

Essex Pension Fund's draft financial statements for 2010/11

Pension Fund Accounts

Introduction

The Pension Fund accounts, and accompanying notes, summarise the financial transactions and net assets related to the provision of pensions and other benefits payable to former employees of the Council, Essex district, borough and unitary councils, and for other scheduled and admitted bodies. The Pension Fund accounts are set out in the following pages, as detailed below.

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Fund account for the year ended 31 March 2011

| 2008/09 £000 | 2009/10 £000 | Note | | 2010/11 £000 | £000 |
|--------------------|--------------------|------|---|-----------------|--------------------|
| | | | Contributions and Benefits | | |
| | | | Income | | |
| | | | Contributions receivable | | |
| (47,271) | (49,558) | 5 | Member contributions | (50,353) | |
| (163,956) | (154,488) | 5 | Employers' contributions | (173,106) | |
| (22,358) | (25,264) | 5 | Transfers in from other Pension Funds | (27,683) | |
| (192) | (201) | | Other income | (169) | |
| <u>(233,777)</u> | <u>(229,511)</u> | | Total income | | (251,311) |
| | | | Expenditure | | |
| | | | Benefits payable | | |
| 115,672 | 125,384 | 5 | Pensions | 130,775 | |
| 32,020 | 31,826 | | Commutation of pensions & lump sum retirement benefits | 43,229 | |
| 3,510 | 3,986 | | Lump sum death benefits | 3,338 | |
| | | | Payments to and on account of Leavers | | |
| 6 | 14 | | Refunds of contributions | 15 | |
| 6 | 5 | | State scheme premiums | - | |
| 13,701 | 16,141 | 5 | Transfers out to other schemes | 17,246 | |
| 1,812 | 1,869 | 7 | Administration expenses | 1,816 | |
| <u>166,727</u> | <u>179,225</u> | | Total expenditure | | 196,419 |
| (67,050) | (50,286) | | Net additions from dealings with members | | (54,892) |
| | | | Returns on investments | | |
| (69,956) | (46,999) | 6 | Investment income | (48,977) | |
| 822,540 | (778,921) | 9 | Profit and losses on disposal of investments and changes in market value of investments | (241,068) | |
| 3,340 | 2,512 | | Taxes on income | 2,134 | |
| 13,687 | 13,627 | 8 | Investment management expenses | 13,560 | |
| <u>769,611</u> | <u>(809,781)</u> | | Net returns on investments | | (274,351) |
| 702,561 | (860,067) | | Net (increase)/decrease in the assets available for benefits during the year | | (329,243) |
| (2,927,368) | (2,224,807) | | Net assets as at 1 April | | (3,084,874) |
| <u>(2,224,807)</u> | <u>(3,084,874)</u> | | Net assets as at 31 March | | <u>(3,414,117)</u> |

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Net assets statement as at 31 March 2011

| 31 March 2009 £000 | 31 March 2010 £000 | Note | | 31 March 2011 £000 | £000 |
|-----------------------|-----------------------|-----------|--|-----------------------|------------------|
| | | 9 | Investments at market value | | |
| | | | Investment assets | | |
| 149,665 | 217,771 | | Fixed interest securities | 226,019 | |
| 1,348,654 | 1,905,749 | | Equities | 2,118,859 | |
| 72,068 | 172,895 | | Index linked securities | 171,839 | |
| 120,822 | 186,281 | | Property unit trusts | 234,688 | |
| 325,981 | 381,123 | | Managed funds | 406,925 | |
| 4,996 | 1,631 | | Derivative Contracts | 22 | |
| 83,165 | 117,700 | | Property | 147,520 | |
| 103,882 | 92,716 | | Cash/deposits | 76,737 | |
| 15,479 | 24,408 | | Other investment balances | 13,347 | |
| <u>2,224,712</u> | <u>3,100,274</u> | | | | 3,395,956 |
| | | | Investment liabilities | | |
| (38,908) | (28,896) | | Derivative Contracts | (3,060) | |
| (4,003) | (4,787) | | Other investment balances | (9,429) | |
| <u>(42,911)</u> | <u>(33,683)</u> | | | | (12,489) |
| <u>2,181,801</u> | <u>3,066,591</u> | | Total Investments | | <u>3,383,467</u> |
| | | 11 | Current assets and liabilities | | |
| | | | Current Assets | | |
| 14,413 | 5,065 | | Cash | | 13,150 |
| 32,151 | 19,337 | | Contributions due from employers and other current assets | | 31,174 |
| <u>46,564</u> | <u>3,090,993</u> | | | | <u>3,427,791</u> |
| | | | Current liabilities | | |
| (3,558) | (6,119) | | Unpaid benefits and other current liabilities | | (13,674) |
| <u>2,224,807</u> | <u>3,084,874</u> | | Net assets of the scheme available to fund benefits | | <u>3,414,117</u> |

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Notes to the Pension Fund Accounts

1. Background

Under the Local Government Pension Scheme (LGPS) (Administration) Regulations 2008, Essex County Council is required to maintain a pension fund (the Fund) for its employees and those of other scheduled Bodies within its area. The Fund is also empowered to admit the employees of certain other bodies, town and parish councils, educational establishments, contractors providing services transferred from scheduled bodies and community interest bodies. As a result the Fund now contains around 420 employing bodies. A complete list of the employers participating in the Fund is contained in the Pension Fund Annual Report & Accounts. The Fund does not provide pensions for teachers, for whom separate arrangements exist. Uniformed police and fire staff are also subject to separate pension arrangements.

Independent investment managers have been appointed to manage the investments of the Fund. The Fund also invests in private equity infrastructure and shareholder activism through the use of limited partnerships. The Investment Steering Committee (ISC) oversees the management of these investments and meets regularly with the investment managers to monitor their performance against agreed benchmarks. The ISC in turn reports to the Essex Pension Fund Board. The Fund's Statement of Investment Principles is contained in the Pension Fund Annual Report & Accounts.

2. Basis of preparation

The Pension Fund Statement of Accounts has been prepared in accordance with the Code of Practice on Local Authority Accounting for England 2010/11 issued by CIPFA, and the main recommendations of the Statement of Recommended Practice (SORP): 'Financial Reports of Pension Schemes' (Revised May 2007). This is the first year of preparation that the Code has incorporated the requirement of the International Requirement Financial Standards (IRFS).

The Pension Fund publishes a number of statutory documents, including a Statement of Investment Principles, a Funding Strategy Statement and Statements of Compliance. Copies can be obtained by contacting the Council's Investments team or alternatively are available from www.essexpensionfund.co.uk.

The Pension Fund Statement of Accounts summarises the transactions of the scheme and the net assets of the Fund. The accounts do not reflect obligations to pay pensions and benefits that fall due after the financial year. However, for the first time, a statement calculating the Fund's promised retirement benefits as at 31 March 2010 using IAS19 methodology is included in the notes to the accounts and can be found at Note 3.3.

