N Hancock

Apologies:

Councillors P May, D Morgan, A Turner, Darlington Borough Councillor C P McEwan and O Brown.

Councillor Martin, on behalf of the Committee conveyed best wishes to the Chair Councillor Andy Turner for a speedy recovery from illness.

A1 Minutes

The Minutes of the meeting held on 21 June 2010 were confirmed as a correct record subject to Councillor Ord's attendance being recorded.

The Chair signed the Minutes.

A2 Declarations of Interest

There were no declarations of interest received from Members in relation to the business on the agenda.

A3 Graphs Showing Recent Movements in Stock and Share Indices

Consideration was given to graphs showing recent movement in the Stock and Share Indices (for copy see file of Minutes).

Resolved:

That the information be noted.

A4 Graphs Showing Recent Movements in the Major Currencies Against Sterling

Consideration was given to graphs showing recent movement in the Major Currencies Against Sterling (for copy see file of Minutes).

Resolved:

That the information be noted.

A5 Performance Measurement Report

Consideration was given to the report of the Interim Corporate Director, Resources which provided an overview for Members of the performance of the Fund to date (for copy see file of Minutes).

Resolved:

That the report be noted.

At this point Councillor Carr entered the meeting.

A6 Pension Fund Investments

Consideration was given to the report of the Interim Corporate Director, Resources which informed Members of the overall value of the Pension Fund as at 30 June 2010, of the additional sums available to the Managers for further investment and of the result of the latest Fund Rebalancing. A table showing the cash rebalancing matrix was circulated for Members information (for copy see file of Minutes).

A Member queried the difference in the estimated expenditure for the quarter ended 31 March 2010 which was around £9m lower than the actual expenditure at the period end.

The Committee was advised that this was as a result of payments which had been incorrectly allocated as County Council payments but had since been rectified.

Resolved:

That the report be noted.

A7 Statement of Accounts for the Year Ended 31 March 2010

Consideration was given to the report of the Interim Corporate Director, Resources which informed Members of the Pension Fund Accounts which were included in the Statement of Accounts for Durham County Council for the financial year ended 31 March 2010 (for copy see file of Minutes).

Members were advised that The Statement of Accounts had been approved by Audit Committee but were subject to audit by the Audit Commission. An extract of the Statement of Accounts relating to the Pension Fund was attached to the report at Appendix 1.

In discussing the Pension Fund Accounts Members noted the current position in relation to cash flow resulting from the increased number of retirements following unitary status. Assurance was sought that this was a short term cash flow issue.

Resolved:

That the report be noted and an update be provided at the next meeting in relation to the current position on the Pension Fund cash flow situation.

A8 Annual Meeting of the Pension Fund

Consideration was given to the report of the Interim Corporate Director, Resources which informed Members of the Annual Meeting of the Pension Fund (for copy see file of Minutes).

A draft Agenda and timetable was attached to the report at Appendix 1 for Members' consideration and the meeting was due to be held on Thursday 4 November 2010, a different date to that scheduled in Members' diaries.

At this point Members expressed concern at the change in date and the scheduling of Council meetings in general and asked that their concerns be taken on board.

RESOLVED that the date of the Annual meeting be agreed, subject to the availability of the newly appointed Director of Corporate Resources.

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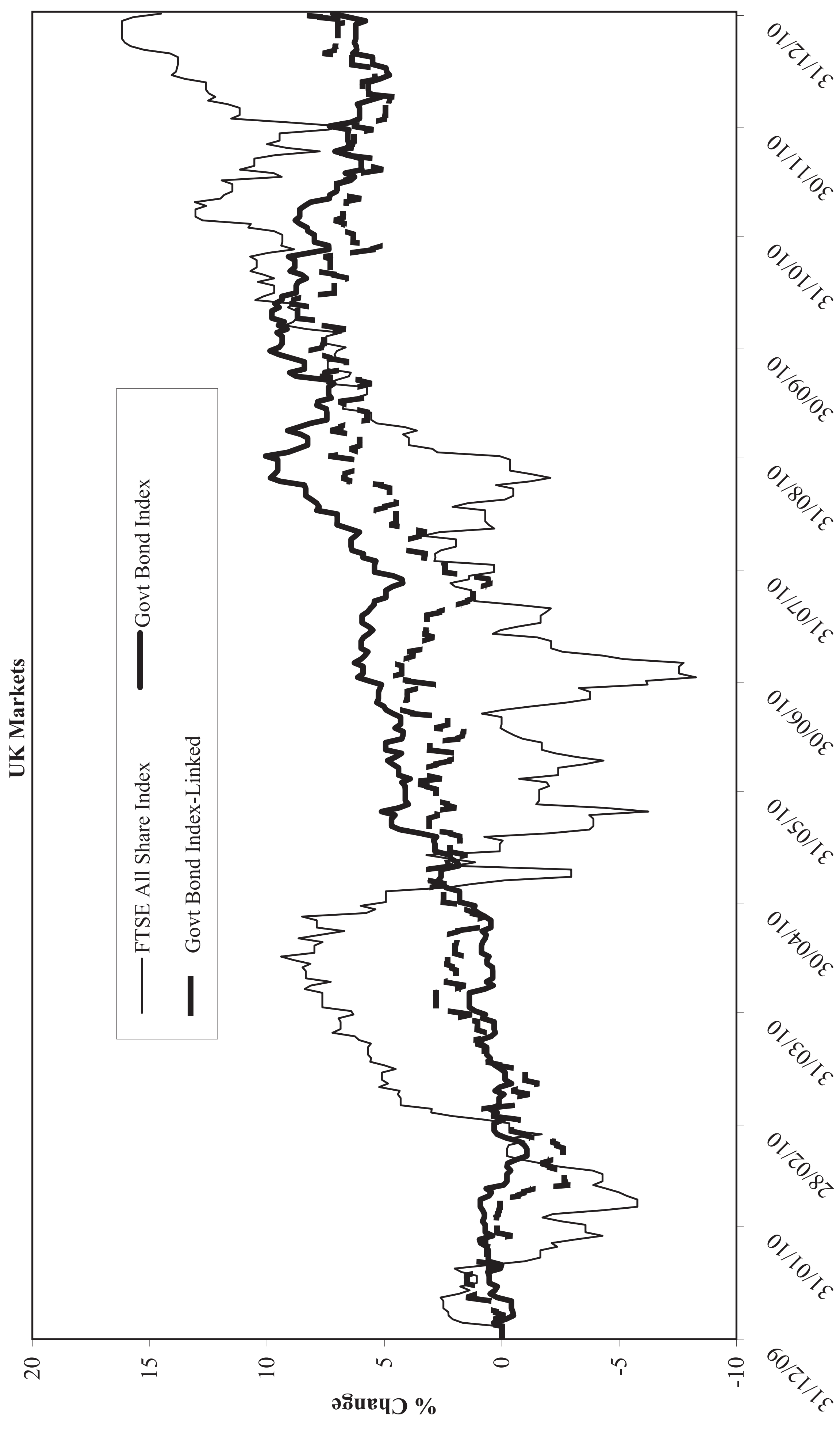
Agenda Item No.3



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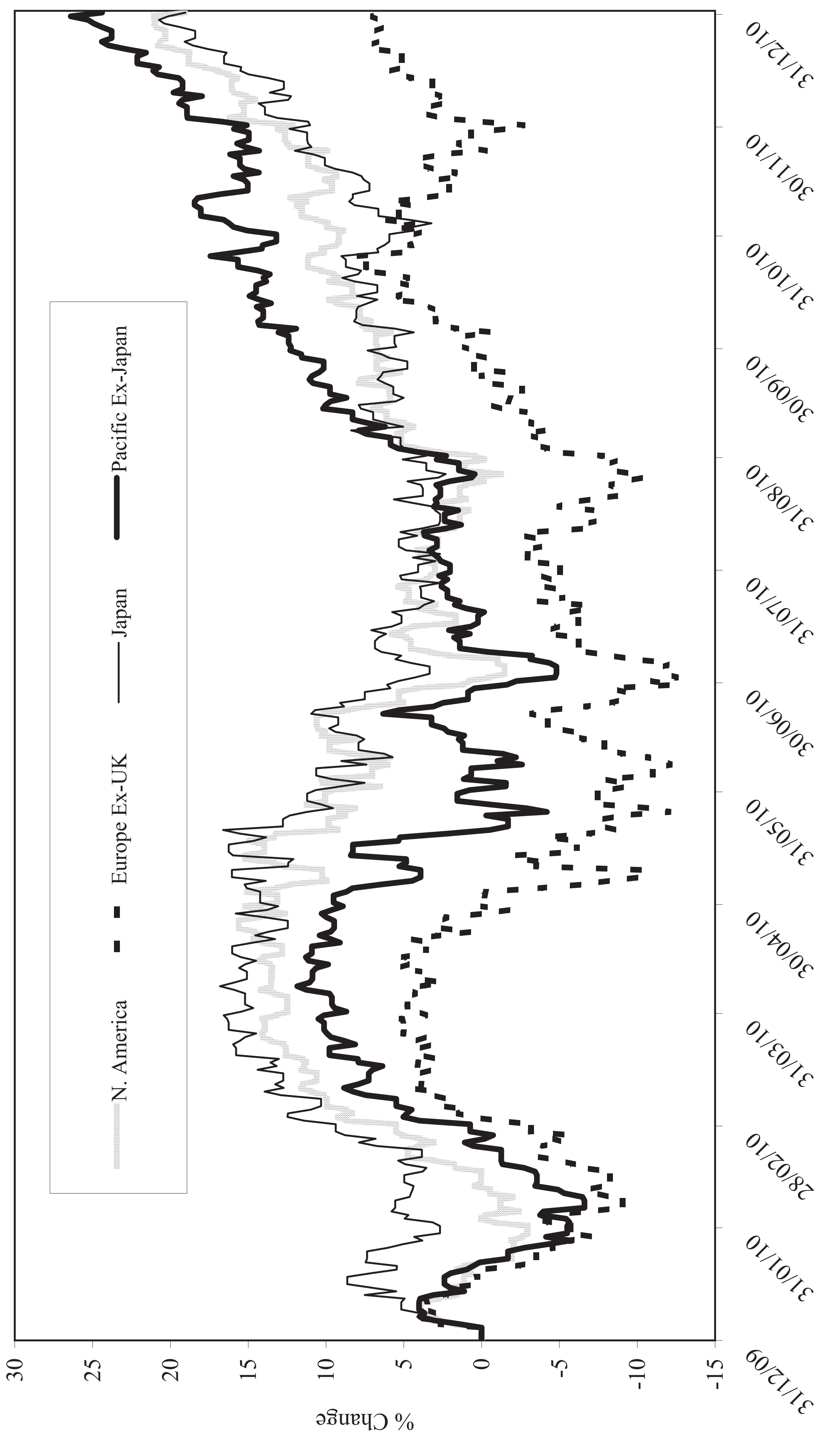
Overseas Equity Markets



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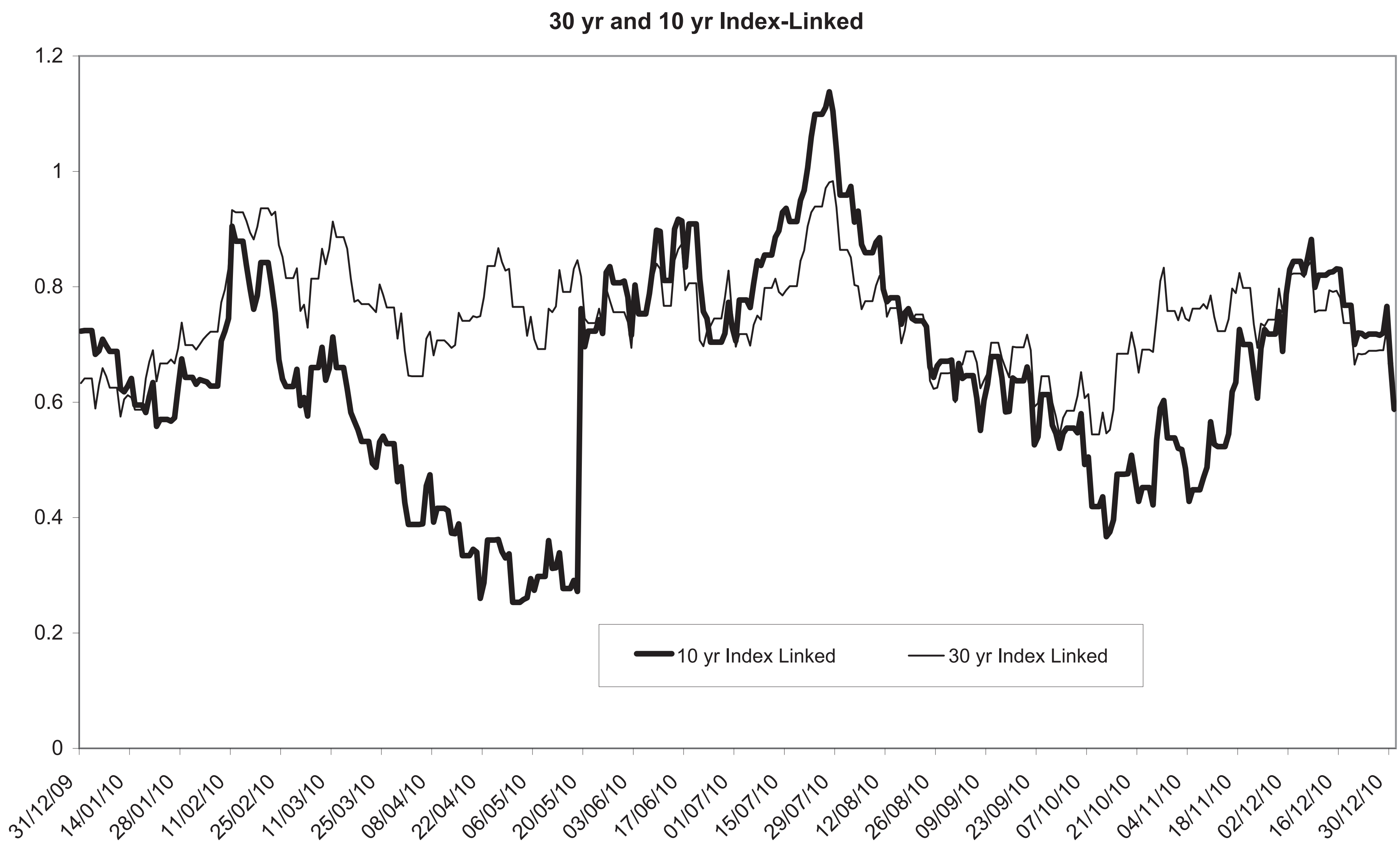
30 yr and 10 yr Index-Linked
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0.4
0.2
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14/01/10
28/01/10
11/02/10
25/02/10
11/03/10
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04/11/10
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10 yr Index Linked
30 yr Index Linked

