

Section Two - 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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Pension Fund Accounts

Fund Account for the year ended 31 March 2014

2012/13 £000	Note		2013/14 £000	£000
		Contributions and Benefits		
		Income		
		Contributions receivable		
(47,260)	7	Member contributions	(48,843)	
(177,755)	7	Employers' contributions	(164,798)	
(13,217)	7	Transfers in from other Pension Funds	(10,157)	
(132)		Other income	(66)	
<u>(238,364)</u>		Total income		<u>(223,864)</u>
		Expenditure		
		Benefits payable		
154,022	7	Pensions	162,589	
36,138		Commutation of pensions & lump sum retirement benefits	36,518	
4,403		Lump sum death benefits	3,951	
		Payments to and on account of Leavers		
70		Refunds of contributions	29	
6		State scheme premiums	7	
8,851	7	Transfers out to other schemes	9,967	
1,744	9	Administration expenses	2,292	
<u>205,234</u>		Total expenditure		<u>215,353</u>
(33,130)		Net additions from dealings with members		<u>(8,511)</u>
		Returns on investments		
(71,300)	8	Investment income	(63,564)	
(355,171)	11	Profit and losses on disposal of investments and changes in market value of investments	(330,474)	
3,106	14	Taxes on income	3,010	
17,669	10	Investment management expenses	20,638	
<u>(405,696)</u>		Net returns on investments		<u>(370,390)</u>
(438,826)		Net (increase)/decrease in the assets available for benefits during the year		<u>(378,901)</u>
(3,519,647)		Net assets as at 1 April		<u>(3,958,473)</u>
<u>(3,958,473)</u>		Net assets as at 31 March		<u>(4,337,374)</u>

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Net Assets Statement as at 31 March 2014

31 March 2013 £000	Note		31 March 2014	
			£000	£000
	11	Investments at market value		
		Investment assets		
179,980		Fixed interest securities	186,598	
2,427,887		Equities	2,644,294	
264,371		Index linked securities	344,996	
195,665		Property	237,300	
222,930		Property unit trusts	231,664	
196,995		Private Equity	212,033	
113,567		Infrastructure	127,236	
30,972		Timber	34,705	
25,332		Active currency	-	
175,598		Other managed funds	185,029	
1,925		Derivative contracts	4,282	
96,481		Cash/deposits	93,508	
10,570		Other investment balances	10,524	
<u>3,942,273</u>				4,312,169
		Investment liabilities		
(18,010)		Derivative contracts	(390)	
<u>(3,191)</u>		Other investment balances	<u>(1,541)</u>	
<u>(21,201)</u>				(1,931)
3,921,072		Total Investments		<u>4,310,238</u>
		Long term assets		
9,414		Contributions due from employers		7,907
	13	Current assets and liabilities		
		Current Assets		
17,276		Cash		13,638
17,853		Contributions due from employers and other current assets		18,516
<u>3,965,615</u>				<u>4,350,299</u>
		Current liabilities		
(7,142)		Unpaid benefits and other current liabilities		(12,925)
<u>3,958,473</u>		Net assets of the scheme available to fund benefits		<u>4,337,374</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").

The Essex Pension Fund is part of the Local Government Pension Scheme and is administered by Essex County Council ("the Administering Authority") which is the reporting entity for this pension fund.

Established by the Local Government Superannuation Regulation 1974, the Fund is administered in accordance with the following secondary legislation:

- Local Government Pension Scheme(LGPS) Benefits, Membership and Contribution Regulations 2007 (as amended);
- LGPS (Administration) Regulations 2008 (as amended);
- LGPS (Management and Investment of Funds) Regulations 2009; and
- LGPS (Miscellaneous Amendments) Regulations 2014.

The Fund is a contributory defined benefit pension scheme administered by Essex County Council to provide pensions and other benefits for its employees and those other scheduled Bodies within its area. It 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 **530** 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.

The Council has delegated its pension functions to the Essex Pension Fund Board and Investment Steering Committee. Responsibility for the administration and financial management of the Fund has been delegated to the Executive Director for Corporate Services and Customer Operations along with the Director for Essex Pension Fund.

Independent investment managers have been appointed to manage the investments of the Fund. The Fund also invests in private equity, infrastructure and timber 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.