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3. Actuarial valuation

The contributions payable for 2010/11 were determined by the 2007 Actuarial Valuation.

3.1 Actuarial valuation 2007

The market value of the assets as at the 2007 actuarial valuation was **£3,043m**. The assets of the Fund were valued on the market value approach and showed that the assets held were sufficient to cover **79.6%** of the Fund's liabilities at that time. The valuation was carried out using the projected unit method.

The main economic assumptions used in the actuarial valuation were:

| | Past service liabilities % per annum | Future service liabilities % per annum |
|---|---|---|
| Rate of return on investments | | |
| Pre retirement | 6.90% | 6.50% |
| Post retirement | 5.40% | 6.50% |
| Rate of pay increases | 4.60% | 4.25% |
| Rate of increase to pensions in payment | 3.10% | 2.75% |

The actuary has set a common contribution rate of **12.7%** of pensionable pay. This rate is varied for each participating body depending on their individual circumstances. In addition, a past service deficiency contribution of **7.0%** has been set to enable the Fund to reach 100% funding in 20 years from the date of the last actuarial valuation. This rate and recovery period are also varied for individual employers, to reflect their individual circumstances. The report of the actuary can be found in the Pension Fund Annual Report & Accounts.

3.2 Actuarial Valuation 2010

An actuarial valuation of the Essex Pension Fund was carried out as at 31 March 2010 to determine the contribution rates with effect from 1 April 2011 to 31 March 2014. The results of the valuation are contained within the Statement by the Consulting Actuary of the Pension Fund Report and Accounts.

On the basis of the assumptions adopted, the valuation revealed that the value of the Fund's assets of **£3,085m** represented **71%** of the Funding Target liabilities of **£4,319m** at the valuation date. The valuation also showed that a common rate of contribution of **12.2%** of Pensionable Pay per annum was required from employers. The common rate is calculated as

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being sufficient, together with contributions paid by members, to meet all liabilities arising in respect of service after the valuation date.

Adopting the same method and assumptions as used for assessing the Funding Target the deficit could be eliminated by an average additional contribution rate of **9.2%** of Pensionable Pay for 20 years. This would imply an average employer contribution rate of **21.4%** of Pensionable Pay in total.

In practice, each individual employer's position is assessed separately and the contributions required are set out in the Actuary's statement. In addition to the certified contributions, payments to cover additional liabilities arising from early retirements (other than ill-health retirements) will be made to the Fund by the employers.

The funding plan adopted in assessing the contributions for each individual employer is in accordance with the Funding Strategy Statement (FSS). Different approaches adopted in implementing contribution increases and deficit recovery periods are as determined through the FSS consultation process.

The valuation was carried out using the projected unit actuarial method. Full details of the actuarial assumptions are contained within the full valuation report that is available from www.essexpensionfund.co.uk, but the main financial assumptions used for assessing the Funding Target and the common contribution rate were as follows:

| | For past service liabilities (Funding Target) | For future service liabilities (Common Contribution Rate) |
|---|--|--|
| Rate of discount: | | |
| ▪ pre retirement | 7.0% per annum | 6.75% per annum |
| ▪ post retirement | 5.5% per annum | 6.75% per annum |
| Rate of pay increases | 4.5% per annum | 4.5% per annum |
| Rate of increases in pensions in payment (in excess of Guaranteed Minimum Pension): | 3.0% per annum | 3.0% per annum |

The assets were assessed at market value.

The next triennial actuarial valuation of the Fund is due as at 31 March 2013. Based on the results of this valuation, the contributions payable by the individual employers will be revised with effect from 1 April 2014.

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3.3 Actuarial present value of promised retirement benefits

IAS 26 requires the present value of the Fund's promised retirement benefits to be disclosed, and for this purpose the actuarial assumptions and methodology used should be based on IAS 19 rather than the assumptions and methodology used for funding purposes.

In order to assess the value of the benefits on this basis, the Actuary has used the same actuarial assumptions as those used for funding purposes, other than the discount rate where we have used a rate of 5.6% per annum both before and after retirement, rather than the rates as outlined above. The Actuary has also used valuation methodology in connection with ill-health and death benefits which is consistent with IAS 19. On this basis, the value of the Fund's promised retirement benefits as at 31 March 2010 was **£4,720m**.

Similar calculations were carried out as at the previous actuarial valuation date of 31 March 2007, using the same actuarial assumptions as those used for funding purposes at that date, other than the discount rate where a rate of 5.4% per annum both before and after retirement was used. On this basis, the value, for IAS 26 purposes, of the Fund's promised retirement benefits at that date was **£4,213m**.

4. Accounting policies

4.1 Accounting convention

The Pension Fund Statement of Accounts has been prepared on an accruals basis, except for transfers to and from the scheme which are accounted for on a cash basis.

4.2 Investments

In the majority of cases, equity investments are valued at the last traded price recorded on the Stock Exchange Electronic Trading Service or bid market price at 31 March 2011.

For unquoted equity in the private equity limited partnerships, there is usually a time delay in receiving information from the private equity fund managers. The valuations shown in the net asset statement for these investments are the latest valuations provided to the County Council. In general these are valuations at 31 March 2011 and are compiled in accordance with the guidelines issued by the British Venture Capital Association or an equivalent body. In a limited number of cases, an estimate of the valuation as at 31 March 2011 has been made. To estimate the valuation at 31 March 2011, the Fund amends the 31 December 2010 valuation for payments made to and payments received from the private equity managers in the period 1 January 2010 to 31 March 2011.

Unit Trusts and managed funds are valued at the bid prices provided by the relevant fund managers, which reflect the market value of the underlying investments.

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The value of fixed interest investments in the Fund's investment portfolio excludes interest earned but not paid over at the Fund year end, which is included separately within accrued investment income (as disclosed in Note 9).

Futures are valued at the closing market price published by the relevant futures exchange (eg. London International Financial Futures Exchange).

Forward foreign exchange contracts outstanding at year end are stated at fair value, which is determined as the loss or gain that would arise if the outstanding contract was required to be settled on 31st March.

Direct property investments have been valued, at open market value, at 31 March 2011, by Jones Lang LaSalle, Chartered Surveyors.

Acquisition costs are included in the purchase cost of investments.

4.3 Investment income

Investment income is taken into account where dividends have been declared at the end of the financial year. Investment income also includes withholding tax where this cannot be recovered. The amount of irrecoverable withholding tax is disclosed as a separate line item on the face of the fund account.

Income from fixed interest and index linked securities, cash and short-term deposits is accounted for on an accruals basis.

Income from other investments is accounted for on an accruals basis.