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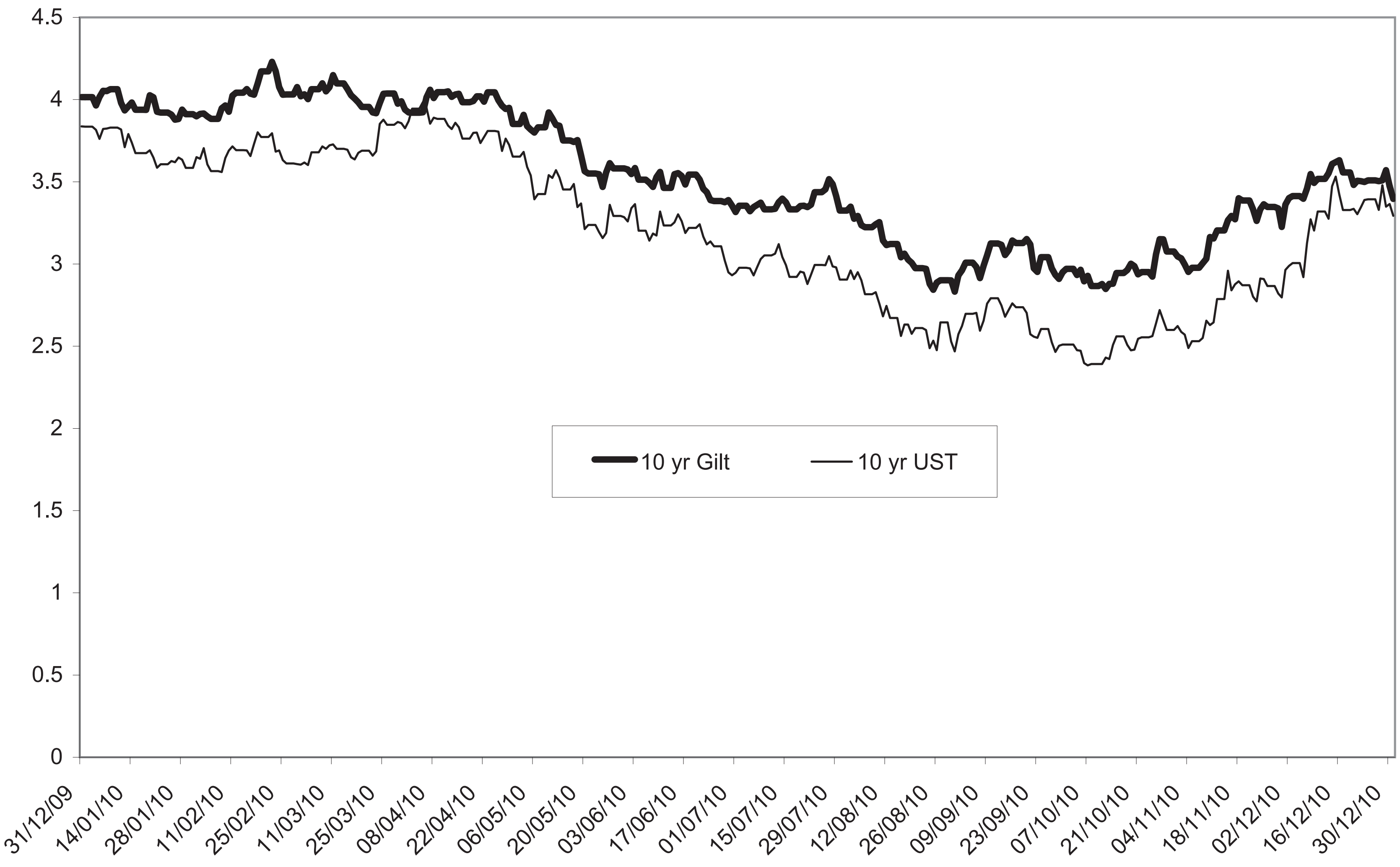
10 Year US and UK Government Bond Yields



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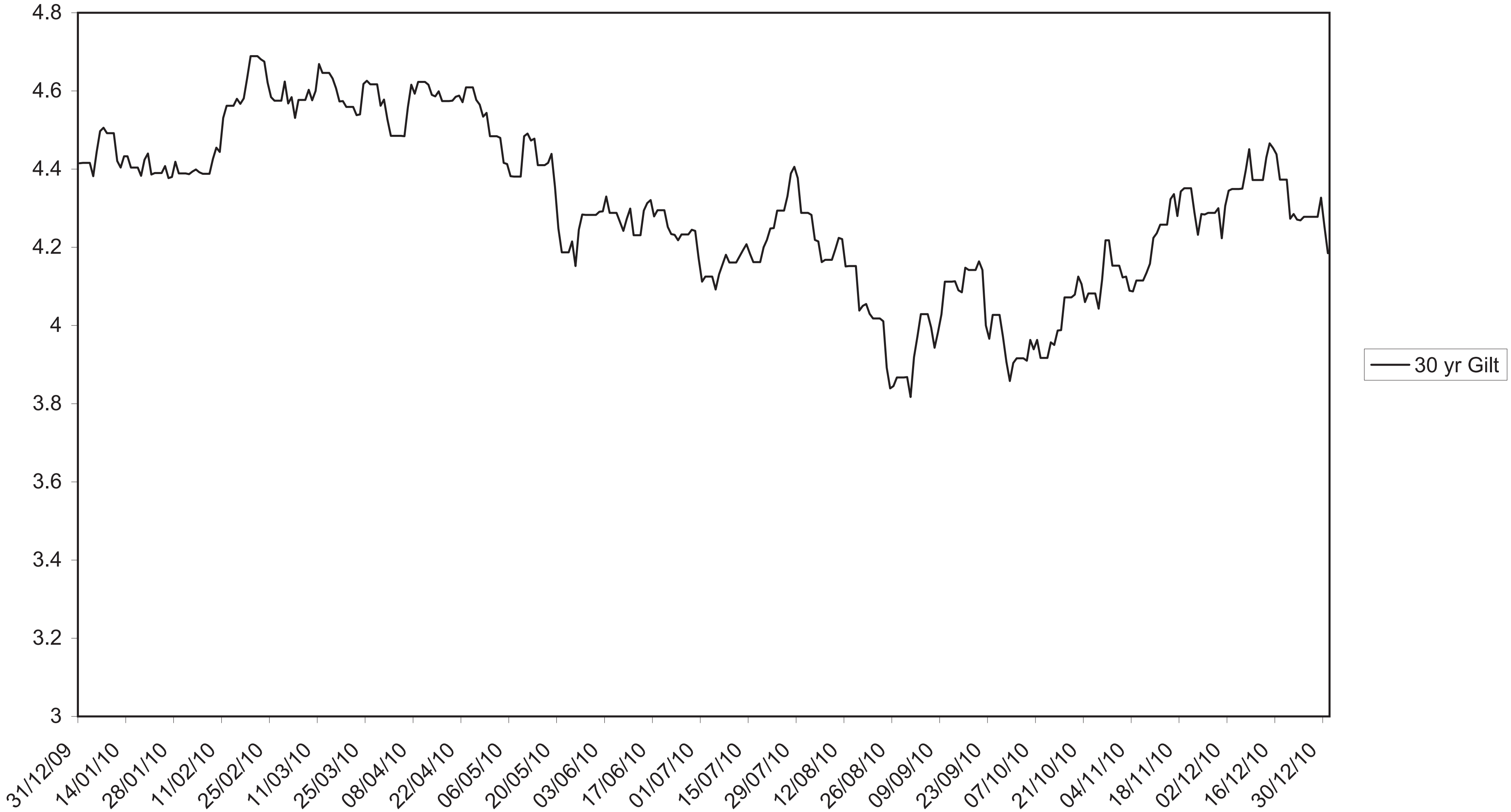
30 yr Gilt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30/12/10
30 yr Gilt

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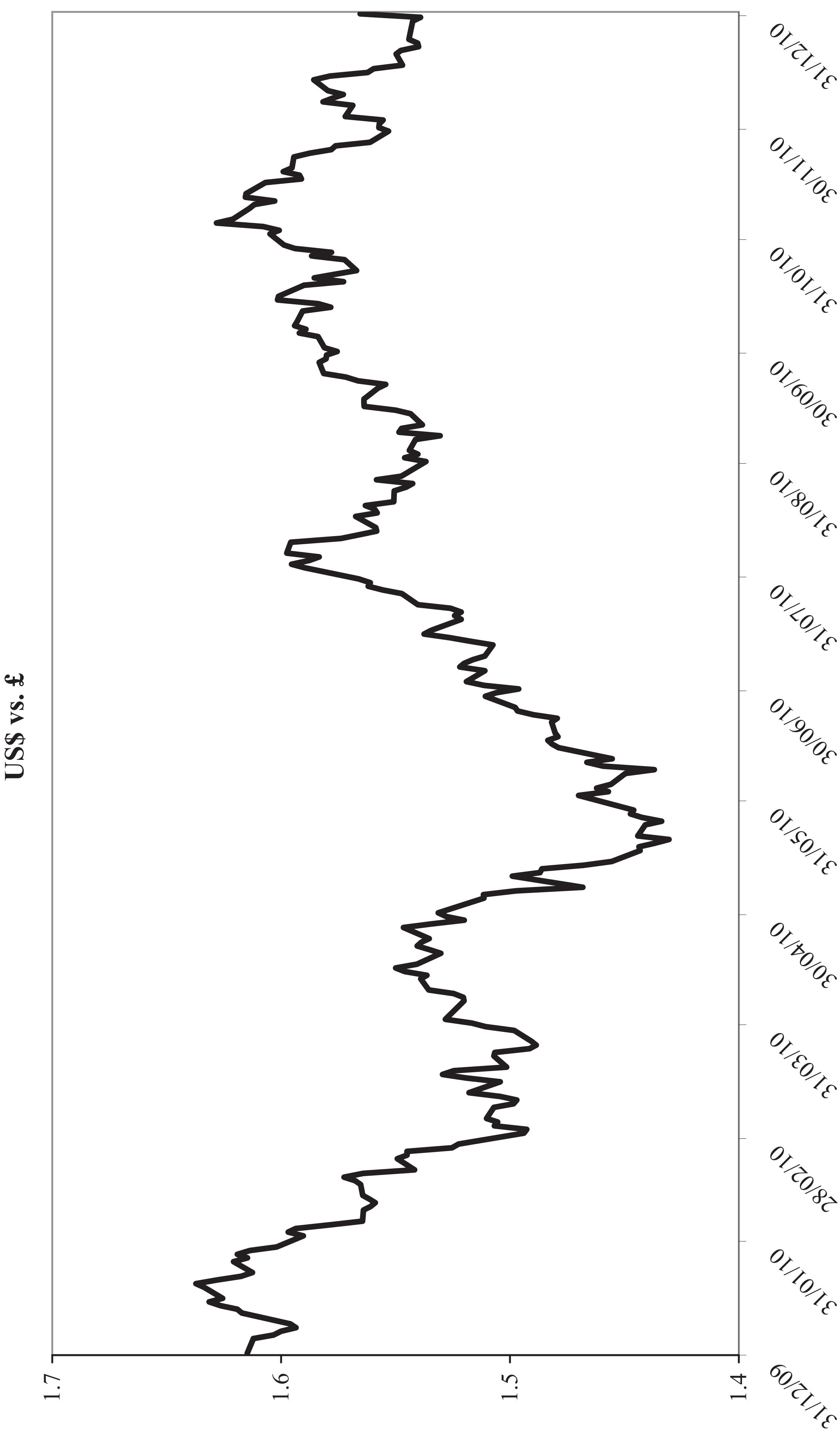
Agenda Item No.4