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2. Basis of preparation

The financial statements have been prepared in accordance with the requirements of the Local Government Pension Scheme (Administration) Regulations 2008, the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 issued by CIPFA which is based upon International Financial Reporting Standards (IFRS) as amended for UK public sector and with the guidelines set out in the Statement of Recommended Practice 2013/14 (SORP) and the Financial Reports of Pension Schemes Statement of Recommended Practice (revised May 2007). The accounts are prepared on a going concern basis.

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 Financial Statement of Accounts summarises the transactions for the 2013/14 financial year and its position as at 31 March 2014. The accounts do not reflect obligations to pay pensions and benefits that fall due after the financial year. However, a statement calculating the Fund's actuarial present value of promised retirement benefits as at 31 March 2014 using IAS19 methodology is included in the notes to the accounts and can be found at Note 3.3.

3. Actuarial valuation

The contributions payable for 2013/14 were determined by the 2010 Actuarial Valuation.

3.1 Actuarial Valuation 2013

An actuarial valuation of the Essex Pension Fund was carried out as at 31 March 2013 to determine the contribution rates with effect from 1 April 2014 to 31 March 2017. 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 **£3,958m** represented **80%** of the Funding Target liabilities of **£4,878m** at the valuation date. The valuation also showed that a common rate of contribution of **14.3%** of Pensionable Pay per annum was required from employers. The common rate is calculated as 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 **7.2%** of Pensionable Pay for 20 years. This would imply an average employer contribution rate of **21.5%** of Pensionable Pay in total.

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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.

The main financial assumptions used were as follows:

	Past and Future liabilities <i>Rate per annum</i>
Rate of discount	5.80%
Retail Price Index (RPI)	3.50%
Consumer Price Index (CPI)	2.70%
Rate of increase to pensions in payment (in excess of guaranteed minimum pension)	3.00%
Short term pay increase	In line with CPI assumptions for 2 years to 31 March 2015
Long term pay increase	4.50%

The assets were assessed at market value.

The next triennial actuarial valuation of the Fund is due as at 31 March 2016. Based on the results of this valuation, the contributions payable by the individual employers will be revised with effect from 1 April 2017.

3.2 Actuarial present value of promised retirement benefits

Many of the Fund's employers comply with the accounting disclosure requirements of either IAS 19 or FRS 17. These accounting standards specify the approach taken when calculating liabilities for disclosure in an employer's annual accounts – they do not determine the employer

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contribution. Employer contributions are determined via the Actuarial Valuation (as described in note 3 above).

3.3 Actuarial present value of promised retirement benefits

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

In order to assess the present value of the Fund's obligation on this basis, the Actuary, allowing for the different financial assumptions required under IAS 19 has a roll forward approach in valuing the Fund's liabilities which were last calculated at the triennial actuarial valuation as at 31 March 2013.

Liabilities are valued using a discount rate based on corporate bond yields. At 31 March 2014 the Actuary has used the point of the Merrill Lynch AA-rated corporate bond curve which is closest to the duration of the Fund's liabilities.

The duration of the Fund's liabilities is the weighted average time to pay each future expected cash flow for each member. This is based on the data from the last actuarial valuation. The Fund's liability duration as at 31 March 2014 is 18 years which in turn means a discount rate of **4.4%** per annum (31 March 2013: 4.3%). The value of the Fund's promised retirement benefits as at 31 March 2014 was **£6,515m** (31 March 2013: £6,585m).

Similar calculations were carried out as per the prior actuarial valuation date of 31 March 2010, using the same actuarial assumptions as those used for funding purposes at that date, other than the discount rate where a rate of 5.6% per annum was used. On this basis, the value, for IAS 26 purposes, of the Fund's promised retirement benefits at that date was **£4,720m**.

4. Accounting policies

4.1 Fund Account – revenue recognition

4.1.1 Contribution income

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

Employers' augmentation contributions and financial strain contributions are accounted for in the period in which the liability arises. Any amounts due in the year but unpaid are classed as a current financial asset. Amounts not due until future years are classed as long-term assets.

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4.1.2 Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the Local Government Scheme Regulations (see Note 7 which commences on page 147).

Transfers in from members wishing to use the proceeds of their additional voluntary contributions to purchase scheme benefits are accounted for on a receipts basis and included in Transfers in (see Note 7 which commences on page 147).

Bulk (group) transfers are accounted for on an accruals basis in accordance with the terms of the transfer agreement.