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

4.4 Foreign currencies

Transactions in foreign currencies are taken into account at the ruling rate of exchange at the time of the transaction. In the financial statements, balances are recorded at rates ruling on 31 March 2011.

4.5 Contributions

Normal contributions, both from the members and from employers, are accounted for in the payroll month to which they relate at rates as specified in the rates and adjustments certificate. Additional contributions from employers are accounted for when received.

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4.6 Benefits payable

Under the rules of the Fund, retirees receive a lump sum retirement grant in addition to their annual pension. Lump sum retirement grants are accounted for from the date of retirement. Where a member can choose whether to take a greater retirement grant in return for reduced pension these lump sums are accounted for on an accruals basis from the date that the option is exercised. Other benefits are accounted for on the date the member leaves the Fund or on death.

4.7 Transfers to / from other schemes

Transfer values are normally accounted for on a payment/receipts basis since not only do they frequently apply to several past years but, in the case of transfer values due, information is not available at the year end on which to make an accrual.

4.8 Administrative and other expenses

Administration and investment management expenses are accounted for on an accruals basis. Expenses are recognised net of any recoverable VAT. A proportion of relevant officers' salaries have been charged to the Fund on the basis of time spent on investment related matters and pension administration.

5. Membership activities

5.1 Membership

| 31 March 2009 | 31 March 2010 | | 31 March 2011 (Provisional) |
|------------------|------------------|---------------------|-----------------------------------|
| 46,857 | 43,728 | Contributors | 43,636 |
| 26,272 | 32,173 | Deferred pensioners | 34,737 |
| 27,992 | 29,165 | Pensioners | 30,764 |

Deferred pensioners are former employees who have chosen not to transfer their pension rights.

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5.2 Pension benefits payable

| 2008/09 £000 | 2009/10 £000 | | 2010/11 £000 |
|-----------------|-----------------|--------------------------------|-----------------|
| 44,551 | 47,629 | County Council | 49,311 |
| 51,539 | 55,122 | District / unitary authorities | 56,718 |
| 9,944 | 11,588 | Other scheduled bodies | 11,547 |
| 9,638 | 11,045 | Other admitted bodies | 13,199 |
| <u>115,672</u> | <u>125,384</u> | | <u>130,775</u> |

5.3 Contributions receivable

Contributions receivable from employers are set out below:

| 2008/09 £000 | 2009/10 £000 | | 2010/11 £000 |
|-----------------|-----------------|--------------|-----------------|
| 88,097 | 94,680 | Normal | 96,103 |
| 145 | 105 | Augmentation | 16 |
| 69,731 | 55,390 | Deficit | 71,482 |
| 5,983 | 4,313 | Other | 5,505 |
| <u>163,956</u> | <u>154,488</u> | | <u>173,106</u> |

Other employers' contributions relate to payments for the cost of early retirements.

| 2008/09 | | 2009/10 | | | 2010/11 | |
|----------------|------------------|----------------|------------------|--------------------------------|----------------|------------------|
| Member £000 | Employer £000 | Member £000 | Employer £000 | | Member £000 | Employer £000 |
| 16,315 | 51,634 | 17,167 | 53,130 | County Council | 16,473 | 55,855 |
| 14,588 | 52,860 | 15,020 | 54,742 | District / unitary authorities | 14,940 | 55,387 |
| 12,272 | 31,131 | 12,886 | 33,969 | Other scheduled bodies | 12,564 | 31,739 |
| 4,096 | 28,331 | 4,485 | 12,647 | Other admitted bodies | 6,376 | 30,125 |
| <u>47,271</u> | <u>163,956</u> | <u>49,558</u> | <u>154,488</u> | | <u>50,353</u> | <u>173,106</u> |

During 2010/11 lump sum contributions in respect of the Actuarial deficit were received from the Essex Probation of **£0.100m** and an accrual in respect of the Essex Magistrates Court Committee **£12.556m**.

During 2009/10 no lump sum employer contributions in respect of actuarial deficit were received.

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During 2008/09 lump sum contributions in respect of the Actuarial deficit were received from Chelmsford Borough Council **£1.419m**, CCETSW **£16.235m** and SCIE **£0.265m**. These amounts were paid following the 31st March 2007 Actuarial Valuation and, in accordance with the Pension SORP, have been recognised on receipt.

5.4 Transfers in from other pension funds

During 2010/11 **£0.700m** was received from Suffolk County Council, Ipswich Museum and **£0.005m** was received from Metropolitan Police Superannuation Scheme. There were no amounts received in respect of group transfers from other schemes during 2009/10 or 2008/09.

5.5 Transfers out to other schemes

No amounts were payable in respect of group transfers to other schemes during 2010/11. During 2009/10 **£1.249m** was paid out to HPSS and a further **£0.436m** was paid to Tayside Council as a result of the termination of fund membership of the Central Council for the Education and Training of Social Workers. No amounts were payable in respect of group transfers to other schemes during 2008/09.

6. Investment income

| 2008/09 £000 | 2009/10 £000 | | 2010/11 £000 |
|-----------------|-----------------|---------------------------------------|-----------------|
| 5,021 | 2,325 | Income from fixed interest securities | - |
| 42,872 | 26,492 | Dividends from equities | 30,142 |
| 416 | 3,677 | Income from index linked securities | 3,156 |
| 7,396 | 7,904 | Net rent from properties | 9,235 |
| 12,892 | 5,295 | Interest from cash deposits | 5,728 |
| 1,359 | 1,306 | Other | 716 |
| 69,956 | 46,999 | Total | 48,977 |

7. Administrative expenses

| 2008/09 £000 | 2009/10 £000 | | 2010/11 £000 |
|-----------------|-----------------|-----------------------------------|-----------------|
| 1,491 | 1,485 | Administration and Processing | 1,332 |
| 128 | 175 | Actuarial Fees | 413 |
| 193 | 209 | Legal and other Professional Fees | 71 |
| 1,812 | 1,869 | | 1,816 |

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The administration and processing expenses represent a proportion of relevant officers' salaries on the basis of time spent on pensions' administration and investment matters.