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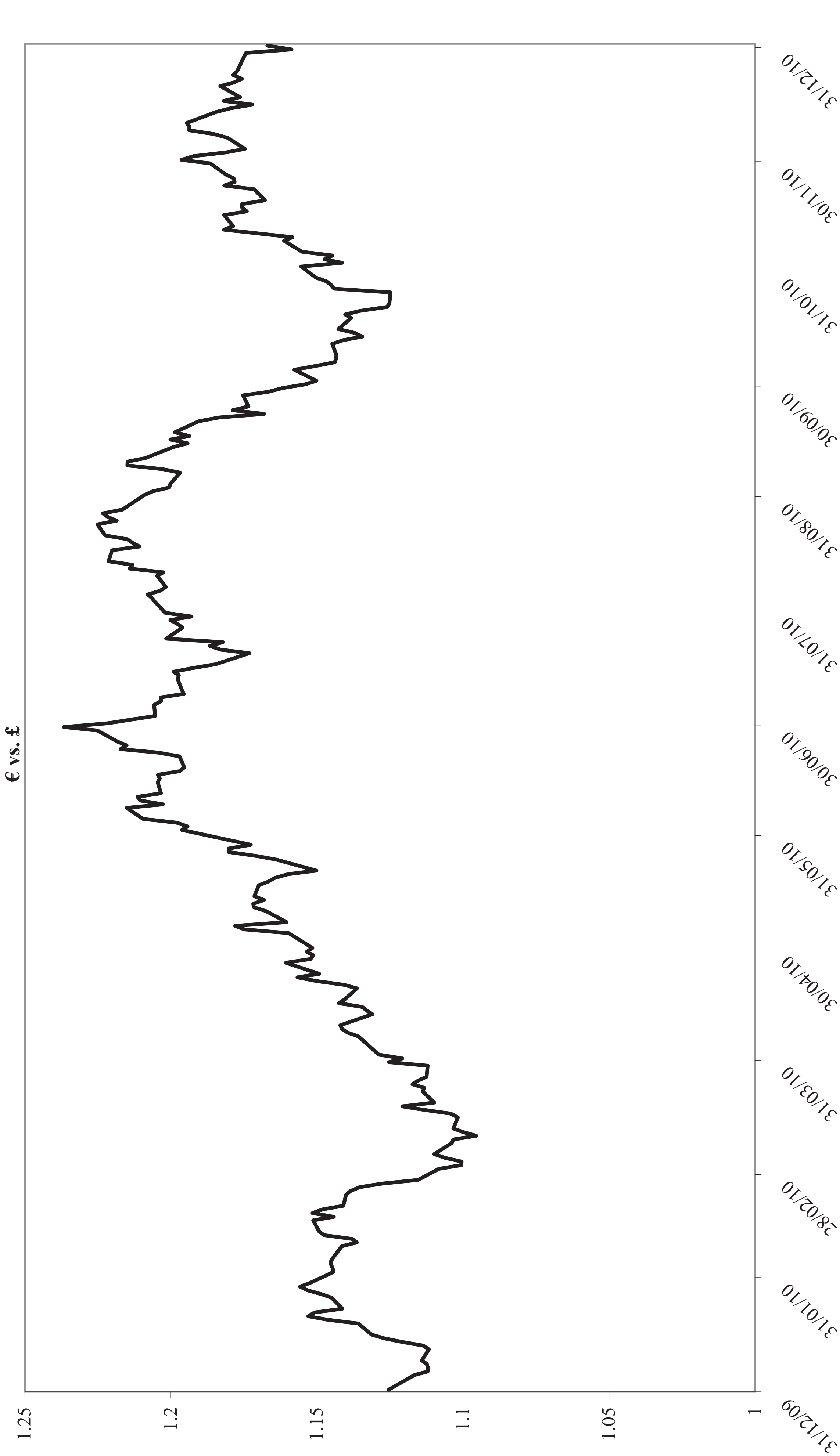
€ vs. £
1.25
1.2
1.15
1.1
1.05
1
31/12/09
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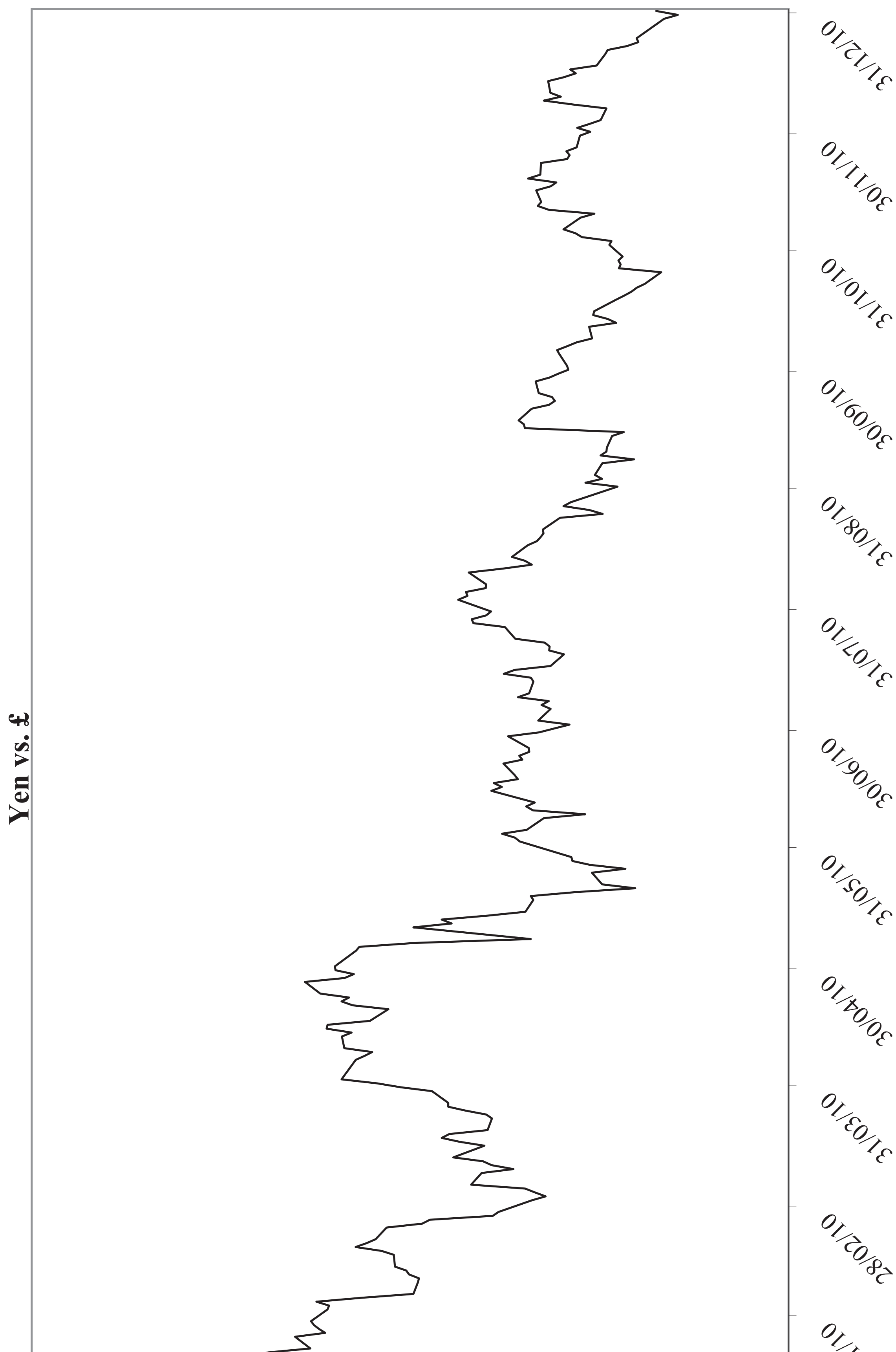
Yen vs. £
160
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30/11/10
31/12/10

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Pension Fund Committee

28 February 2011

Performance Measurement Report

Don McClure, Corporate Director, Resources

Purpose of the Report

1 The purpose of the report is to provide an overview for Members of the performance of the Fund to date.

Background

2 The performance of the six Managers is measured against personalised benchmarks chosen at the inception of the Fund. The attached report from JPMorgan, the Fund's custodian, shows:-

(a) The Managers benchmarks.

(b) The total Fund performance, for the quarter, year to date and since inception.

(c) The Managers' performance in absolute and relative terms against the relevant benchmarks, for the quarter, year to date and since inception.

(d) A portfolio comparison for the quarter ended 31 December 2010 and for the period since inception.

Recommendation

3 Members note the information contained in this report.

Contact: Hilary Appleton Tel: 0191 3833544

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J.P.Morgan

Worldwide Securities Services

Performance Measurement Report
for
Durham County Council Pension Fund

for period ending
December 31, 2010

Contents

Page

Benchmark Association Table

PORTFOLIO	INDEX	TARGET	WEIGHT %
Edinburgh Partners	MSCI AC World Index (Gross)	+3% pa	100.00
Blackrock	FTSE All Share (Gross)	+3% pa	100.00
Alliance Berstein	GBP Libor	+3% pa	100.00
Royal London	FTSE index Linked >5 years	+0.5% pa	100.00
Barings	GBP Libor	+4% pa	100.00
CBRE 1	Headline RPI	+5% pa	100.00
CBRE 2	Headline RPI	+5% pa	100.00
Re Alliance Berstein PPIP	GBP Libor	+3% pa	100.00
Total Plan Composite	Manager Weighted benchmark	Not Applicable	100.00

Executive Summary of Total Plan as at 31/12/2010

Overview

During the quarter the total market value of the Durham County Council Pension Plan increased by +£72.71m to £1,724.36m. Net contributions to the plan over the quarter were +£3.67m, net gains were therefore +£69.04m.

The performance return for the Plan over the fourth quarter of 2010 was +4.11%, compared to the Plan benchmark return of +5.33%. The Plan therefore underperformed the benchmark by -1.22%.

Equity markets were up over the fourth quarter with the FTSE All Share rising around +8.18% and the MSCI AC World index also up by around +10.35% in Sterling terms. Index Linked bonds were also up with the FTSE index linked over 5 years index gaining around +1.22%.

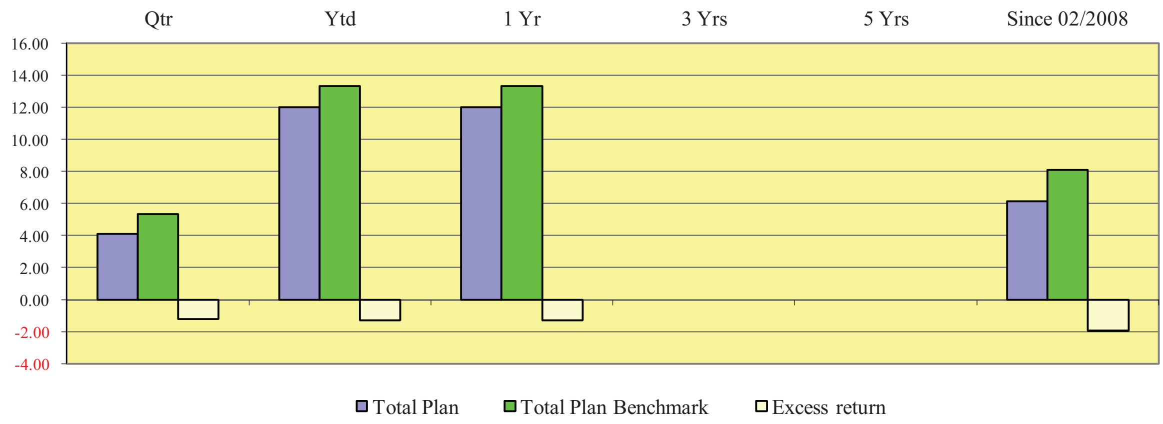
Market Values

	In GBP mil's			
	Qtr 4 - 10	**Qtr 3 - 10**	**Qtr 2 - 10**	**Qtr 1 - 10**
Total Plan	**1,724.36**	**1,651.65**	**1,560.54**	**1,651.49**

Performance

	Performance (%) *					
	Qtr	**Ytd**	**1 Yr**	**3 Yrs**	**5 Yrs**	**Since 02/2008**
Total Plan	4.11	12.01	12.01	-	-	6.14
Total Plan Benchmark	5.33	13.30	13.30	-	-	8.08
Excess return	*-1.22*	*-1.29*	*-1.29*			*-1.93*

Total Plan Performance

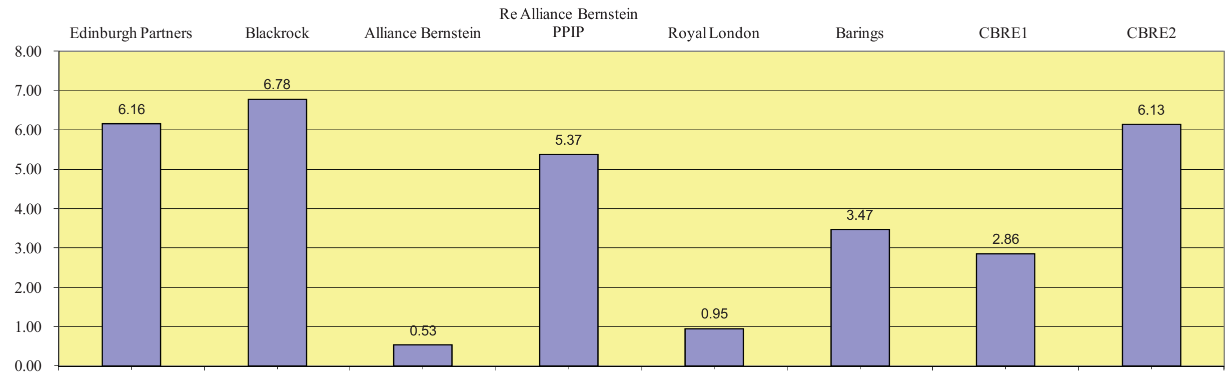


Total Plan Performance Returns as at 31/12/10

Currency GBP		**Performance (%) ***					
	Mkt. Val. in Mil's	**Qtr**	**Ytd**	**1 Year**	**2 Years**	**3 Years**	**Since 02/2008**
Total Plan	**1724.4**	4.11	12.01	12.01	15.30	-	6.14
Total Plan Benchmark		5.33	13.30	13.30	14.32	-	8.08
Excess return		-1.22	-1.29	-1.29	0.97		-1.93