4.1.3 Investment Income

▪ Dividend income

This income is recognised in the Fund Account on the date the shares are quoted ex-dividend. Any amounts not received by 31 March are disclosed in the Net Asset Statement as other investment balances due. 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, and a more detailed breakdown can be found in Note 14 (page 162).

▪ Income from fixed interest, index linked securities, cash and short term deposits

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

▪ Income from other investments

This income is accounted for on an accruals basis. Any amount not received by the end of the reporting period is disclosed in the Net Asset Statement under other investment balances.

▪ Property related income

This consists primarily of rental income on property leases, and is recognised on a straight line basis over the term of the leases.

▪ Change in market value of investments

This is recognised as income during the year and 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.

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4.2 Fund Account – Expense items

4.2.1 Benefits payable

Under the regulations, retirees can receive a lump sum retirement grant in addition to their annual pension. Pensions and lump sum retirement grants are accounted for from the date of retirement. When a member chooses 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. Any amounts due but not paid are disclosed in the Net Asset Statement as current liabilities.

Other benefits are accounted for on the date that members' leave the Fund, or upon death.

4.2.2 Taxation

The Fund is a registered public service scheme under section 1 (1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax accounted for as a fund expense as it arises (see note 14).

As Essex County Council is the administering authority for the Fund, VAT input tax is recoverable on all Fund activities, including expenditure on investments and property expenses.

4.2.3 Administration expenses

Administration expenses are accounted for on an accruals basis. All expenses are recognised net of any recoverable VAT. All relevant staff costs including management, accommodation and other overhead costs has been charged direct to the Fund on the basis of time spent on investment related matters and pension administration. In 2013/14 this totalled **£1.686m** (2012/13: £1.438m).

4.2.4 Investment management expenses

All investment management expenses are accounted for on an accruals basis.

Fees of the external investment managers and custodian are agreed in their mandates governing their appointments. Broadly these are based on the market value of investments under their management and therefore increase or reduce as the value of investments change. In addition, an element of some managers' fees is performance related, subject to them reaching a trigger point. Performance related fees totalled **£401,000** in 2013/14 (2012/13: £1.466m).

The cost of obtaining investment advice from external consultants is included in investment management charges.

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4.3 Net Asset Statement

4.3.1 Financial Assets

Financial assets are held at fair value, as at each 31 March, and are recognised on the date the Fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in fair value of the asset are recognised in the Fund Account. Acquisition costs are included in the purchase cost of investments.

4.3.2 Valuation of investments

The value of investments is determined as outlined in the following paragraphs.

- **Market Quoted Investments**

The value of these investments is taken as the bid market price ruling on each 31st March.

- **Unquoted Investments**

Unquoted equity, and private equity limited partnership, investments are valued based on the latest financial statements published by the respective fund managers. In general these are valued as at each 31 March, in accordance with the guidelines issued by the British Venture Capital Association or an equivalent body. However, in a few cases an estimate of the valuation at 31 March 2014 is made – in such instances, the 31 December valuation is adjusted for payments made to, and received from, the private equity managers in the period 1 January to 31 March.

Investments in unquoted property, timber and infrastructure pooled funds are valued at the net asset value or a single price advised by the fund manager.

- **Directly held investments**

These include investments in limited partnerships, unlisted companies, trust and bonds.

The valuation of other unquoted securities (typically including pooled investments in property, infrastructure, debt securities and private equity) is undertaken by the investment manager or responsible entity and advised as a unit or security price. The valuation standards followed in these valuations adhere to industry guidelines or standards set by the constituent documents of the pool or the management agreement.

- **Unit trusts and managed funds**

These are valued at bid prices provided by the relevant fund managers, which reflect the market value of the underlying investments.

In the case of pooled investment vehicles that are accumulation funds, change in market value also includes income which is reinvested in the Fund, net of applicable withholding tax.

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- **Value of fixed interest investments**

Fixed interest investments are recorded at net market value, based on their current yield (i.e. excludes interest earned but not paid over at the Fund year-end, which is included separately within accrued investment income and disclosed within note 11).

- **Direct Property Investments**

Direct property investments have been valued, at open market value as at 31 March 2014, by Jones Lang LaSalle, Chartered Surveyors. The valuer's opinion of market value and existing use value was primarily derived using comparable recent market transactions on arm's-length terms.

4.3.3 Derivatives

Derivative financial instruments are used to manage exposure to specific risks arising from its investments activities – they are not held for speculative purposes.