8. Investment expenses

| 2008/09 £000 | 2009/10 £000 | | 2010/11 £000 |
|-----------------|-----------------|--|-----------------|
| 13,266 | 13,228 | Administration, Management and custody | 13,127 |
| 89 | 55 | Performance Measurement Services | 54 |
| 332 | 344 | Other Advisory Services | 379 |
| <u>13,687</u> | <u>13,627</u> | Total | <u>13,560</u> |

9. Investments

9.1 Investments held by managers

The value of investments held by each manager together with investments in private equity, infrastructure, financing and shareholder activism partnerships on 31 March was as follows:

| 2009 | | 2010 | | | 2011 | |
|--------------|--------------|--------------|--------------|--|--------------|--------------|
| £m | % | £m | % | | £m | % |
| 146 | 6.7 | 224 | 7.3 | Alliance Bernstein | 234 | 6.9 |
| 271 | 12.4 | 357 | 11.6 | Aviva Investors | 396 | 11.7 |
| 160 | 7.3 | 248 | 8.1 | Baillie Gifford and Co | 293 | 8.7 |
| 218 | 10.0 | 1 | - | Capital International | - | - |
| - | - | 224 | 7.3 | FIL Pensions Management | 244 | 7.2 |
| 97 | 4.5 | 154 | 5.0 | First State Investments (UK) Ltd | 180 | 5.3 |
| 133 | 6.1 | 161 | 5.2 | Goldman Sachs Asset Management International | 169 | 5.0 |
| 711 | 32.6 | 1,051 | 34.3 | Legal and General Investment Management | 1,137 | 33.6 |
| 146 | 6.7 | 245 | 8.0 | Marathon Asset Management Ltd | 282 | 8.3 |
| - | - | - | - | Martin Currie Investment Management Ltd | - | - |
| 14 | 0.6 | 24 | 0.8 | Mellon Capital Management | 30 | 0.9 |
| - | - | - | - | Mirabaud Investment Management Ltd | - | - |
| - | - | - | - | Nomura Asset Management UK Ltd | - | - |
| 111 | 5.1 | 137 | 4.5 | M&G Investments Alpha Opportunities | 144 | 4.3 |
| 48 | 2.2 | 46 | 1.5 | M&G Investments Infracapital | 54 | 1.6 |
| - | - | - | - | M&G Investments Financing Fund | 7 | 0.2 |
| - | - | - | - | Partners Group Management II S.à r.l | 12 | 0.4 |
| 65 | 3.0 | 112 | 3.7 | Private Equity | 168 | 5.0 |
| (9) | -0.4 | 33 | 1.1 | Record Currency Management | 28 | 0.8 |
| 71 | 3.2 | 49 | 1.6 | Shareholder activism | 5 | 0.1 |
| <u>2,182</u> | <u>100.0</u> | <u>3,066</u> | <u>100.0</u> | | <u>3,383</u> | <u>100.0</u> |

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9.2 Movement in the market value of investments

The table below shows the movement in the market value of the investments held during the financial year, including profits and losses realised on the sales of investments since 1 April.

| | Value at 1 April 2009 | Value at 1 April 2010 | 2010/11 Movement | | | | Value at 31 March 2011 |
|---|--------------------------|--------------------------|--|--------------------------|--------------------------------------|--------------------------|---------------------------|
| | £000 | £000 | Purchases plus net transfers £000 | Sale Proceeds £000 | Change in Market Value £000 | Cash Movement £000 | £000 |
| Fixed interest | 149,665 | 217,771 | 3,656 | (6,146) | 10,738 | - | 226,019 |
| Equities | | | | | | | |
| UK | 237,351 | 329,583 | 31,214 | (43,941) | 27,089 | - | 343,945 |
| Overseas | 1,111,303 | 1,576,166 | 430,103 | (387,859) | 156,504 | - | 1,774,914 |
| Index Linked | 72,068 | 172,895 | 13,996 | (24,701) | 9,649 | - | 171,839 |
| Managed & Unitised | | | | | | | |
| PUTS | 120,822 | 186,281 | 49,838 | (9,396) | 7,965 | - | 234,688 |
| Other | 325,981 | 381,123 | 69,063 | (64,461) | 21,200 | - | 406,925 |
| Derivative Contracts | (1,905) | 21 | - | - | 1 | - | 22 |
| Properties | 83,165 | 117,700 | 24,072 | - | 5,748 | - | 147,520 |
| Cash Deposits | 101,600 | 92,557 | 33,000 | (2,168) | 2,168 | (48,985) | 76,572 |
| Margin Account | 2,282 | 159 | - | (6) | 6 | 6 | 165 |
| | 2,202,332 | 3,074,256 | 654,942 | (538,678) | 241,068 | (48,979) | 3,382,609 |
| Debtors - outstanding sales | 7,978 | 18,687 | | | | | 8,082 |
| Creditors - outstanding purchases | (3,838) | (4,609) | | | | | (9,281) |
| Investment income debtors | 7,501 | 5,721 | | | | | 5,265 |
| Investment income creditors | (165) | (178) | | | | | (148) |
| Derivative Contracts pending fx debtors | 1,804 | 1,610 | | | | | - |
| Derivative Contracts pending fx creditors | (33,811) | (28,896) | | | | | (3,060) |
| | 2,181,801 | 3,066,591 | | | | | 3,383,467 |

For 2010/11, the total transaction costs were **£1.2m** (2009/10: £2.0m and 2008/09: £1.9m).

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9.3 Analysis of investment assets

An analysis of investment assets at 31 March is shown below.

| 2009 £000 | 2010 £000 | | 2011 £000 |
|------------------|------------------|-----------------------------------|------------------|
| | | Fixed interest securities | |
| 63,278 | 57,037 | UK public sector quoted | 57,344 |
| 42,409 | 160,734 | UK quoted | 168,675 |
| 267 | - | Overseas public sector | - |
| 43,711 | - | Overseas quoted | - |
| | | Equities | |
| 57,807 | 78,128 | UK quoted | 71,609 |
| 684,967 | 993,734 | Overseas quoted | 1,135,418 |
| 179,544 | 251,455 | UK unit trusts | 272,336 |
| 426,336 | 582,432 | Overseas unit trusts | 639,496 |
| | | Index linked securities | |
| 72,068 | 172,895 | UK public sector quoted | 171,839 |
| | | Managed funds | |
| 171,542 | 195,008 | UK unquoted | 206,455 |
| 115,616 | 128,758 | Overseas quoted | 142,129 |
| 38,823 | 57,357 | Active currency | 58,341 |
| | | Derivative Contracts | |
| 4,996 | 1,631 | Derivative Assets | 22 |
| (38,908) | (28,896) | Derivative Liabilities | (3,060) |
| | | Property | |
| 21,950 | 27,650 | UK properties (leasehold) | 27,445 |
| 61,215 | 90,050 | UK properties (freehold) | 120,075 |
| 120,822 | 186,281 | Property unit trusts | 234,688 |
| | | Cash deposits | |
| 84,484 | 80,875 | Sterling | 40,393 |
| 17,116 | 11,682 | Foreign currency | 36,179 |
| 2,282 | 159 | Margin accounts | 165 |
| | | Investment accruals | |
| 7,978 | 18,687 | Debtors - outstanding sales | 8,082 |
| (3,838) | (4,609) | Creditors - outstanding purchases | (9,281) |
| 7,501 | 5,721 | Income accrual - Debtor | 5,265 |
| (165) | (178) | Income accrual - Creditor | (148) |
| 2,181,801 | 3,066,591 | Value at 31 March | 3,383,467 |