	Mkt. Val. in Mil's	**Qtr**	**Ytd**	**1 Year**	**2 Years**	**3 Years**	**Since 02/2008**
Edinburgh Partners	**505.3**	6.16	8.27	8.27	13.35	-	5.93
MSCI AC World Index (Gross) +3% pa		10.35	20.27	20.27	22.22	-	10.81
Excess return		-4.19	-12.00	-12.00	-8.87		-4.88
Blackrock	**388.8**	6.78	21.08	21.08	28.23	-	5.92
FTSE All Share (Gross) +3% pa		8.18	17.96	17.96	25.74	-	7.72
Excess return		-1.40	3.11	3.11	2.49		-1.81
Alliance Bernstein	**234.0**	0.53	7.34	7.34	14.50	-	4.74
GBP Libor +3% pa		0.93	3.71	3.71	3.98	-	5.33
Excess return		-0.39	3.63	3.63	10.52		-0.59
Re Alliance Bernstein PPIP	**25.8**	5.37	30.12	30.12	-	-	28.05
GBP Libor +3% pa		0.93	3.71	3.71	-	-	3.70
Excess return		4.45	26.41	26.41			24.34
Royal London	**333.5**	0.95	9.66	9.66	8.04	-	6.56
FTSE index Linked >5 years +0.5% pa		1.22	9.60	9.60	7.84	-	6.20
Excess return		-0.27	0.06	0.06	0.20		0.37
Barings	**140.5**	3.47	10.87	10.87	16.71	-	9.42
GBP Libor +4% pa		1.17	4.71	4.71	4.98	-	6.35
Excess return		2.30	6.16	6.16	11.73		3.07
CBRE1	**63.4**	2.86	9.97	9.97	-1.81	-	-7.26
Headline RPI +5% pa		2.61	9.99	9.99	8.74	-	7.89
Excess return		0.24	-0.02	-0.02	-10.55		-15.15
CBRE2	**33.1**	6.13	18.57	18.57	32.43	-	3.37
Headline RPI +5% pa		2.61	9.99	9.99	8.74	-	7.89
Excess return		3.52	8.59	8.59	23.69		-4.53

Manager Quarterly Returns

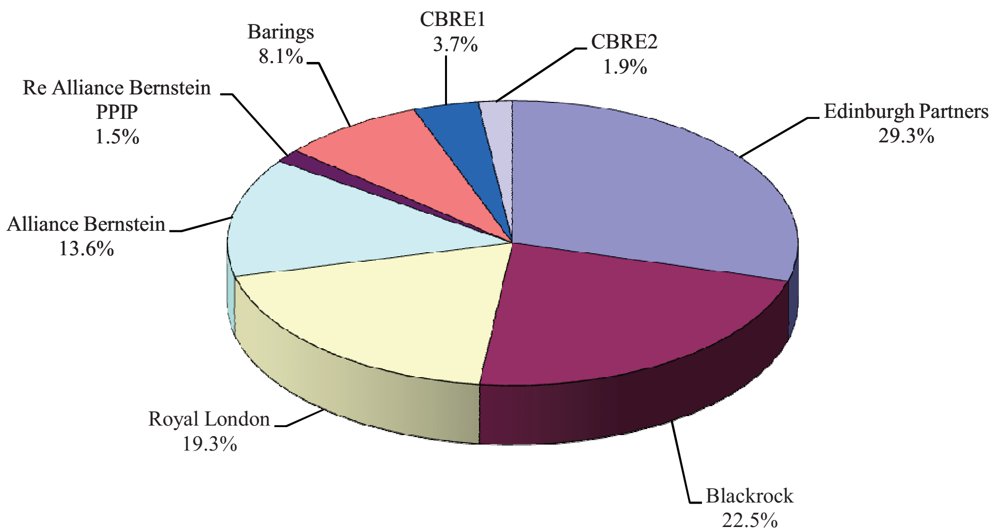


***All Portfolio and Composite returns are Gross of Fees. For time periods in excess of 1 year the performance returns are annualised.**

Portfolio Comparison for Quarter 4, 2010

Portfolio Name	Current Market Value	Portfolio Weight	Portfolio Return (%)	Benchmark Return (%)	Excess Return (%)	Current Contribution to Return
Total Plan	**1,724,357,963**	**100.00%**	**4.11**	**5.33**	**(1.22)**	
Edinburgh Partners	505,320,818	29.30%	6.16	10.35	(4.19)	1.50
Blackrock	388,757,681	22.55%	6.78	8.18	(1.40)	0.18
Royal London	333,472,002	19.34%	0.95	1.22	(0.27)	0.08
Alliance Bernstein	233,988,073	13.57%	0.53	0.93	(0.39)	1.79
Re Alliance Bernstein PPIP	25,811,183	1.50%	5.37	0.93	4.45	0.29
Barings	140,503,317	8.15%	3.47	1.17	2.30	0.11
CBRE1	63,408,854	3.68%	2.86	2.61	0.24	0.12
CBRE2	33,096,036	1.92%	6.13	2.61	3.52	0.08

Manager Allocation



Portfolio Comparison for Year to Date, 2010

Portfolio Name	Current Market Value	Portfolio Weight	Portfolio Return (%)	Benchmark Return (%)	Excess Return (%)	Current Contribution to Return
Total Plan	**1,724,357,963**	**100.00%**	**12.01**	**13.30**	**(1.29)**	
Edinburgh Partners	505,320,818	29.30%	8.27	20.27	(12.00)	4.40
Blackrock	388,757,681	22.55%	21.08	17.96	3.11	1.85
Royal London	333,472,002	19.34%	9.66	9.60	0.06	1.08
Alliance Bernstein	233,988,073	13.57%	7.34	3.71	3.63	2.69
Re Alliance Bernstein PPIP	25,811,183	1.50%	30.12	3.71	26.41	0.87
Barings	140,503,317	8.15%	10.87	4.71	6.16	0.32
CBRE1	63,408,854	3.68%	9.97	9.99	(0.02)	0.33
CBRE2	33,096,036	1.92%	18.57	9.99	8.59	0.17

Pension Fund Committee

28 February 2011

Pension Fund Investments

Don McLure, Corporate Director Resources

Purpose of the Report

1. To inform the Committee of the overall value of the Pension Fund as at 31 December 2010 of the additional sums available to the Managers for further investment and of the result of the latest Fund Rebalancing.

Value of the Fund

2. Reports from the six appointed Managers AllianceBernstein, Barings, BlackRock, CBRE, Edinburgh Partners and Royal London have been sent out with the papers but for information the Value of the Fund as at 31 December 2010 was £1,724,211,893.

Allocation of New Money

3. Table 1 details the cash position of the Fund, cash flow for the last four quarters, and an estimated cash flow for the quarter ending 31 December 2010.

4. In determining the amount of cash to be allocated to Managers at the quarter ended 31 March 2011, the un-invested cash balance at the end of the previous quarter, together with interest received in that quarter, is considered. The amount allocated to each Manager is subject to the need to retain money to meet the Fund's net cash outflow. After taking these issues into account it was decided that no money be added to the sums to be allocated to the Managers for investment in the quarter.

Fund Rebalancing

5. Table 2 showing the Cash Rebalancing matrix. From this quarter the dates for the rebalancing will be set in advance, and I list them below. The rebalancing will reflect the figures shown in the “Rebalanced” column.

Committee/Meeting Date	Date of Rebalancing
28 February 2011	24 March 2011
6 June 2011	7 July 2011
5 September 2011	6 October 2011
6 December 2011	12 January 2012
5 March 2012	29 March 2012

Recommendation

6. Members are asked to note the information contained in this report.

Contact: Hilary Appleton Tel: 0191 3833544

TABLE 1

	31.3.10		30.06.10		30.09.10		31.12.10		31.03.11
Quarter Ended (1)	**Estimate** (2)	**Actual** (3)	**Estimate** (4)	**Actual** (5)	**Estimate** (6)	**Actual** (7)	**Estimate** (8)	**Actual** (9)	**Estimate** (10)
	£	£	£	£	£	£	£	£	£
Contributions - DCC	17,100,000	17,035,039	17,000,000	17,316,968	17,000,000	17,510,856	17,500,000	17,738,724	17,400,000
- Other	7,800,000	7,778,191	7,800,000	7,408,084	7,400,000	7,344,735	7,400,000	7,191,370	7,300,000
Pensions Increase	1,500,000	1,642,355	1,000,000	835,214	800,000	1,903,957	1,200,000	1,136,723	1,100,000
Transfer Values	2,500,000	2,483,105	1,500,000	1,719,376	1,800,000	2,819,490	2,000,000	1,854,135	2,000,000
Loans Repaid	0	0	0	0	0	0	0	0	0
Other Income	0	0	0	2,173,219	0	1,421,218	1,000,000	1,029,707	500,000
Gross Dividend & Interest	300,000	0	0	0	0	0	0	0	0
Total Income	29,200,000	28,938,690	27,300,000	29,452,801	27,000,000	31,300,256	29,100,000	28,950,659	28,300,000
Payroll Paysheets	18,000,000	27,994,283	18,000,000	17,316,968	17,000,000	17,510,856	17,500,000	17,728,137	18,000,000
Payables Paysheets (incl. Managers' fees)	9,000,000	10,110,870	10,000.000	11,593,086	10,000,000	9,964,085	10,000,00	8,100,045	8,500,000
Total Expenditure	27,000,000	38,105,153	28,000,000	28,910,054	27,000,000	27,474,941	27,500,000	25,828,182	26,500,000
Surplus / (Deficit)	2,200,000	(9,166,463)	(700,000)	542,807	0	3,525,315	1,600,000	3,122,477	1,800,000
Net Capital payments/(receipts)		644,336		0		996,160		3,670,489	
Balance at Bank (opening)		19,915,225		5,882,733		2,053,829		25,087,188	
Balance at Bank (closing)		5,882,733		2,053,829		25,087,188		22,235,857	
Money paid/(recovered) to/(from Manager)		0		0		20,000,000		0	

REBALANCING OF Durham P/F ASSETS

Strategic Fund	Benchmark Proportion	Mandate Type
Matching Fund	20%	Government Bonds
Investment Fund	80%	Various

After Rebalancing	
20.0%	344.88
80.0%	1379.52
100.0%	1724.40

	31-Dec-10 Value	%	Target	+/- Allocation £m	Rebalanced £m	%	5% Tolerance Min % (95%)	Min £m.	Max % (105%)	Max £m.	Outside Limit	
Matching Bond Manager												
RLAM	333.50	19.3%	**20.0%**	20.4	353.89	**20.5%**	19.0%	327.64	21.0%	362.12	0.00	0.00
Matching Fund sub-total	333.50	19.3%	**20.0%**	20.4	353.89	**20.5%**	19.0%	327.64	21.0%	362.12	0.00	0.00
UK Equity Manager												
Blackrock	388.80	22.5%	**20.0%**	-34.9	353.89	**20.5%**	19.0%	327.64	21.0%	362.12	0.00	-26.68
Broad Bond Manager	**£m**											
AllianceBernstein	259.80	15.1%	**16.0%**	23.3	283.11	**16.4%**	15.2%	262.11	16.8%	289.70	2.31	0.00
Global Equity Manager	**£m**											
Edinburgh Partners	505.30	29.3%	**28.0%**	-9.9	495.45	**28.7%**	26.6%	458.69	29.4%	506.97	0.00	0.00
DAA Manager												
Barings	140.50	8.1%	**8.0%**	1.1	141.56	**8.2%**	7.6%	131.05	8.4%	144.85	0.00	0.00
Global Property Manager												
CBRE 1		0.0%										
CBRE 2		0.0%										
Allocated undrawn cash					41.5							
Sub-Total	96.50	5.6%	**8.0%**	0.0	96.50	**5.6%**	7.6%	131.05	8.4%	144.85	34.55	0.00
Investment Fund sub-total	1390.90	80.7%	**80.0%**	-20.4	1370.51	**79.5%**	76.0%	1310.54	84.0%	1448.50	0.00	0.00
Investments sub-total	1724.40	100.0%	**100.0%**	0.00	466.12	**100.0%**	95.0%	393.16	95.2%	1642.29	0.00	-82.11
Cash												
Internal Cash	0.00			0.0								
Cash at Custodian	0.00			0.0								
Cash sub-total	0.00	0.0%	**0.0%**	0.0	0.00	0.0%	0.0%	0.00	0.0%	0.00	0.00	0.00
Fund Total	**1724.40**	**100.0%**	**100.0%**	**0.00**	**1724.40**	**100.0%**					**34.55**	**-82.11**

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Pension Fund Committee

28th February 2011

Provisional Valuation Results

Report of Don McLure, Corporate Director, Resources

Purpose of the Report

1 The purpose of the report is to advise Members of the provisional results of the actuarial valuation of the Pension Fund as at 31 March 2010.