Derivative contracts assets are held at fair value bid price, and liabilities are fair valued at offer prices. Changes in the fair value of derivatives are included in the change in market value (see note 11).

The value of futures contracts is determined using exchange prices published by the relevant futures exchange (e.g. LIFFE – London International Financial Futures Exchange) at the reporting date. Amounts due from or owed to the broker are amounts outstanding in respect of the initial margin and variation margin.

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 31 March.

4.3.4 Dividends, Interest and Foreign Currencies

Dividend, interest, purchases and sales of investments in foreign currencies have been accounted for at the spot market rates at the date of transaction. End of year spot market exchange rates are used to value cash balances held in foreign currency bank accounts, market values of overseas investments and purchases and sales outstanding at the end of the reporting period.

4.3.5 Cash and Cash Equivalents

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

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4.3.6 Financial Liabilities

Financial liabilities are recognised on the date the Fund becomes party to the liability at fair value as at each 31 March. From this date, any gains or losses arising from changes in the fair value of the liability are recognised by the Fund.

4.3.7 Contingent liabilities and contingent assets

Contingent liabilities are possible obligations that arise from past events whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the Pension Fund's control.

Contingent assets are possible assets that arise from past events, whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain events not wholly within the Council's control.

Contingent liabilities are not recognised in the financial statements, but are disclosed as a note to the accounts, unless the possibility of an outflow of resources is remote.

Contingent assets are not recognised in the financial statements but are disclosed as a note to the accounts where an inflow of economic benefits or service potential is probable and can be reliably measured.

4.3.8 Financial Instruments

Financial assets are recognised only when goods or services have been provided or rendered to a third party. Financial liabilities are recognised when the goods or services ordered from a third party have been received by the Fund and the third party has performed its contractual obligations.

The Fund currently only has liabilities carried at amortised cost and the carrying amount for instruments that will mature within the next twelve months from the balance sheet date is assumed to equate to the fair value.

The fair values of loans and receivables at 31st March have been reviewed and were assessed as being the same as the carrying amounts in the Balance Sheet. Assets are carried in the Balance Sheet at fair value. The values are based on the bid price.

When an asset or liability is translated at balance sheet date the gain / loss is taken as unrealised but when the asset or liability is settled (i.e. received / paid) the gain / loss becomes realised. The Fund has not entered into any financial guarantees that are required to be accounted for as financial instruments.

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5. Critical judgements in applying accounting policies

In applying the accounting policies set out within Note 4, the Fund has had to make certain judgements about complex transactions or those involving uncertainty about future events. The critical judgements made in the Fund Accounts are:

- **Use of Financial Instruments**

The Fund uses derivatives financial instruments to manage its exposure to specific risks arising from its investments. The valuation of these types of investments is highly subjective in nature. They are inherently based on forward-looking estimates and judgements that involve many factors.

- **Unquoted private equity**

Unquoted private equities are valued by the investment managers using guidelines set out by the British Venture Capital Association. The value of unquoted private equities as at 31 March 2014 was **£212m** (31 March 2013: £197m).

- **Infrastructure**

Overseas infrastructure values are determined in accordance with generally accepted valuation principles, in compliance with article 5 (3) of the Luxembourg law of 15 June 2004 on investment companies in risk capital. The infrastructure portfolio managed by M&G Investments is valued by the investment manager using guidelines set out by the International Private Equity and Venture Capital (IPEV) Valuation Guidelines. The value of infrastructure as at 31 March 2014 was **£127.2m** (31 March 2013: £113.6m).

- **Timber**

Timber valuations are determined by independent appraisers that typically estimate fair market values in accordance with the Uniform Standards of Professional Appraisal Practice (USPAP) and standards of professional appraisal practice that prevail in the countries where assets are located. The value of timber as at 31 March 2014 was **£34.7m** (31 March 2013: £31m).

- **Pension fund liability**

The pension fund liability is calculated every three years by the appointed actuary, with annual updates in the intervening years. The methodology used is in line with accepted guidelines and in accordance with International Accounting Standard (IAS) 19. This estimate is subject to significant variances, based on changes to the underlying assumptions.

As permitted under IAS26, the Fund has opted to disclose the actuarial present value of the promised retirement benefits by way of a note to the Net Asset Statement. This is shown in Note 3.3.