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9.4 Unit trusts/pooled vehicles

The Fund holds the following investments in unit trusts/pooled vehicles at 31 March which are in excess of 5% of the value of the Fund:

| 2009 | | 2010 | | Unit trust / pooled vehicle | 2011 | |
|---------|-----|---------|-----|---|---------|-----|
| £000 | % | £000 | % | | £000 | % |
| 179,544 | 8.1 | 251,456 | 8.2 | Legal and General - UK Equity Index | 272,336 | 8.0 |
| 139,490 | 6.3 | 188,021 | 6.1 | Legal and General - Europe (Ex UK) Equity Index | 217,569 | 6.4 |
| 139,221 | 6.3 | 192,169 | 6.2 | Legal and General - North America Equity Index | 213,791 | 6.3 |
| n/a | n/a | 160,734 | 5.2 | Goldman Sachs - UK Sterling Credit Portfolio | 168,675 | 4.9 |

Pension Fund Accounts

9.5 Single investments

The Fund holds the following single investments which are in excess of 5% of any asset class or type of security:

| 2009 | | 2010 | | Asset Type | Asset Name | 2011 | |
|----------------------|--------|---------|-------|-----------------------------------|---|---------|--------|
| £000 | % | £000 | % | | | £000 | % |
| FIXED INTEREST | | | | | | | |
| 8,847 | 14.0% | - | - | UK Govt Fixed Interest | UK Treasury 5.0% 07 Sept 2014 | - | - |
| 5,204 | 8.2% | - | - | UK Govt Fixed Interest | UK Treasury 6.0% 07 Dec 2028 | - | - |
| 4,718 | 7.5% | - | - | UK Govt Fixed Interest | UK Treasury 4.75% 07 Sept 2015 | - | - |
| 4,605 | 7.3% | - | - | UK Govt Fixed Interest | UK Treasury 4.50% 07 Dec 2042 | - | - |
| 3,455 | 5.5% | - | - | UK Govt Fixed Interest | UK Treasury 4.25% 07 Jun 2032 | - | - |
| 3,381 | 5.3% | - | - | UK Govt Fixed Interest | UK Treasury 4.25% 07 Dec 2055 | - | - |
| 267 | 100.0% | - | - | Overseas Govt Fixed Interest | Germany (Fed Rep) 4.25% Bonds 04 July 2039 EURO.01 | - | - |
| 3,075 | 7.0% | - | - | Overseas Corporate Fixed Interest | European Investment Bank 5.50% 07 Dec 2011 | - | - |
| 3,058 | 7.0% | - | - | Overseas Corporate Fixed Interest | Instituto de Credito Oficial 4.50% 07 Dec 2011 | - | - |
| EQUITIES | | | | | | | |
| 5,768 | 10.0% | 7,831 | 10.0% | UK Quoted Equities | Vodafone Group | 6,395 | 8.9% |
| 3,133 | 5.4% | - | - | UK Quoted Equities | Sabmiller plc | 5,944 | 8.3% |
| - | - | 5,102 | 6.5% | UK Quoted Equities | Rio Tinto | 5,765 | 8.1% |
| - | - | - | - | UK Quoted Equities | Astrazeneca | 5,545 | 7.7% |
| 4,510 | 7.8% | - | - | UK Quoted Equities | BP Plc | - | - |
| INDEX LINKED BONDS | | | | | | | |
| 11,157 | 15.5% | 9,861 | 5.7% | UK Index Linked | UK (Govt) Treasury IL Stock 2.5% 26 July 2016 | 8,905 | 5.2% |
| 9,397 | 13.0% | - | - | UK Index Linked | UK (Govt) Treasury IL Stock 2.500% 16 April 2020 | - | - |
| 8,096 | 11.2% | - | - | UK Index Linked | UK (Govt) Treasury IL Stock 17 Jul 2024 | - | - |
| 6,276 | 8.7% | - | - | UK Index Linked | UK (Govt) Treasury IL Stock 4.125% 22 Jul 2030 | - | - |
| 5,111 | 7.1% | - | - | UK Index Linked | UK (Govt) Treasury IL Stock 1.125% 22 Nov 2037 | - | - |
| 4,382 | 6.1% | - | - | UK Index Linked | UK (Govt) Treasury IL Stock 2.0% 26 Jan 2035 | - | - |
| 4,111 | 5.7% | - | - | UK Index Linked | UK (Govt) Treasury IL Stock 1.875% 22 Nov 2022 | - | - |
| 3,998 | 5.5% | - | - | UK Index Linked | UK (Govt) Treasury IL Stock 1.25% 22 Nov 2055 | - | - |
| UNIT TRUSTS | | | | | | | |
| - | - | 20,486 | 11.0% | Unit Trusts | Aviva Investors Property Fund | 24,317 | 10.4% |
| - | - | 20,644 | 11.1% | Unit Trusts | Lothbury Property Fund | - | - |
| 21,218 | 17.6% | 15,781 | 8.5% | Unit Trusts | Blackrock UK Property Fund | - | - |
| 10,854 | 9.0% | 9,883 | 5.3% | Unit Trusts | Capital Residential Fund | - | - |
| 7,242 | 6.0% | - | - | Unit Trusts | Schroder Property Investment Management Fund | - | - |
| 6,656 | 5.5% | - | - | Unit Trusts | Henderson UK Retail Warehouse Fund | - | - |
| 6,503 | 5.4% | - | - | Unit Trusts | Hercules Unit Trust | - | - |
| 6,274 | 5.2% | - | - | Unit Trusts | Quercus Healthcare Property | - | - |
| MANAGED FUNDS | | | | | | | |
| 111,081 | 34.1% | 137,435 | 36.1% | Managed Funds | M&G Alpha Opportunities Fund | 144,375 | 35.5% |
| 47,772 | 14.7% | 45,633 | 12.0% | Managed Funds | Infracapital Partners | 53,913 | 13.2% |
| 24,370 | 7.5% | 23,998 | 6.3% | Managed Funds | Mellon Offshore Currency Opp Enhanced UK Equitized Fund | 30,053 | 7.4% |
| | | 33,359 | 8.8% | Managed Funds | Record Currency Alpha US Equitized Fund | 28,288 | 7.0% |
| | | 21,653 | 5.7% | Managed Funds | Goverance of Owners European Focus Fund | - | - |
| DERIVATIVE CONTRACTS | | | | | | | |
| - | - | - | - | Derivative Contracts | S&P 500 Emini Index Futures Exp June 11 | 22 | 100.0% |
| 2,654 | 53.1% | - | - | Derivative Contracts | FTSE 100 Index Future Expiry June 2009 | - | - |
| 422 | 8.4% | - | - | Derivative Contracts | UK Long Gilt Future Expiry June 2009 | - | - |
| 273 | 5.5% | - | - | Derivative Contracts | US 10 yr Treasury Note Future Expiry June 2009 | - | - |
| 269 | 5.4% | - | - | Derivative Contracts | DJ Euro Stock 50 Future Expiry June 2009 | - | - |
| PROPERTY | | | | | | | |
| 10,000 | 12.0% | 13,150 | 11.2% | Property | 55-57 Dean Street, London | 13,220 | 9.0% |
| - | - | - | - | Property | 74-82 Western Road | 10,600 | 7.2% |
| - | - | 7,500 | 6.4% | Property | 32-36 High Street, Guildford | 8,350 | 5.7% |
| 7,050 | 8.5% | 7,350 | 6.2% | Property | Redditch Abbey Retail Park | 8,200 | 5.6% |
| - | - | - | - | Property | Cardiff Gate Business Park, Cardiff | 8,175 | 5.5% |
| 6,600 | 7.9% | 7,600 | 6.5% | Property | 121 Dunmow Road, Bishops Stortford | 7,800 | 5.3% |
| 6,725 | 8.1% | 6,900 | 5.9% | Property | Stortford Hall, Bishops Stortford | 7,750 | 5.3% |
| 5,650 | 6.8% | 6,500 | 5.5% | Property | Victoria Road Retail Park, Wellingborough | - | - |
| 5,000 | 6.0% | 6,100 | 5.2% | Property | 13-15 Magdalen Street, Oxford | - | - |
| | | | | Property | Metropolis, Borehamwood | - | - |
| CASH | | | | | | | |
| - | - | - | - | Cash | BNY Mellon Euro Liquidity Fund | 22,347 | 29.1% |
| 78,973 | 76.0% | 59,077 | 63.7% | Cash | BNP Paribas Investment Partners GBP | 20,658 | 26.9% |
| - | - | - | - | Cash | BNY Mellon Sterling Liquidity Fund | 17,924 | 23.4% |
| - | - | - | - | Cash | BNP Paribas Investment Partners US\$ | 4,643 | 6.1% |