Background

2 Every three years the actuary carries out a valuation of the Pension Fund, comparing the market value of the assets with the assumed value of the liabilities and this is used to set employer contribution rates for the three year period after the results are certified.

3 The actuary presented indicative provisional whole Fund results to the Annual General Meeting in November, which showed the overall funding position would be broadly similar to the last valuation. Individual employer results were not available at that time but the actuary commented that although contribution rates for scheduled body employers were not likely to change significantly, there may be significant changes for some admitted body employers.

Actuarial Assumptions Provisional Actuarial Valuation Results

4 The financial assumptions used by the actuary are as follows, shown alongside the assumptions used at the previous valuation for comparison:

	2010 Valuation Basis (%pa)	2007 Valuation Basis (%pa)
Discount rate (in service)	6.8%	6.2%
General pay increases	5.3%	4.7%
Retail price inflation	3.8%	3.2%
Consumer price inflation	3.3%	n/a
Pension increases (on benefits in excess of GMPs)	3.3%	3.2%
Pension increases on post-88 GMPs	2.7%	2.7%
Deferred pension increases	3.3%	3.2%
GMP increases in deferment	5.3%	4.7%

5 The demographic assumptions used by the actuary are set out at Appendix A.

Provisional Actuarial Valuation Results – Past Service Funding Position

6 The table below sets out the past service funding position of the Fund on this basis alongside the results from the previous valuation for comparison:

	Provisional 2010 Valuation Results (£M)	2007 Valuation Results (£M)
Value of past service benefits for		
- Actives	1,057.3	948.0
- Deferred pensioners	206.8	168.6
- Pensioners	844.0	724.7
Funding target	2,108.1	1,841.3
Value of assets	1,662.9	1,459.2
Past service deficiency	**445.2**	**382.1**
Funding ratio	**79%**	**79%**

Provisional Actuarial Valuation Results – Overall Employer Contribution Rate

7 The table at paragraph 10 below shows the contribution rate as a percentage of payroll for the Fund as a whole with shortfall contributions assuming a stable pensionable workforce and a recovery period of 19 years. A stable pensionable workforce in

this context implies that pensionable payroll increases in line with the actuary's salary increase assumption of 5.3% a year.

8 In the current environment it is unlikely there will be a stable workforce going forward and contribution rates quoted would therefore not be enough to meet the shortfall over 19 years. The actuary has recommended that shortfall contributions are expressed as monetary amounts which will give more certainty to the amount being paid to meet the shortfall. The table also shows the employer contribution rate for the whole Fund it the past service shortfall as at 31 March 2010 is recovered as a series of shortfall contributions which are

- Fixed in cash terms as at 1 April 2011, and increasing each April after that at the rate of 5.3% a year (the salary increase assumption)
- Payable for a period of 19 years from 1 April 2011 in monthly instalments

The initial monetary amount has been worked out as the shortfall contribution set out in the first part of the table assuming members' pensionable pay over the year commencing 1 April 2011 is £418M (the pensionable salary data provided to the actuary increased by 5.3% a year for two years). These amounts would increase on 1 April 2012 and every subsequent April by 5.3%.

9 Probability of funding success is also shown. The actuary has confirmed an appropriate adjustment has been made to take account of the change to pension increases (from being based on increases to the Retail Prices Index (RPI) to being based on increases to the Consumer Prices Index (CPI)).

10 **Required 2010 Valuation whole Fund contribution rates (with 2007 result shown for comparison)**

	Proposed 2010 Valuation Basis (% of Pensionable Pay)	2007 Valuation Results (% of Pensionable Pay)
Value of benefits accruing	19.0	19.5
Death in service lump sum	0.4	0.4
Administration expenses	0.3	0.3
Employee contributions	(6.4)	(6.3)
Employer future service contribution rate	**13.3**	**13.9**
Deficiency contributions (recovery period of 19 years)	**6.6**	**6.3**
Total employer contribution rate	**19.9**	**20.2**
Annual deficiency contribution required in 2011/12	**£27.6M**	
Approximate probability of funding success	67%	

Provisional Actuarial Valuation Results – Individual Employer Contribution Rates

11 The actuary has calculated individual employer contribution rates for each employer with active members in the Fund. Some categories of employer are facing more challenging valuation results than others. In particular, admission bodies that do not have any guarantee from a scheduled body employer, or where there is either a small length of time left on their contract or they are closed to new entrants may be facing significant increases to rates.

12 Most employers are having to take into account the split contributions that will apply from 1 April 2011, with a specific monetary amount being required for the deficit recovery payments as well as the ongoing percentage rate for future service cost.

13 We have now advised employers of the new rates required over the next three years and will work with employers to discuss any difficulties the new rates may cause them.

Next steps

14 The actuary is expected to produce a full valuation report by the end of March. When this is available copies will be provided to Members and to all contributing employers.

Recommendation

15 Members are asked to note this report.

Contact:	Nick Orton	Tel:	0191 383 4429

Demographic Assumptions for the 2010 Actuarial Valuation

Post-retirement mortality	Base Rates Normal Health: Standard SAPS All Lives base tables making allowance for improvements in mortality in line with the CMI 2009 M/F improvement factors to 2010. Ill-health: Standard SAPS Ill-heath tables making allowance for improvements in mortality in line with the CMI 2009 M/F improvement factors to 2010. Scaling Factors Rates adjusted by scaling factors as dictated by Fund experience Males (normal health) 105% Females (normal health) 105% Males (ill-health) 110% Females (ill-health) 110% Future Improvement to Base Rates An allowance for improvements in line with the CMI 2009 M/F improvements with a long term rate of 1.25% p.a.
Pre-retirement mortality	Males: Standard SAPS All lives table scaled by 75% Females: Standard SAPS All lives table scaled by 75%
Early retirements	All members are assumed to retire at the earliest age at which they can retire as of right, with no reduction to benefits accrued prior to 1 April 2008. Members joining on or after 1 October 2006 are assumed to retire at age 65.
Withdrawals	Allowance made for withdrawals from service. On withdrawal, members are assumed to leave a deferred pension in the Fund, and are not assumed to exercise their option to take a transfer value.
Retirement due to ill health	Allowance made for retirements due to ill health. Proportions assumed to fall into the different benefit tiers applicable after 1 April 2008 are: Tier 1 (upper tier) 70% Tier 2 (middle tier) 15% Tier 3 (lower tier) 15%

Demographic Assumptions for the 2010 Actuarial Valuation

Family details	A man is assumed to be 3 years older than his spouse, civil partner or cohabitee. A woman is assumed to be 3 years younger than her spouse, civil partner or cohabitee. 90% of non-pensioners are assumed to be married / cohabiting at retirement or earlier death. 90% of pensioners are assumed to be married / cohabiting at their retirement date.
Commutation	Each member assumed to exchange 60% of the maximum amount permitted of their past service pension entitlements. Each member assumed to exchange 80% of the maximum amount permitted of their future service pension entitlements.
Promotional salary increases	Allowance made for age-related promotional increases.
Expenses	0.3% of Pensionable Pay added to the cost of future benefit accrual.

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Pension Fund Committee

28th February 2011

Update on Annual Governance Report Recommendations for the year ended 31st March 2010

Report of Don McLure, Corporate Director Resources

Purpose of the Report

1 To inform Members of the progress on addressing the recommendations of the Audit Commission's Annual Governance Report for the financial year ended 31st March 2010.

Background

2 A report to the Pension Fund Committee on 29th November 2010 included the Pension Fund Annual Report and Accounts and the Annual Governance Report for the Pension Fund.

Pension Fund Accounts

3 For the first time for 2009/10, there was a separate Audit opinion for the Pension Fund Accounts. This opinion was included in the Annual Report on pages 33 to 35 and stated that, in his opinion:

- the pension fund accounting statements and related notes give a true and fair view, in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2009: A Statement of Recommended Practice, of the financial transactions of the Pension Fund during the year ended 31st March 2010, and the amount and disposition of the fund's assets and liabilities as at 31st March 2010, other than liabilities to pay pensions and other benefits after the end of the scheme year; and

- the information given in the commentary on financial performance included within the Pension Fund Annual Report is consistent with the pension fund accounting statements.

Annual Governance Report

4 The Audit Commission also completed a separate Annual Governance Report for the Pension Fund. There are a number of recommendations for improvements and actions to rectify problems have been identified and reported at Appendix 1 to this report.

5 A commentary reviewing progress on each of the 13 recommendations has also been included in the Appendix 1.

Summary

6 Members are asked to note the contents of this report.

Background papers

(a) Pension Fund Committee 29th November 2010 – Annual Report and Accounts for the year ended 31st March 2010

Contact: Hilary Appleton Tel: 0191 383 3544

Appendix 1: Appendix 5 of the Annual Governance Report 2009/10 – with review of progress

Recommendations	
Recommendation 1	
Strengthen internal quality control to ensure errors in the financial statements are minimised.	
Responsibility	Hilary Appleton
Priority	High
Date	27th October 2010
Comments	During the 2009/10 year end a process for the review of working papers and reconciliations was introduced that will be continued in the 2010/11 year end. Additionally a quarter end is to be introduced to ensure more regular reconciliation of key accounts. Officers now have a clearer understanding of the systems and processes involved in the compilation of financial data and the control points and where to introduce new controls of the data and these have been documented.
Review of Progress	The review of working papers is to continue for 2010/11 closedown. Quarter end procedures have not as yet been introduced, but investments and all significant Balance Sheet Account Balances are now reconciled on a monthly basis.
Recommendation 2	
Ensure the closedown timetable is monitored by an appropriate officer to ensure that draft accounts are submitted on time, supported by accurate and complete working papers.	
Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	A comprehensive timetable was used and monitored that detailed the working papers required during the 2009/10 year end. Unfortunately there was slippage against the timetable due to the quantity of reconciliation work required, partly due to vacant posts in the Strategic Finance area as a result of Local Government Reorganisation. It is understood that generally the quality of working papers submitted was of high standard and allowed queries to be quickly and easily resolved once raised.
Review of Progress	A closedown timetable will be prepared for 2010/11. This will be reviewed and monitored by Strategic Finance. All account reconciliations will be supported by working papers which will be reviewed, referenced, dated, signed and filed.
Recommendation 3	
Strengthen accounting records maintained for augmentation payments and ensure that Pension SORP requirements for inclusion of augmentation payments are complied with in 2010/11.	

Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	The requirement to treat augmentation payments differently from the current treatment was only raised in August 2010 by the Audit Commission following the release of a technical guidance paper; after the majority of the audit had been completed. With the implementation of IFRS for financial year 2010/11 the confusion between whether the Local Authority SORP or Pensions SORP applies should be reduced. Officers will update the period end checklists to incorporate regular accounting for augmentation payments.
Review of Progress	The reconciliation of 2010/11 Augmentation payments to Pensions Group records has been implemented. This should facilitate easier calculation of the debtor for 2010/11.
Recommendation 4	
Monthly bank reconciliations should be reviewed and authorised.	
Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	Currently bank reconciliations are performed by a senior member of the pension team in Strategic Finance. A monthly review and authorisation of the reconciliations will be undertaken. At present, a vacancy remains within the Pensions team. This post will be responsible for carrying out bank reconciliations, once appointed.
Review of Progress	Bank reconciliations are completed on a monthly basis and are now routinely completed, reviewed and signed within 5 days of the period end. The Audit Commission are currently auditing the 2010/11 bank reconciliations.
Recommendation 5	
Formal risk management of the pension fund needs to be implemented and reviewed at least annually.	
Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	Agreed. Internal Audit and Risk Management will be a part of the overall review of the Pension Fund management arrangements undertaken by the Pension Fund Committee.
Review of Progress	Internal Audit and Risk Management are implementing arrangements to carry out this task.
Recommendation 6	
Journals should be subject to review and authorisation.	
Responsibility	Hilary Appleton
Priority	
Date	27th October 2010

Comments	A process for journal authorisation was introduced during the 2009/10 year end. Although this is occurring outside the Oracle system, officers recognise the merits of journal sign –off and have continued with this in the day-to-day accounting for the Pension Fund.
Review of Progress	Journals are reviewed by the Principal Accountant in Strategic Finance before being input into the financial system. This action has identified potential coding errors which have been corrected before entry to the accounts.

Recommendation 7

The Fund should work with AllianceBernstein to improve management information received from the fund manager and the custodian, both in-year and at the year-end.

Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	Agreed. The Investment Management Agreement with AllianceBernstein will be reviewed to ensure that all information required is received by the Pension Fund.
Review of Progress	Strategic Finance has contacted both the Fund Manager and the Custodian and this work is on-going.

Recommendation 8

SAS 70 reports should be obtained from all fund managers and custodians. These reports should be reviewed, and evidenced as reviewed, to ensure that they provide all of the assurances required.

Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	This task has been built into the period end checklist and Final Accounts timetable and reports will be reviewed in 2010/11.
Review of Progress	SAS 70 reports received from Fund Managers and Custodian will be reviewed to consider exceptions to compliance, and the review will be evidenced,

Recommendation 9

In-year controls should be introduced to verify the accuracy and completeness of the following items of income and expenditure.