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

The Fund Accounts contains estimated figures that are based on assumptions made about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because balances cannot be determined with certainty, actual results could be materially different from the assumptions and estimates. The items in the net assets statement at 31 March 2014 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of promised retirement benefits	Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets. A firm of consulting actuaries is engaged to provide the fund with expert advice about the assumptions to be applied.	<p>The effects on the net pension liability of changes in individual assumptions can be measured. For instance, a 0.5% decrease in the discount rate assumption would result in an increase in the pension liability of £415m.</p> <p>A 0.5% increase in the long-term rate of salary increase would increase the value of liabilities by approximately £46m.</p> <p>Increasing the long-term rate of improvement used in the mortality projection from 1.5% to 1.75% per annual would increase the liability by approximately £45m.</p>
Private equity / Infrastructure / Timber	Private equity investments are valued at fair value in accordance with British Venture Capital Association guidelines. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total private equity investments in the financial statements are £212m . There is a risk that this investment may be under or overstated in the accounts.

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7. Membership activities

7.1 Membership

31 March 2013		31 March 2014 <i>Provisional</i>
45,001	Contributors	49,516
42,092	Deferred pensioners	43,693
33,873	Pensioners	35,254

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

7.2 Pension benefits payable

2012/13 £000		2013/14 £000
57,296	Administering Authority	60,296
81,284	Scheduled Bodies	85,589
7,327	Admitted Bodies	7,681
4,075	Community Admission Bodies	4,354
3,580	Transferee Admission Bodies	4,171
460	Resolution Bodies	498
154,022		162,589

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7.3 Contributions receivable

7.3.1 By category

Contributions receivable from employers are set out below:

2012/13		2013/14
£000		£000
93,082	Normal	97,611
-	Augmentation	4
78,669	Deficit	62,905
6,004	Other	4,278
<u>177,755</u>		<u>164,798</u>

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

7.3.2 By type

2012/13			2013/14		
Member	Employer		Member	Employer	
£000	£000		£000	£000	
15,400	50,062	Administering Authority	15,355	49,821	
24,583	87,854	Scheduled Bodies	26,699	92,997	
1,006	20,764	Admitted Bodies	848	4,448	
3,628	10,633	Community Admission Bodies	3,340	9,467	
2,422	7,794	Transferee Admission Bodies	2,371	7,367	
221	648	Resolution Bodies	230	698	
<u>47,260</u>	<u>177,755</u>		<u>48,843</u>	<u>164,798</u>	

During 2013/14 Greenfields paid a total of **£815,000** (2012/13: £689,000) towards the Actuarial deficiency.

The 2013 Actuarial Valuation took place during 2013/14. A number of employers opted to pay in 2013/14 sums based on the emerging results. These were:

- Orchestras Live - **£5,000**;
- Local Valuation Service - **£13,000**;
- Open College Network Eastern Region - **£52,000**;
- Inclusion Trust - **£14,000**; and
- Social Care Institute for Excellence - **£148,000**.

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8.2 Investment property net rental

2012/13 £000		2013/14 £000
13,783	Rental Income from investment property	13,825
(661)	Direct operating expenses arising from investment property	(1,251)
13,122	Total	12,574

8.3 Movement in the fair value of investment properties

	Freehold £000	Leasehold £000	Total £000
Fair value at 1 April 2012	153,260	42,780	196,040
Additions	416	7,541	7,957
Disposals	(100)	(21)	(121)
Net gain/loss on fair value	(7,236)	(975)	(8,211)
Fair value at 31 March 2013	146,340	49,325	195,665
Additions	30,272	9,539	39,811
Disposals	(9,854)	-	(9,854)
Net gain/loss on fair value	7,572	4,106	11,678
Fair value at 31 March 2014	174,330	62,970	237,300

9. Administrative expenses

2012/13 £000		2013/14 £000
1,438	Administration and Processing	1,686
114	Actuarial Fees	194
51	Audit fees	64
134	Legal fees	348
7	Other professional fees	-
1,744		2,292

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

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10. Investment management expenses

2012/13 £000		2013/14 £000
15,841	Management fees	17,800
357	Custody fees	527
29	Performance monitoring services	4
459	Advisory fees	407
983	Other	1,900
17,669	Total	20,638