Pension Fund Accounts

At 31 March 2011, the Fund had a commitment to contribute a further **£221m** to existing partnership investments, including private equity, infrastructure and financing (31 March 2010: £133m, 31 March 2009: £113m). It is anticipated that payments against these commitments will be made over the next 1-5 financial years.

9.6 Derivative contracts

A breakdown of derivative contracts is as follows:

| 31 March 2009 | | 31 March 2010 | | 31 March 2011 | |
|---|--------------|-------------------|--------------|-------------------|--------------|
| Economic Exposure | Market Value | Economic Exposure | Market Value | Economic Exposure | Market Value |
| £000 | £000 | £000 | £000 | £000 | £000 |
| Futures contracts - exchange traded | | | | | |
| 32,899 | 523 | - | - | - | - |
| (40,182) | (132) | - | - | - | - |
| 125,291 | 2,669 | - | - | - | - |
| (123,327) | (4,965) | 1,229 | 21 | 948 | 22 |
| 5,319 | - | (1,229) | - | (948) | - |
| - | (1,905) | - | 21 | - | 22 |
| Forward foreign exchange contracts | | | | | |
| 652,455 | - | 830,955 | - | 901,434 | - |
| (684,462) | - | (858,241) | - | (904,494) | - |
| - | 1,804 | - | 1,610 | - | - |
| - | (33,811) | - | (28,896) | - | (3,060) |
| (32,007) | (33,912) | (27,286) | (27,265) | (3,060) | (3,038) |
| Total Derivative Contracts held at year end | | | | | |

Futures contracts are used to gain exposure to investment markets without the need to purchase underlying stocks and shares.

Forward foreign exchange contracts are used to hedge against the currency risk of the Fund's overseas investments.

10. Additional Voluntary Contributions (AVC) Investments

In accordance with the Local Government Pension Scheme (Administration) Regulations 2008, additional voluntary contributions (AVCs) are not included within the transactions recorded within the Fund Account.

The AVC providers to the Fund are the Equitable Life Assurance Society and Standard Life Assurance Company. The assets of these investments are held separately from the Fund. The AVC providers secure additional benefits on a money purchase basis for those members electing to pay additional voluntary contributions. Members participating in these arrangements each receive an annual statement confirming the amounts held in their account and the movements in the year.

Pension Fund Accounts

The Fund relies on individual contributors to check that deductions made on their behalf are accurately reflected in the statements provided by the AVC providers. A summary of the information provided by Equitable Life and Standard Life to the Fund is shown in the table below.

| 2008/09 £000 | 2009/10 £000 | | 2010/11 £000 |
|-----------------|-----------------|--|-----------------|
| 6,355 | 5,446 | Value of AVC fund at beginning of year | 6,050 |
| 646 | 365 | Employees contributions | 421 |
| (768) | 1,098 | Investment income and change in market value | 361 |
| (787) | (859) | Benefits paid and transfers out | (836) |
| <u>5,446</u> | <u>6,050</u> | | <u>5,996</u> |

11. Current assets and liabilities

| 31 March 2009 £000 Restated | 31 March 2010 £000 Restated | | 31 March 2011 £000 |
|--------------------------------------|--------------------------------------|--------------------------------------|--------------------------|
| | | Current assets | |
| 14,413 | 5,065 | Cash | |
| - | - | Cash at bank | 540 |
| - | - | Cash on short term deposit <3 months | 12,610 |
| | | Debtors and payments in advance | |
| | | Contributions due | |
| 278 | 241 | Central Government | 12,930 |
| 11,380 | 16,496 | Other Local Authorities | 9,875 |
| 15 | 23 | NHS Bodies | - |
| 20,191 | 2,231 | Public Funded Bodies | 1,468 |
| 287 | 346 | Other | 6,901 |
| | | Current liabilities | |
| | | Creditors and receipts in advance | |
| | | Unpaid Benefits | |
| (112) | (89) | Central Government | (7) |
| (1,555) | (2,559) | Other Local Authorities | (454) |
| - | - | NHS Bodies | - |
| (264) | (819) | Public Funded Bodies | (15) |
| (37) | (56) | Other | (8,437) |
| (1,590) | (2,596) | Investment management expenses | (4,533) |
| | | Other liabilities | |
| - | - | Central Government | (173) |
| - | - | Receipts in advance | (55) |
| <u>43,006</u> | <u>18,283</u> | Net total | <u>30,650</u> |

Pension Fund Accounts

As at the 1 April the Fund put in place a separate bank account arrangement. Before this the Pension Fund cash was aggregated with the County Council's balance as such comparison figures as at 31 March 2009 and 31 March 2010 for cash at bank and cash on deposit can not be separately identified. In addition the Fund also holds cash in bank and on deposit with the Fund's custodian The Bank of New York Mellon. The settled cash position is shown separately in the Net Asset Statements under the sub heading of Investments.