- Transfer Values In.
- Transfer Values Out.
- Pensions payable.
- Pensions commutations and lump sums.

Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	Documented processes and controls will improve this area. The introduction of a consistent format of reconciliations at key points in the

	processes will be introduced across Strategic Finance, Pensions, Payroll, and Creditors
Review of Progress	Work in this area is on-going, greater narrative in both systems will be required to facilitate improvements in this area.

Recommendation 10	
The Fund should work with employers to reduce late payments.	
Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	It is our intention that the Pensions Manager write to each employer to remind them of their statutory duty and consequences of repeated failure to meet deadlines. A more pro-active process over the collection of employer contributions will reduce the likelihood of late payments.
Review of Progress	The Funding Strategy Statement covers the rules surrounding the timely receipt of Pension Contributions, the Pensions Manager will take appropriate action in cases of non-compliance,

Recommendation 11	
The Fund should introduce systems to verify the accuracy and completeness of contributions receivable from employers.	
Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	Agreed. This recommendation will be implemented
Review of Progress	The Funding Strategy Statement covers the rules surrounding the timely receipt of Pension Contributions, the Pensions Manager will take appropriate action in cases of non-compliance,

Recommendation 12	
Fund administration costs should be budgeted and reported to the Pension fund Committee.	
Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	Agreed, however the need to implement better control and assurance over the Pension Fund accounting and administration will be a priority in 2010/11. Officers intend to budget for administration and fund manager fees from financial year 2011/12.
Review of Progress	This recommendation has not been implemented, although it is intended that this will be done during 2011/12.

Recommendation 13	
The accounts should be reviewed prior to submission for audit to ensure they are fully SORP compliant.	

Responsibility	Hilary Appleton
Priority	
Date	27th October 2010
Comments	Agreed. This will be done using the disclosure checklists provided by the Audit Commission and ensure any SORP compliance issue raised in the Annual Governance Report is addressed in a timely manner. This task was built into the 2009/10 Final Accounts timetable and will remain in future timetables.
Review of Progress	This is part of the overall timetable for the Statement of Accounts for the County Council. The Pension Fund Accounts will be reviewed by the Audit Commission’s Technical Team for compliance with the Code of Practice.

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Pension Fund Committee

28th February 2011

Pension Fund Policy Documents – Funding Strategy Statement and Statement of Investment Principles

Report of Don McLure, Corporate Director Resources

Purpose of the Report

1 To inform Members of the review of the policy documents for the year ended 31st March 2011.

Background

2 The Local Government Pension Scheme (England and Wales) (Amendment) Regulations 2004 provide the statutory framework from which Local Government Pension Schemes (LGPS) administering authorities are required to have prepared a Funding Strategy Statement (FSS).

3 A copy of the FSS is attached at Appendix 1.

4 The key requirements for preparing the FSS can be summarised as follows:

- After consultation with all relevant interested parties involved with the Fund the Administering Authority will prepare and publish their funding strategy;
- In preparing the FSS, the Authority must have regard to :

  i. the guidance issued by CIPFA for this purpose; and
  ii. their own Statement of Investment Principles (SIP) for the Fund.
  iii. The FSS must be revised and published whenever there is a material change in either the policy on the matters set out in the FSS or the Statement of Investment Principles.

5 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 consolidate the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (the “Regulations”) which require administering authorities to prepare and review a written statement recording the investment policy of the Pension Fund – the ‘Statement of Investment Principles’ (SIP).

6 The 2009 regulations also require pension fund administering authorities to state the extent to which they comply with guidance given by the Secretary of State, previously the Chartered Institute of Public Finance (CIPFA) Pensions Panel Principles for Investment Decision Making in the Local Government Pension Scheme in the United Kingdom.

7 A copy of the SIP is attached at Appendix 2.

Review of the FSS and SIP

8 The FSS should be reviewed regularly and when there is a material change to the SIP. The FSS is the framework within which the Fund's actuary carries out triennial valuations to set contribution rates for individual scheme employer contribution rates. As the triennial valuation is due to be completed at 31st March 2011, no changes to the FSS are suggested at this time.

9 The 2009 Regulations required that the SIP containing the compliance statement was published by 1st July 2010 in line with the Regulations, and that it is reviewed and if necessary, revised from time to time, and in the case of any material change in the administering authority's policy on investments or their management.

10 The SIP has been reviewed and there have been no material changes since July 2010.

11 It is anticipated that review of the FSS and the SIP will be considered as part of the Review of the Pension Fund Arrangements.

Summary

12 Members are asked to note the contents of this report and the review of the Pension Fund's policy documents.

Background papers

(a) Pension Fund Committee - 25th October 2004 – Funding Strategy Statement

(b) Pension Fund Committee – 21st June 2010 – The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009

Contact: Hilary Appleton Tel: 0191 383 3544

Appendix 1

Durham County Council Pension Fund

Funding Strategy Statement

Version Updated 2005

Index

(A) STATUTORY BACKGROUND AND KEY ISSUES

1. The Local Government Pension Scheme (England and Wales) (Amendment) Regulations 2004 come into effect on 1st April 2004. They provide the statutory framework from which Local Government Pension Schemes (LGPS) administering authorities are required to prepare a Funding Strategy Statement (FSS) by 31 March 2005.

2. Key issues:

   - After consultation with relevant interested parties involved with the Fund, e.g. local authority employers, admitted bodies, scheduled/resolution bodies, the administering authority is required to prepare and publish their funding strategy.

   - In preparing the FSS, the administering authority has to have regard to:

     - CIPFA guidance
     - Its Statement of Investment Principles (SIP) published under Regulation 9A of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (as amended).

   - The first statement must be published by 31 March 2005.

   - The FSS must be revised and published whenever there is a material change in policy either on the matters set out in the FSS or the Statement of Investment Principles.

   - Each Fund Actuary must have regard to the FSS as part of the fund valuation process and the Fund Actuary has therefore been consulted on the contents of this FSS.

   - Benefits payable under the Scheme are secure, because they are guaranteed by statute. The FSS addresses the issue of managing the need to fund those benefits over the long term, whilst at the same time, allowing for scrutiny and accountability through improved transparency and disclosure.

   - The Scheme is a defined benefit final salary scheme. The benefits are specified in the governing legislation, the Local Government Pension Scheme Regulations 1997 (the Regulations). Constraints on the levels of employee contributions are also specified in the Regulations.

   - Employer contributions are determined in accordance with the Regulations, which require that an actuarial valuation is completed every three years by the Fund Actuary.

(B) PURPOSE OF THE FUNDING STRATEGY STATEMENT

3. The purpose of this Funding Strategy Statement (FSS) is:

- To establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward;

- To support the regulatory requirement to maintain as nearly constant employer contribution rates as possible; and

- To take a prudent longer-term view of funding those liabilities.

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

(C) AIMS AND PURPOSE OF THE PENSION FUND

4. The aims of the fund are to:

- **Enable employer contribution rates to be kept as nearly constant as possible and at reasonable cost to the taxpayers, scheduled, resolution and admitted bodies**

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

  - the regulatory requirement to secure solvency
  - the requirement to ensure that costs are reasonable, and
  - maximising return from investments

  In order to achieve nearly constant employer contribution rates there may be a need to invest in assets that match the employer's liabilities.

  The Administering Authority currently invests a large proportion of the Fund in equities, which are perceived as having higher long-term rates of return. These assets are more risky in nature than fixed interest investments, and this can lead to more volatile returns in the short-term.

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

There is a balance to be struck between the Fund's investment policy, actuarial smoothing adjustments and employer's contribution rates.

- **Manage employers' liabilities effectively**

  The Administering Authority seeks to manage employers' liabilities effectively. This is achieved by seeking actuarial advice and regular monitoring of the investment of the Fund's assets through quarterly meetings of the Pension Fund Committee.

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

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

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

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

  - Taking advice from its professional advisers, e.g. the Fund Actuary, Investment advisers and investment managers
  - Controlling levels of investment in asset classes through the Statement of Investment Principles
  - Restricting investment to asset classes recognised as appropriate for UK Pension Funds.

5. The purpose of the fund is to:

- Receive money in respect of contributions, transfer values and investment income, and

- Pay out money in respect of scheme benefits, transfer values, costs, charges and expenses,

as defined in the Local Government Pension Scheme Regulations and in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998.

(D) RESPONSIBILITIES OF THE KEY PARTIES

6. Although a number of parties including investment fund managers and external auditors have responsibilities to the fund, the following are considered to be of particular relevance:

7. The administering authority should:

- Collect employer and employee contributions

- Determine a schedule of due dates for the payment of contributions - Section 70(1)(a) of the Pensions Act 2004 suggests that Administering Authorities are now required to report breaches as defined in Section 70 (2) of the 2004 Act. This places monitoring of the date of receipt of employer contributions on the Administering Authority and therefore places a duty to report late payments of contributions to the Occupational Pensions Regulatory Authority (Opra).

- Take action to recover assets from admission bodies whose Admission Agreement has ceased.

- Invest surplus monies in accordance with the 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 effective communications with the Fund's Actuary to:

  - Ensure that the Fund Actuary is clear about the Funding Strategy;
  - Ensure reports are made available as required by guidance and regulation;
  - Agree timetables for the provision of information and valuation results;
  - Ensure provision of accurate data; and
  - Ensure that participating employers receive appropriate communications.

- Consider the appropriateness of interim valuations.

- Prepare and maintain an FSS and a SIP, both after proper consultation with interested parties, and

- Monitor all aspects of the fund's performance and funding and amend the FSS and SIP on an annual basis as part of the on-going monitoring process.

8. The individual employers should:

- Deduct contributions from employees' pay correctly.

- Pay all contributions, including their own as determined by the actuary, promptly by the due date.

- Exercise discretions within the regulatory framework.

- Make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits and early retirement strain, and

- Notify the administering authority promptly of all changes to membership, or as may be proposed, which affect future funding.

9. The fund actuary should:

- Prepare triennial valuations including the setting of employers' contribution rates after agreeing assumptions with the administering authority and having regard to the FSS

- Prepare advice and calculations in connection with bulk transfers and individual benefit-related matters.

- In response to a request from the Administering Authority, assess the impact of Regulatory changes on costs.

(E) SOLVENCY ISSUES AND TARGET FUNDING LEVELS

10. LGPS administering authorities prudentially seek to achieve full funding. The scheme regulations refer to each administering authority securing solvency by means of employer contribution rates established by mandatory valuation exercises and to the desirability of maintaining as nearly constant a rate as possible.

11. The LGPS however remains outside of the solvency arrangements established for private sector occupational pension schemes. It is not therefore unreasonable for administering authorities to establish longer-term recovery periods than those in the private sector where this is considered to be prudentially appropriate and relevant to local circumstances, and linked to the scheme's triennial valuation exercise requirements.

12. The Administering Authority will prudentially seek to secure the solvency of the Fund. Solvency is defined as being achieved when the value of the Fund's assets is greater than or equal to the value of the Fund's liabilities, as measured by the Fund's Actuary. Solvency is not defined in the Regulations, and its definition is therefore the Administering Authority's interpretation. Funding can be interpreted differently

depending on the assumptions used. The liabilities are measured on 'on-going' actuarial methods and assumptions where 'on-going' actuarial assumptions and methods are taken to be measurement by use of the projected unit method of valuation, using assumptions generally recognised as suitable for open, ongoing UK pension fund with a sponsoring employer of sound covenant.

13. The Administering Authority will agree with the Fund's Actuary the assumptions used in this calculation prior to each actuarial valuation.

14. The Administering Authority has agreed with the Fund Actuary that a market led approach should be used for future valuations at least for the foreseeable future. Under this method of valuation, the assets are taken into account at their mid market value and the value is then compared with the value of the Fund's liabilities calculated using consistent, market rates of interest. The Administering Authority has also agreed with the Fund Actuary that some element of smoothing of the assets can be used in the valuations. The size of the smoothing adjustment will be discussed at each valuation.

15. The rates of interest are obtained by examination of prevailing yields in the long term gilt market, which are then adjusted to make partial allowance for excess returns expected on other types of riskier investments such as equities. The risk of this approach is that the additional returns may not be achieved.

16. Where a valuation shows the Fund to be in surplus or deficit against the solvency measure, employer's contribution rates will be adjusted to reach the solvent position over a number of years. The 'recovery period' for reaching 'full' funding is set by the Administering Authority in consultation with the Actuary and the employer.

17. It is recognised that a large proportion of the Fund's liabilities are expected to arise as benefits payments over a long period of time. The Administering Authority is therefore prepared to agree recovery periods that are longer than the average future working lifetime of the membership of that employer. There is however a risk involved in relying on long recovery periods and the Administering Authority has agreed with the Actuary a maximum recovery period of 30 years. It is the intention of the Administering Authority to agree with employers a recovery period of as short a time as possible within this 30 year limit having regard to the affordability of the revised contribution rate in general taking into account the legislative requirements of securing solvency and maintaining as nearly a constant a contribution rate as possible. For each individual employer the following will also be taken into account:

- covenant and strength of any guarantee relating to an employer and hence the risk of default
- length of participation in the Fund
- whether the employer is closed to new entrants or is likely to have a contraction in its membership of the Fund

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

19. The Administering Authority will permit some employers to be treated as a group for the purposes of setting contribution rates. For smaller employers the contribution rate can be volatile due to the increased likelihood that demographic movements could have a material effect. The Administering Authority's policy is to consider the position carefully at each valuation and to notify each employer that is grouped that this is the case and which other employers it is grouped with. If the employer objects to this grouping, it will be offered its own contribution rate. The Administering Authority recognises that grouping can give rise to cross subsidies from one employer to another over time.