11. Investments

11.1 Value of 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:

2013			2014		
£m	%		£m	%	
465	11.9	Aviva Investors	510	11.8	
320	8.2	Baillie Gifford and Co	383	8.9	
281	7.2	FIL Pensions Management	-	-	
232	5.9	First State Investments (UK) Ltd	217	5.0	
180	4.6	Goldman Sachs Asset Management International	186	4.3	
3	0.1	Hermes UK Smaller Companies Focus Fund	4	0.1	
1,598	40.7	Legal and General Investment Management	1,531	35.5	
(16)	-0.4	Legal and General Investment Management (Currency)	4	0.1	
-	-	Longview Partners	290	6.7	
301	7.7	Marathon Asset Management Ltd	325	7.6	
25	0.6	Mellon Capital Management	-	-	
-	-	M&G Investments	277	6.4	
156	4.0	M&G Investments Alpha Opportunities	166	3.9	
72	1.8	M&G Investments Infracapital	68	1.6	
16	0.4	M&G Investments Financing Fund	15	0.3	
43	1.1	Partners Group Management II S.à r.l	60	1.4	
214	5.4	Private Equity/Other	239	5.6	
31	0.8	Stafford Timberland Limited	35	0.8	
3,921	100.0		4,310	100.0	

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11.2 Investments by asset type

The tables below provide an analysis of investment assets by type and show the movements in the market value of the investments, including profits and losses realised on the sales of investments:

2012/13	Value at 1 April 2012	2012/13 Movement					Value at 31 March 2013
		Purchases	Net Transfers	Sale Proceeds	Change in Market Value	Cash Movement	
	£000	£000	£000	£000	£000	£000	£000
Fixed interest securities							
UK quoted	170,600	-	-	-	9,380	-	179,980
Equities							
UK quoted	77,437	54,811	(31,027)	(23,923)	12,065	-	89,363
Overseas quoted	1,114,687	419,231	(194,123)	(457,019)	123,030	-	1,005,806
UK unit trusts	291,304	-	30,617	(19,100)	49,086	-	351,907
Overseas unit trusts	702,179	-	190,020	(56,309)	144,921	-	980,811
Global unit trusts	-	-	-	-	-	-	-
Index linked securities (UK public sector quoted)	127,446	81,105	47,789	(17,295)	25,326	-	264,371
Property							
UK properties (freehold)	153,260	416	-	(100)	(7,236)	-	146,340
UK properties (leasehold)	42,780	7,541	-	(21)	(975)	-	49,325
Property unit trusts	237,865	1,702	-	(4,570)	(12,067)	-	222,930
Private equity							
UK unquoted	251	-	-	(38)	169	-	382
Overseas unquoted	154,173	52,040	-	(35,402)	25,802	-	196,613
Infrastructure							
UK unquoted	66,762	2,208	-	(4,157)	6,781	-	71,594
overseas unquoted	36,240	6,759	-	(2,024)	998	-	41,973
Timber (Overseas unquoted)	28,181	2,161	-	-	630	-	30,972
Active currency (UK unquoted)	25,676	-	-	-	(344)	-	25,332
Other managed funds							
UK unquoted	162,687	6,955	-	(721)	6,677	-	175,598
Overseas unquoted	723	-	-	(631)	(92)	-	-
Derivative future contracts	21	-	-	-	(21)	-	-
Cash							
Cash deposits held at the custodian/other							
Sterling	40,951	-	7,017	-	-	20,471	68,439
Foreign currency	27,588	-	-	28,630	(28,630)	454	28,042
Cash deposits held in the margin account at GSAM							
Sterling	276	-	-	-	-	(276)	-
Foreign currency	53	-	-	329	(329)	(53)	-
	3,461,140	634,929	50,293	(592,351)	355,171	20,596	3,929,778
Other investment balances							
Assets							
Amounts receivable for sales of investments	2,591						4,156
Investment income due	5,494						6,414
Liabilities							
Amounts payable for purchase of investments	(4,484)						(2,990)
Investment withholding tax payable	(127)						(201)
Derivative pending foreign currency contracts							
Assets	21,632						1,925
Liabilities	(45)						(18,010)
	3,486,201						3,921,072