The contributions accruals for 2008/09 and 2009/10 have been restated in line with best practice.

12. Related party transactions

The Fund is required to disclose material transactions with bodies or individuals that have the potential to control or influence the Council, or to be controlled or influenced by the Council. The intention in making this disclosure is to make explicit the extent to which the Fund might have been constrained in its ability to operate independently, or might have secured the ability to limit another party's ability to bargain freely with the Fund.

During the year, none of the Essex Pension Fund Board Members, Investment Steering Committee Members or Senior Officers undertook any material transactions with the Essex County Council Pension Fund. There were no material contributions due from employer bodies at the year end which remained outstanding after the due date for payment.

As at the 1 April the Fund put in place a separate bank account arrangement. Before this, the Pension Fund cash was aggregated with the County Council's balance. Surplus cash is invested by the County Council treasury management team on the sterling money market, in accordance with the Essex Pension Fund treasury management policy and strategy as agreed by the Essex Pension Fund Board on 31 March 2010. This service is provided to the Fund at a cost of **£0.022m**.

During the year to 31 March 2011, the Pension Fund had an average investment balance of **£10.518m** (2010: £17.962m and 2009: £22.683m) earning **£0.111m** interest (£0.116m, 2010 and £0.904m, 2009).

13. Nature and Extent of Risks arising

The Fund's activities expose it to a variety of financial risks:

- **Credit risk** – the possibility that other parties might fail to pay amounts due to the Pension Fund.
- **Liquidity risk** – the possibility that the Fund might not have funds available to meet its commitments to make payments.
- **Market risk** – the possibility that financial loss might arise for the Fund as a result of changes in such measures as interest rates and stock market movements.

Pension Fund Accounts

Credit Risk

The Fund is exposed to credit risk in its operational activities through forward currency contracts, derivative positions (futures) and treasury management activities. Commercial credit risk also arises with those organisations that pay monies over to the Fund (debtors) as part of the administration function, principally contributions from employers and transfers in from other registered pension schemes.

Except in certain bulk transfer cases, the Fund does not apply service credits in respect of transfers in until cash settlement is made and closely monitors the monthly receipt of contributions and annual reconciliation to member records. The Funding Strategy Statement requires safeguards to be in place on all new admission agreements to protect the Fund from an employer default, including through a guarantee from a tax backed scheme employer for any new body. An analysis of debtor balances at 31 March 2011 is provided in Note 11.

Forward currency contracts are undertaken by Legal & General for the passive currency overlay programme and by the Funds appointed Fund managers. The largest single contracts are entered into for the overseas equity passive currency overlay; the counterparties on these contracts as at 31 March 2011 are shown in the table below. The counterparty on contracts entered into by other investment managers is at the discretion of those managers. All parties entering into forward contracts on behalf of the Fund are FSA regulated and meet the requirements of the LGPS (Management & Investment of Funds) Regulations 2009. Further details of forward foreign exchange contracts are provided in Note 9.

| Counterparty | Total Exposure | |
|------------------------------|------------------|---------------|
| | 2011 | |
| | £000 | % |
| Barclays Capital | 49,525 | 3.3% |
| BNP Paribas Capital Markets | 122,149 | 8.2% |
| Australian Commonwealth Bank | 104,757 | 7.0% |
| Credit Suisse AG | 164,726 | 11.0% |
| Deutsche Bank AG | 132,522 | 8.9% |
| HSBC | 147,100 | 9.9% |
| J P Morgan Securities | 251,447 | 16.9% |
| RBS | 100,227 | 6.7% |
| Royal Bank of Canada | 57,722 | 3.9% |
| SG Securities | 205,032 | 13.7% |
| UBS | 119,070 | 8.0% |
| Westpac Bank Corp | 37,052 | 2.5% |
| Total | 1,491,329 | 100.0% |

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Futures contracts entered into by the Fund are all exchange traded. At the 31 March 2011 the contracts in place were all traded in the US on the CME. Further details of these futures contracts are provided in note 9. In these transactions the clearing broker Goldman Sachs acts as counterparty to both sides of the contract (buyer and seller). The clearing broker requires both parties to put up an initial amount of cash (variation margin). All positions are then marked to market daily, with margins required to be posted and maintained at all times. This minimises the risk of default by either party. In the event that a client does default, FSA rules state that the broker must make good the position to the extent that it is able, primarily through accessing the other party's variation margin. The ultimate default risk therefore lies with Goldman Sachs and their balance sheet strength but is underpinned by the contractual requirement for variation margin. Goldman Sachs is a registered deposit taking institution and therefore monies posted to it are held under banking regulation rather than in accordance with FSA client money rules.

The Fund has operated a separate bank account since 1 April 2010 with Lloyd's TSB Bank plc, which is also banker to the Administering Authority. The bank holds an A+ long term credit rating with Standard and Poor. Cash is not invested with Co-op but is placed with institutions on the Administering Authority's approved counter-party list. The management of cash is carried out by the Treasury Management function of the Administering Authority in accordance with the treasury management policy and strategy approved by the Essex Pension Board. The Board have approved the management of cash in accordance with the policies and practices followed by the Administering Authority for its own investments as outlined in the CIPFA Code of Practice for Treasury Management in the Public Services. The Authority sets detailed credit criteria having taken independent advice and has maximum exposure limits to any single institution. Details of such are shown in the table below. At 31 March 2011 **£13.150m** was under management by the Administering Authority's Treasury Management Team. Over the last five financial years the Pension Fund has no experience of default or uncollectible deposits.

The majority of the cash held by the Fund's custodian, the Bank of New York Mellon (BNY Mellon) is swept overnight to one of two AAA rated money market funds. The historical experience of default from AAA rated entities detailed in the table below is nil. As at 31 March 2011, the total balance held in the sterling, US dollar and Euro AAA money market funds was **£69.944m**, with a smaller balance of **£6.477m** held in the BNY Mellon current account. The use of a money market fund provides an underlying diversification of counter-party and avoids exposure to a single institutional balance sheet, in this case the custodian.

The following table summarises the maximum exposure to credit risk of the cash held with the Administering Authority's Treasury Management Team and the Bank of New York Mellon.