20. For employers whose participation is for a fixed period, grouping is unlikely to be permitted.

(F) LINKS TO INVESTMENT POLICY SET OUT IN THE STATEMENT OF INVESTMENT PRINCIPLES

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

General Principles and diversification

22. The Fund believes that the emphasis of investment over the long term should be on real assets, particularly equities and property. These are most likely to maximise the long term returns. The balance between UK and Overseas equities is, however, a matter of investment judgement. The Fund should also be diversified to include other real assets, such as Index-Linked and 'monetary' assets, such as Bonds and Cash.

23. The neutral benchmark proportions of the various asset classes have been determined by the Fund in consultation with the Investment Advisers and are reviewed at least once every three years to coincide with the Triennial Actuarial Valuation.

24. The active Investment managers are expected to adopt an active asset allocation policy to take advantage of the shorter term relative attractions of the various asset types.

25. The Administering Authority has produced this Funding Strategy Statement having taken a view on the level of risk inherent in the

investment policy set out in the Statement of Investment Principles (SIP) and the funding policy set out in this document.

26. The SIP sets out the investment responsibilities and policies relevant to the Fund.

27. The Administering Authority will continue to review both documents to ensure that the overall risk profile remains appropriate.

(G) IDENTIFICATION OF RISKS AND COUNTER-MEASURES

28. The Administering Authority seeks to identify all risks to the Fund, will monitor the risks and take appropriate action to limit the impact of them wherever possible.

For ease of classification some of the key risks may be identified as follows:

29. Financial

These include:

- Investment markets fail to perform in line with expectations
- Market yields move at variance with assumptions
- Investment fund managers fail to achieve performance targets over the longer term
- Asset reallocations in volatile markets may lock in past losses
- Pay and price inflation significantly more or less than anticipated
- The effect of a possible increase in employer's contribution rate on service delivery and admitted or scheduled bodies

30. Demographic

These include:

- The longevity horizon continues to expand
- Deteriorating pattern of early retirements

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

31. Regulatory

These include:

- Changes to regulations, e.g. more favourable benefits package, potential new entrants to the scheme, e.g. part-time employees

- Changes to national pension requirement and/or Inland Revenue rules

The Administering Authority will keep up to date with all proposed changes, and, if appropriate, request the Actuary to assess the impact on costs of the changes. The Administering Authority will notify employers of the likely impact of changes.

32. Governance

These include:

- Administering authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements)

- Administering authority not advised of an employer closing to new entrants

- An employer ceasing to exist with insufficient funding or adequacy of a bond

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

33. Solvency

These include:

- Allowing for future investment returns in excess of those available on government bonds introduces an element of risk, in that those additional returns may not materialise

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

34. Smoothing of Assets

These include:

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

The Administering Authority's policy is to review the impact of this adjustment at each valuation to ensure that it remains within acceptable limits.

35. Recovery Period

These include:

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

The Administering Authority's policy is to discuss the risks inherent in each situation with the Fund Actuary and to limit the permitted length of recovery period to no longer than 30 years.

36. Stepping

These include:

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

The Administering Authority's policy is to discuss the risks inherent in each situation with the Fund Actuary and to limit the number of permitted steps to three annual steps or, in exceptional circumstances, to six annual steps.

(H) MONITORING AND REVIEW

37. The FSS should be reviewed formally at least every three years and in advance of the triennial valuation cycle. The valuation exercise will establish contribution rates for all employers contributing to the fund for the following three years within the framework provided by the strategy.

Appendix 2

Pension Fund

Statement of Investment Principles

Version Updated June 2010

Table of Contents

1. Introduction

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 consolidate the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (the "Regulations") which require administering authorities to prepare and review a written statement recording the investment policy of the Pension Fund. The 2009 regulations also require pension fund administering authorities to state the extent to which they comply with guidance given by the Secretary of State, previously the Chartered Institute of Public Finance (CIPFA) Pensions Panel Principles for Investment Decision Making in the Local Government Pension Scheme in the United Kingdom. The compliance statement is attached at Appendix A.

Durham County Council is the administering authority (the "Authority") for the Durham County Council Pension Fund (the "Pension Fund") and the purpose of this document is to outline the broad investment principles governing the investment policy of the Pension Fund, thereby satisfying the requirements of the Regulations.

2. Investment Responsibilities

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

The Pension Fund Committee has full delegated authority to make investment decisions.

2.1 The Pension Fund Committee has responsibility for:

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

- Reviewing policy on social, environmental and ethical matters and on the exercise of rights, including voting rights; and
- Reviewing the resources allocated to investment managers on a regular basis.

2.2 The investment managers are responsible for:

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

2.3 The Global Custodian is responsible for:

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

2.4 The Independent Advisers are responsible for:

- Assisting the Corporate Director, Resources and Pension Fund Committee in determining the overall investment strategy, the strategic asset allocation and that the Pension Fund is invested in suitable types of investment, and ensuring that investments are sufficiently diversified.

- Assisting the Corporate Director, Resources and Pension Fund Committee in the preparation and review of Policy documents;
- Assisting the Corporate Director, Resources and Pension Fund Committee in their regular monitoring of the investment managers' performance;
- Assisting the Corporate Director, Resources and Pension Fund Committee in the selection and appointment of investment managers, custodians and Pension Fund Actuary;
- Advising and assisting the Corporate Director, Resources and the Pension Fund Committee on other investment related issues, which may arise from time to time; and
- Providing continuing education and training to the Pension Fund Committee.

2.5 The Actuary is responsible for:

- Providing advice as to the structure of the Pension Fund's liabilities, the maturity of the Pension Fund and its funding level in order to aid the Pension Fund Committee in balancing the short term and long-term objectives of the Pension Fund.
- Undertaking the statutory triennial valuation of the Fund's assets and liabilities.

2.6 The Corporate Director, Resources is responsible for:

- Ensuring compliance with this document and bringing breaches thereof to the attention of the Pension Fund Committee;
- Ensuring that this document is regularly reviewed and updated in accordance with the Regulations;
- Exercising delegated powers granted by the County Council to:
    - Administer the financial affairs in relation to the County Council's functions as a pension fund administering authority;

- Exercise those discretions under the Local Government Pension Scheme Regulations 1997 as appear from time to time in Pension Fund Statements of Policy; and
- Authorise, in cases of urgency, the taking of any action by an investment manager of the Pension Fund which is necessary to protect the interests of the Pension Fund.

- Managing the cash balances of the Pension Fund which the Investment Managers have not invested.

3. Authorised Investments

The powers and duties of the Authority to invest monies are set out in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 as amended from time to time and updated in 2009. The Authority is required to invest any money which is not required immediately to pay pensions and any other benefits and, in so doing, take account of the need for a suitable diversified portfolio of investments and the advice of persons properly qualified on investment matters.

3.1 Types of Investment

Investment can be made in accordance with the regulations in a broad spectrum of investments such as equities, fixed interest and other bonds, collective investment schemes, deposits, money market instruments, unquoted equities and property, both in the UK and overseas. The regulations also specify other investment instruments that may be used such as stock lending, financial futures, traded options, insurance contracts, sub underwriting contracts and a contribution to an unquoted limited liability securities investment partnership.

The limits on the amount of money that can be invested in each individual type of investment are specified in schedule 1 of the Regulations. We do not participate in stock lending or underwriting.

The Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 2003 amended the regulations so as to give Authorities the option to increase some of the limits on certain types of investments provided that the Authority complies with the requirements of the Regulations. These requirements include taking proper advice, the suitability of particular investments and types of investments, the limit on the amount of such investment, the reason for such investment and the period for which the increase in the limit of the type of investment will apply. Any increase in the limit must be kept under review.

The 2009 Regulations now prevent the administering authority from investing the Pension Fund’s cash that is not required immediately along with its own cash. The Pension Fund Committee has agreed that as part of its investment strategy it will allow the administering authority to invest, in the short term, on its behalf in line with the administering authority's Treasury Management Strategy.

Investment Managers are instructed to comply with the regulations in respect of the relevant portfolio subject to any specific instructions. The Authority is responsible for oversight of how compliance affects the compliance of the Pension Fund as a whole.

3.2 Investment Risk

The investment policy has been set with the objective of controlling the risk that the assets will not be sufficient to meet the liabilities of the Pension Fund while achieving a good return on investment.

Dividing the management of the assets between six investment managers, further controls risk. Asset allocation benchmarks have been set and performance is monitored relative to the benchmarks. This is to ensure the investment manager does not deviate from the Pension Fund Committee's investment strategy.

The setting of specific control ranges and other investment guidelines within which the investment managers must operate also controls risk.

The 2009 Regulations require the Pension Fund to describe how it measures and manages risk.

Risk is measured, in part, by the administering authority's risk management section as part of its assessment of the County Council's risks, and is reviewed as part of the independent Governance review undertaken by the Pension Fund.

3.3 Realisation of Investments

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

3.4 Approval has been given to investment as follows:

In-House Management

i. **Midland Enterprise Fund for the North East Exempt Unit Trust**

- Small, private and growing companies in the North East of England:
- £200,000 invested.

ii. Capital North East

- Start up and development capital for businesses in the North East:
- £400,000 invested, up to £500,000 may be invested.

External Investment Management

The Pension Fund Committee has appointed six investment managers to manage the remainder of the Pension Fund's assets. They have been appointed under the terms of the Regulations and their roles are described in the Investment Policy in Appendix B.

4. Allocation Strategy

Having considered advice from the Independent Advisers, and also having due regard for the objectives, the liabilities of the Pension Fund and the risks facing the Pension Fund, the Pension Fund Committee have decided upon the following strategic target asset allocation:

Asset Class	Permitted Assets	Benchmark & Performance Target	Proportion of Total Fund *
Conventional Bonds	Investment grade sterling bonds	FTSE Over 5 Year Index-Linked Gilt Index +0.5%	20%
Broad Bonds	Global bonds	UK 3-month LIBOR +3.0%	16%
UK Equity	UK equities	FTSE All Share Index +3.0%	20%
Global Equities	Global Equities	MSCI AC World Index +3.0%	28%
Dynamic Asset Allocation	All major asset classes with derivative overlay	UK 3-month LIBOR +4.0%	8%
Global Property	Global property	UK Retail Price Inflation +5.0%	8%

* Excluding in-house managed funds

More detailed definitions of the mandates are given at Appendix B.

The Pension Fund Committee and the Corporate Director, Resources, in conjunction with the Independent Advisers, will formally monitor the actual asset allocation of the Pension Fund on a quarterly basis.

5. Stock Selection

Individual investments are chosen by the Investment Managers with the Pension Fund Committee, Corporate Director, Resources and independent external advisers able to question the investment managers on their actions at each quarterly meeting.

6. Cash Management

The administering authority will invest the short term cash balances on behalf of the Pension Fund. This will be done in line with the administering authority's Treasury Management Policy and interest will be paid quarterly to the Pension Fund.

7. Investments Requiring Prior Approval

Subject to changes and agreements with Investment Managers, as included at Appendix B, a detailed report must be submitted to and approved by the Pension Fund Committee prior to making investments in the following:

- Private equity/Venture capital funds and enterprises
- Commodities
- Stock lending
- Currency Hedging - Agreed in principle, subject to prior consultation with the Corporate Director, Resources.

8. Socially Responsible Investing

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

9. Corporate Governance

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

10. Fee Structure

Investment Managers' fees are based on the value of assets under management. In the case of four investment managers, a performance related fee structure is in place based on a base fee plus a percentage of out-performance. In the case of the two remaining investment managers an ad-valorem fee is payable.

Independent Advisers' fees are based on a retainer for attendance at Pension Fund Committee and Annual Meetings and the provision of advice to the Pension Fund Committee. Fees for any additional work are based on a daily or hourly rate, as provided for by agreement or by separate arrangement.

Any additional work will be subject to a suitable fee arrangement or subject to separate tendering exercises.

The administering authority fee for Treasury Management will be based upon a percentage of the interest earned on the Pension Fund cash invested.

11. Reporting Requirements

The investment managers must report quarterly on matters covered in their individual agreements, but should include common items such as:

- Investment Managers' views on the UK or other relevant economies and the proposed asset allocation for the past, present and future quarter.
- Reports on any new investment policy issues requiring the approval of the Pension Fund Committee.
- Performance during the previous quarter, previous twelve months, three years and five years.
- A Portfolio valuation, including details of individual holdings.
- Investment transactions schedule for the previous quarter.
- Portfolio distribution and the changes in the markets - summarised by:
  - type of investment;
  - sector
  - geographic area as appropriate.
- Performance of any collective investment funds or internal pooled funds in which investments are held.
- Underwriting commitments relevant to the Portfolio.
- The cash position of the Pension Fund.
- Voting actions and forthcoming activity.
- Any material matters reported to the Financial Services Authority (FSA) in respect of the Portfolio or which reasonably might be brought to the attention of the Pension Fund Committee.
- Any material matters in respect of the interface with the Custodian.

- Investment or ancillary activities carried out in relation to the Portfolio where there arose a material risk of damage to the interests of the Pension Scheme or where a material risk of damage may arise in the future.
- Dealing errors and action taken.
- Any breach of confidentiality.
- Any breach of this Agreement.