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| | 31 March 2011 £000 | Maximum limit per Financial Institution £000 | Historical risk of default % | Estimated maximum exposure to default and uncollectability £000 |
|--|--------------------------|--|---|--|
| Cash managed by Essex County Council | | | | |
| Deposit with bank and other financial institutions | | | | |
| AA Rated | 7,610 | 10,000 | 0.03% | 2 |
| A Rated | 5,540 | 5,000 | 0.08% | 4 |
| Cash managed by The Bank of New York Mellon - Other | | | | |
| Deposit with bank and other financial institutions | | | | |
| AAA Rated | 69,944 | 60,000 | - | - |
| AA Rated | 6,628 | - | 0.03% | 2 |
| A Rated | 165 | - | 0.08% | - |
| Total | 89,887 | 75,000 | | 8 |

The table below provides a breakdown of where the Pension Fund cash is managed:

| 2008/09 £000 | 2009/10 £000 | Cash | 2010/11 £000 |
|---------------------------------|-----------------|--------------------------------------|-----------------|
| Cash managed externally | | | |
| Cash held on deposit | | | |
| BNP Paribas Investment Partners | | | |
| 78,973 | 59,077 | Currency - GBP | 20,658 |
| 2,542 | 3,290 | Currency - US\$ | 4,643 |
| 4,371 | 1,930 | Currency - EURO € | 3,524 |
| - | - | BNY Mellon Liquidity Fund | |
| - | - | Currency - GBP | 17,924 |
| - | - | Currency - US\$ | 848 |
| | | Currency - EURO € | 22,347 |
| Cash held in Current Account | | | |
| 15,664 | 28,210 | The Bank of New York Mellon | 6,477 |
| 50 | 50 | Barclays plc | 151 |
| 2,282 | 159 | Cash held in a Margin Account | 165 |
| 103,882 | 92,716 | Total cash managed externally | 76,737 |
| Cash managed internally | | | |
| Cash held on deposit | | | |
| 14,413 | 5,065 | Barclays Bank | 7,000 |
| - | - | Royal Bank of Scotland Group | 5,000 |
| - | - | Santander UK | 610 |
| Cash held in Current Account | | | |
| - | - | Lloyds TSB Bank plc | 540 |
| 14,413 | 5,065 | Total cash managed internally | 13,150 |
| 118,295 | 97,781 | Total | 89,887 |

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Credit risk will be considered by the Fund's bond managers in their portfolio construction. A bond is a saleable debt instrument issued by a corporation, government or other entity, the instrument may be purchased direct from the issuer or in the secondary market. In addition to passive manager, Legal & General, the Fund has two active bond managers M&G Investments (M&G) and Goldman Sachs Asset Management (GSAM). M&G manage pooled assets against a LIBOR plus benchmark. At 31 March 2011, the average credit quality of this mandate was A+ rated and the portfolio had suffered 4 defaults since inception. GSAM manage pooled assets against the iBoxx Sterling Non Gilts index. At 31 March 2011 the average credit quality of this mandate was an AA- rated and the portfolio had suffered no defaults since inception.

Liquidity Risk

The majority of the Fund's investments are quoted on major stock markets and are in readily realisable form. The Fund's strategic allocation to property and partnership investments, which are relatively illiquid, was as a result of a review of strategic asset allocation on 23 February 2011, 22.5% of the Fund's assets. The Fund is relatively immature with almost as many contributors as pensioners, dependants and deferred pensioners. In consequence the Fund has a positive cash flow and is able to pay benefits from contributions received. As the Fund is not in the position of a forced seller, i.e. it does not need to sell assets in order to pay benefits, it is considered appropriate to hold such investments to increase diversification, minimise risk and improve long-term investment performance.

Market Risk

Market risk is inherent in the investments that the Fund makes. To mitigate market risk the investments are made in a diversified pool of asset classes and investment approaches to ensure a risk adjusted balance between categories. The Fund takes formal advice from its independent investment consultant (Hymans Robertson LLP) and the portfolio is split between a number of managers and investment strategies with different benchmarks and performance targets. Full details can be found in the Statement of Investment Principles shown in of the Pension Fund Report and Accounts and is also available from the website www.essexpensionfund.co.uk. Investment risk and strategy are regularly reviewed by the Investment Steering Committee.

Interest rate risk primarily impacts on the valuation of the Funds' bond holdings and to a lesser degree the return it receives on cash held. As detailed above, the Fund has one passive bond mandate with Legal & General. For the M&G and GSAM portfolios bond exposure is actively managed.

Currency risk is the extent to which the pension fund is exposed to fluctuations in exchange rates and the impact these fluctuations have on the Sterling valuation of assets denominated in foreign currency. To partly mitigate this risk the Fund has a currency overlay programme in place the details of which can be found in note 9.

Price risk is the risk of volatility (+/-) in the price (valuation) of the assets held by the Fund. The level of volatility will vary by asset class and also over time. The Fund has some

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diversification in the asset classes in which it invests, which seeks to reduce the correlation of price movements between different asset types, while employing specialist investment managers to best deploy capital in line with the Funds overall strategy. The Local Government investment regulations contain prescribed limits to avoid over-concentration in specific areas.

Custody

The Fund has appointed BNY Mellon as a global custodian with responsibility for safeguarding the assets of the Fund. As at 31 December 2010 BNY Mellon had \$25.0 trillion of assets under custody - making it the world's largest global custodian – and had a credit rating of AA-. The existing custody contract commenced in 2006. The contract is due for re-tender during 2010/11 in which time a procurement process will be undertaken. Monthly reconciliations are performed between the underlying records of the custodian and all investment managers and partnerships of the Fund.

Investment Management

The Fund has appointed a number of segregated and pooled fund managers to manage portions of the Fund. An Investment Management Agreement is in place for each relationship. All appointments meet the requirements set out in the LGPS (Management and Investment of Funds) Regulations 2009. Reports on manager performance are monitored by the Investment Steering Committee on a quarterly. The Fund makes use of a third party performance measurement service BNY Mellon Performance & Risk Analytics Europe Limited. In addition to presenting to the Investment Steering Committee, managers also meet with Fund officers and advisers to review progress

Sensitivity of funding position to market conditions and investment performance
When preparing the formal valuation the Actuary takes the assets of the fund at market value on the valuation date. Volatility in investment performance as a result of market risk factors can have an immediate and tangible effect on the funding level and deficit. This is particularly relevant because the Fund is invested predominantly in riskier (and historically higher return) assets such as equities and equity-like investments (e.g. property). A rise or fall in the level of equity prices can have a direct impact on the financial position of the Fund.

Less obvious is the effect of anticipated investment performance on the Fund's liability to pay future pension benefits. Here the returns available on government bonds (gilts) are important, as the discount rate that is used to place a value on liabilities is the gilt yield at the valuation date plus a margin of 2.5% per annum (pre retirement) and 1.0% per annum (post retirement). Effectively if the gilt yield rises the discount rate will increase and all other things being equal the value placed on liabilities will fall. If the fund was invested entirely in gilts rather than potentially higher returning assets the discount rate would be lower as no margin for performance over gilts could be assumed.

Pension Fund Accounts

14. Further information

The Council publishes a separate Pension Fund Report and Accounts. Copies may be obtained from the website www.essexpensionfund.co.uk or contacting:

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