Annually, the Global Custodian must present a detailed report relating to the individual investment managers’ fund performance and the combined fund performance.

Appendix A - Principles

This appendix sets out the extent to which Durham County Council as the Administering Authority of the Durham County Council Pension Fund complies with the ten principles of investment practice set out in the document published in April 2002 by CIPFA, the Chartered Institute of Public Finance and Accountancy, and called "CIPFA Pensions Panel Principles for Investment Decision Making in the Local Government Pension Scheme in the United Kingdom" (Guidance note issue No. 5), in future, compliance with guidance given by the Secretary of State will be reported.

Principle 1 — Effective decision-making

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

Principle 2 – Clear objectives

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

Principle 3 – Focus on asset allocation

Fully compliant: All major asset classes are considered. An asset liability modelling exercise is being considered as part of the ongoing review of the administration of the Pension Fund.

Principle 4 – Expert advice

Fully compliant: Two independent advisers were appointed in November 2004. Actuarial services have been subject to a separate open tender process.

Principle 5 – Explicit mandates

Fully compliant: Explicit written mandates agreed with all investment managers. Investment managers have been asked to report on transaction costs and commission.

Principle 6 – Activism

Partial compliance: Investment Managers are required to exercise voting rights on behalf of the Pension Fund when it is in the best interests of the Pension Fund. Normal practice is to allow the Investment Managers to follow their in-house voting policy unless otherwise instructed by the Pension Fund Committee. The mandates do not specifically incorporate the principle of the US Department of Labor Interpretative Bulletin on activism.

Principle 7 – Appropriate benchmark

Fully compliant: Appropriate benchmarks have been set in consultation with the independent advisers and the actuary.

Principle 8 – Performance measurement

Partial compliance: Performance of the Pension Fund is measured; separate monitoring of Pension Fund Committee performance and independent adviser performance has yet to be established.

Principle 9 – Transparency

Fully compliant: Investment objective and asset allocation strategy covered in the Funding Strategy Statement or Statement of Investment Principles. Investment Manager and independent adviser fee structures are included.

Principle 10 – Regular reporting

Fully Compliant: The Funding Strategy Statement including the Statement of Investment Principles is available on the internet and is included in the Pension Fund's Annual Report and Accounts. A summary of overall Pension Fund performance is reported to members of the Pension Fund annually.

Appendix B - Investment Managers

The Pension Fund Commitee has appointed six Investment Managers: Edinburgh Partners Limited (‘Edinburgh Partners’), BlackRock Investment Management (UK) Limited ('BlackRock'), AllianceBernstein Limited ('AllianceBernstein'), Royal London Asset Management ('RLAM'), CB Richard Ellis Collective Investors Limited (‘CBRE’) and Baring Asset Management Limited ('Barings') to manage the assets of the Pension Fund.

The long-term strategic allocation is as follows (the actual allocation may vary due to market movements):

Investment Manager	%	Asset Classes	Investment Style
Edinburgh Partners	28	Global Equities	Active
BlackRock	20	UK Equities	Active
AllianceBernstein	16	Global Bonds	Active
RLAM	20	Investment grade sterling bonds	Active
CBRE	8	Global Property	Active
Barings	8	Dynamic Asset Allocation – All major asset classes with derivative overlay	Active

The investment restrictions detailed in this Appendix form part of the contractual agreement with Investment Managers and will only be varied after consultation with the Investment Managers in accordance with their contracts.

The Investment Manager may hold cash up to the value of 5% of the market value of the portfolio in respect of which the Investment Manager has been appointed, subject to agreements with individual Investment Managers, who may require a different limit to invest their part of the Pension Scheme’s assets. Cash in excess of this value should be returned to Durham County Council as Administering Authority.

The mandates for each Investment Manager, subject to the overall requirements of the Regulations and this Statement of Investment Principles, are as follows:

Edinburgh Partners

The Pension Fund Committee has appointed Edinburgh Partners to manage a portfolio to be invested in Global Equities.

The Investment Manager's objective is to outperform the benchmark by 3% per annum net of fees over 3 year rolling basis.

The benchmark allocation is as follows:

Asset Class	Benchmark
Global Equities	MSCI AC World Index

Edinburgh Partners intend to invest in the following to achieve their objective:

Portfolio	%
EP Global Equity	100

Edinburgh Partners have a number of guidelines in place at the regional, sectoral and stock level when considering the control of risk within the portfolio. These are detailed below:

Sector	Range
Number of Stocks	Typically holding 30 to 50 stocks
Maximum holding in one stock	5% of the portfolio's value at time of investment. With market movement max. 7.5% before reduction in holding
Holding in cash	Typically not expected to exceed 5% of the portfolio's value following the initial investment process
Maximum holding in one sector	Diversified (e.g. Financials/Industrials) 40% Partially Diversified (e.g. Consumer Goods) 30% Homogeneous (e.g. Oil) 20%
Maximum holding in any one country	US, Japan, UK max 50% each Other developed markets max 20% each Emerging Market Country (as defined by MSCI Emerging Markets Index) max 10% each

There are limits on the holding of the following asset classes:

Asset Class	Maximum Holding
Collective Investment Schemes (CIS)	10% of the Portfolio or as otherwise advised in writing from time to time
CIS	No CIS sponsored by AllianceBernstein may be held
FM Funds (a sub-class of CIS)	10% of the portfolio or as otherwise advised from time to time
CIS of any one body (a sub-class of CIS)	10% of the Portfolio or as otherwise advised from time to time

BlackRock

The Pension Fund Committee has appointed BlackRock to manage a portfolio to be invested in UK Equities.

The Investment Manager's objective is to outperform the benchmark by 3% per annum net of fees over a rolling three year basis.

The benchmark allocation is as follows:

Asset Class	Benchmark
UK Equity	FTSE All-Share Index

BlackRock intend to invest in the following to achieve their objective:

Portfolio	%
UK Focus approach	100

While the BlackRock UK Focus Fund is unconstrained there are some guidelines within the investment process in respect of the portfolio. These guidelines are set out below:

Sector	Range
No. of stocks	Typically holding 15 to 30 stocks
Maximum holding in one stock	15% of the portfolio's value
Maximum holding in one sector	No maximum limit
Holding in cash	Typically not expected to exceed 2% to 5% of the fund value
Active risk	Expect the ex-ante tracking error (active risk) to fall within the range 5% pa to 11% pa.

There are limits on the holding of the following asset classes:

Asset Class	Maximum Holding
Collective Investment Schemes (CIS)	0% to10% of the Portfolio or as otherwise advised in writing from time to time

AllianceBernstein

The Pension Fund Committee has appointed AllianceBernstein to manage a portfolio to be invested in Global Bonds.

The Investment Manager's objective is to outperform the benchmark by 3% per annum net of fees over a rolling three year basis, with 5 – 10% volatility.

The benchmark allocation is as follows:

Asset Class	Benchmark
Broad Bonds	UK 3-month LIBOR

AllianceBernstein intend to invest in the following to achieve their objective:

Portfolio	%
Diversified Yield Plus Fund	100

AllianceBernstein can use a wide variety of financial instruments to generate returns within the portfolio.

AllianceBernstein intends to make use of financial derivative instruments and shall employ the Value-at-Risk (VaR) approach to measure risk associated with the use of such instruments. The Diversified Yield-Plus strategy employed by AllianceBernstein anticipates VaR exposure of less than or equal to 5%, as calculated by AllianceBernstein or its delegates.

VaR reports will be produced and monitored on a daily basis based on the following criteria:

- 1 month holding period
- 99% confidence level.

The limitations that apply to the investments are detailed below:

Sector	Range
High Yield	0% to 30%
Bank Loans	0% to 25%
Emerging Markets	0% to 20%
Foreign Exchange	0% to 30% gross,0% to 15% net
Sovereign	0% to 100%
MBS	0% to 40%
CMBS/ABS	0% to 30%
Investment-Grade Corporates	0% to 75%

Up to 100% of the Portfolio may be invested in Unit-linked Insurance Contracts issued by Associates of the Investment Manager. Direct investment in Collective Investment Schemes (CIS) is subject to prior approval.

RLAM

The Pension Fund Committee has appointed RLAM to manage a portfolio to be invested in Investment Grade Bonds.

The Investment Manager's objective is to outperform the benchmark by 0.5% per annum net of fees over a rolling three year basis.

The benchmark allocation is as follows:

Asset Class	Benchmark
Conventional Bonds	FTSE Over 5 Year Index-Linked Gilt Index

RLAM intend to invest in the following to achieve their objective:

Portfolio	%
Segregated – mainly index-linked securities with a specified range of +/- 2 years duration of the benchmark	100

RLAM can invest in a wide variety of bonds to generate returns within the Fund. The limitations to the extent of the investments in each classification are detailed below:

Bond classification	Range
UK Government Index Linked Bonds	50% to 100%
Overseas Government Index-Linked Bonds*	0% to 20%
UK Non-Government Index Linked Bonds	0% to 20%
UK Conventional Government Bonds	0% to 20%
UK Investment Grade Corporate Bonds (or equivalent)	0% to 20%
Overseas Conventional Bonds**	0% to 10%
Derivatives***	0%
Cash or cash equivalents (less than 1 year maturity)	0% to 10%

*Includes government and non-government bonds

**Includes government and corporate bonds and Currency hedged into sterling.

***Derivatives may only be used for the purpose of hedging currency risk.

There are limits on the holding of the following asset classes:

Asset Class	Maximum Holding
Collective Investment Schemes (CIS)	0% of the Portfolio or as otherwise advised in writing from time to time
Any single security excluding government bonds	Maximum of 5% of portfolio

CBRE

The Pension Fund Committee has appointed CBRE to manage a portfolio to be indirectly invested in Property. Investment will not be restricted to UK vehicles, but can be invested on at least a pan-European basis.

The Investment Manager's objective is to outperform the benchmark by 5% per annum net of fees to be achieved over a five year time horizon.

The benchmark allocation is as follows:

Asset Class	Benchmark
Global Property	UK Retail Price Inflation

CBRE intend to invest in the following to achieve their objective:

Portfolio	%
CB Richard Ellis RPI +5%	100

There are limitations that apply with the construction of the CBRE portfolio. They are as follows:

Restrictions	Range
Collective Investment Schemes (CIS)	0% to 50% until notified in writing and thereafter 0% to 100%
Maximum allocation to any single fund	0% to 15%
Maximum allocation to listed investments	0% to 30%
Maximum allocation to any single country (including the UK)	0% to 25%
Maximum regional allocations -	
Asia Pacific Region	0% to 40%
North American Region	0% to 40%
Other Regions (excluding Europe)	0% to 10%

In the case of Collective Investment Schemes (CIS) taken on at the Effective Date, the requirement shall be that the Investment Manager liquidate these assets at a time that is appropriate in the reasonable opinion of the Investment Manager. There is no long stop date on this process.

Baring Asset Management

The Pension Fund Committee has appointed Barings to manage a portfolio to be invested in a fully diversified Global portfolio. It is expected that target return will be delivered using dynamic asset allocation over the market cycle incorporating the full range of global investment opportunities.

The Investment Manager's objective is to outperform the benchmark by 4% per annum net of fees over a rolling three year basis, with 5 – 10% volatility.

The benchmark allocation is as follows:

Asset Class	Benchmark
DAA	UK 3-month LIBOR

Barings intend to invest in the following to achieve their objective:

Portfolio	%
Extended Risk Solutions	100

Barings can use a wide variety of asset classes to generate returns within the Fund.

The expected volatility arising from the asset distribution over the medium term is 7% to 11% per annum as represented by standard deviations of monthly returns annualised. Value at Risk (VaR) limit of 5% per 10 days with a 99% confidence level based on three years of data.

The limitations to the extent of the investments in each classification are detailed overleaf:

Asset Class	Range
Equities (segregated and/ or pooled)* and depositary receipts, warrants and P-Notes	0% to 65%
Commodities* in the form of ETFs, CIS' and Index Futures.	0% to 30%
Bonds	0% to 80%
Investment-Grade Corporate Bonds	0% to 50%
High Yield Debt** being all corporate and government sub-investment grade debt securities.	0% to 15%
Emerging Market Debt** being all government debt securities issued by countries falling within the World Bank definition of a developing market country (or similar) at the time of acquisition.	0% to 15%
Property in the form of REITs and CIS'	0% to 30%
Hedge Funds/Structured Products/Private Equity	0% to 50%
Foreign Exchange including Forwards	0% to 40%
Cash/Near Cash	0% to 25%

* Equities and Commodities, aggregate maximum 80%

** High Yield and Emerging Market Debt, aggregate maximum 20%

There are limits on the holding of the following asset classes:

Asset Class	Maximum Holding
Collective Investment Schemes (CIS)	50% of the Portfolio or as otherwise advised in writing from time to time
CIS	No CIS sponsored by AllianceBernstein, titled Diversified Yield Bond Plus Fund, may be held.
FM Funds (a subclass of CIS)	50% of the Portfolio or as otherwise advised in writing from time to time.
CIS of any one body (a subclass of CIS)	50% of the Portfolio or as otherwise advised in writing from time to time.

Note: Allocations to other bond assets such as mortgage backed securities or asset backed securities and bank loans as well as foreign currency exposure are also permitted.

The Pension Fund Committee will allow the Investment Manager to exercise Long/Short strategies; however there will be no net short positions permissable in any asset class.

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By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

Agenda Item 12

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Agenda Item 16

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