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2013/14	Value at 1 April 2013	2013/14 Movement					Cash Movement	Value at 31 March 2014
		Purchases	Net Transfers	Sale Proceeds	Change in Market Value			
	£000	£000	£000	£000	£000	£000	£000	
Fixed interest securities								
UK quoted	179,980	-	-	-	6,618	-	186,598	
Equities								
UK quoted	89,363	22,180	33,073	(13,678)	(2,305)	-	128,633	
Overseas quoted	1,005,806	304,909	(20,700)	(316,123)	79,437	-	1,053,329	
UK unit trusts	351,907	48,559	(104,981)	(98,113)	31,395	-	228,767	
Overseas unit trusts	980,811	480,613	(479,084)	(372,057)	75,697	-	685,980	
Global unit trusts	-	28,972	506,491	-	12,122	-	547,585	
Index linked securities (UK public sector quoted)	264,371	60,626	65,114	(27,828)	(17,287)	-	344,996	
Properties								
UK properties (freehold)	146,340	30,272	-	(9,854)	7,572	-	174,330	
UK properties (leasehold)	49,325	9,539	-	-	4,106	-	62,970	
Property unit trusts	222,930	22,304	-	(22,532)	8,962	-	231,664	
Private equity								
UK unquoted	382	-	-	-	40	-	422	
Overseas unquoted	196,613	34,284	-	(39,912)	20,626	-	211,611	
Infrastructure								
UK unquoted	71,594	1,525	-	(7,301)	1,942	-	67,760	
overseas unquoted	41,973	22,084	-	(2,829)	(1,752)	-	59,476	
Timber (Overseas unquoted)	30,972	5,931	-	(627)	(1,571)	-	34,705	
Active currency (UK unquoted)	25,332	-	(23,509)	-	(1,823)	-	-	
Other managed funds								
UK unquoted	175,598	4,720	-	(2,383)	7,094	-	185,029	
Overseas unquoted	-	-	-	-	-	-	-	
Derivative future contracts	-	-	-	-	-	-	-	
Cash								
Cash deposits held at the custodian/other								
Sterling	68,439	-	-	-	-	(23,727)	44,712	
Foreign currency	28,042	-	-	(99,601)	99,601	20,754	48,796	
Cash deposits held in the margin account								
Sterling	-	-	-	-	-	-	-	
Foreign currency	-	-	-	-	-	-	-	
	3,929,778	1,076,518	(23,596)	(1,012,838)	330,474	(2,973)	4,297,363	
Other investment balances								
Assets								
Amounts receivable for sales of investments	4,156						3,787	
Investment income due	6,414						6,737	
Liabilities								
Amounts payable for purchase of investments	(2,990)						(1,428)	
Investment withholding tax payable	(201)						(113)	
Derivative pending foreign currency contracts								
Assets	1,925						4,282	
Liabilities	(18,010)						(390)	
	3,921,072						4,310,238	

For 2013/14, the total transaction costs were **£1.081m** (2012/13: £1.5m).

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31 March 2013 £000		31 March 2014 £000
	Fixed interest securities	
179,980	UK quoted	186,598
	Equities	
89,363	UK quoted	128,633
1,005,806	Overseas quoted	1,053,329
351,907	UK unit trusts	228,767
980,811	Overseas unit trusts	685,980
-	Global Unit trusts	547,585
264,371	Index linked securities: UK public sector quoted	344,996
	Property	
146,340	UK properties (freehold)	174,330
49,325	UK properties (leasehold)	62,970
222,930	Property unit trusts	231,664
	Private equity	
382	UK unquoted	422
196,613	Overseas unquoted	211,611
	Infrastructure	
71,594	UK unquoted	67,760
41,973	Overseas unquoted	59,476
30,972	Timber: Overseas unquoted	34,705
25,332	Currency: Overseas unquoted	-
175,598	Other managed funds: UK unquoted	185,029
	Derivative contracts	
1,925	Assets: Derivative pending foreign currency contracts	4,282
(18,010)	Liabilities: Derivative pending foreign currency contracts	(390)
	Cash deposits	
	Cash deposits held at custodian/other	
68,439	Sterling	44,712
28,042	Foreign currency	48,796
3,913,693		4,301,255
	Other investment balances	
	Assets	
4,156	Amounts receivable for sales of investments	3,787
6,414	Investment income due	6,737
	Liabilities	
(2,990)	Amounts payable for purchase of investments	(1,428)
(201)	Investment withholding tax payable	(113)
3,921,072	Value at 31 March	4,310,238

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11.3 Pooled investments representing 5% or more of net assets

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

31 March 2013			31 March 2014		
£000	%		£000	%	
373,996	9.4	Legal & General North America Equity Index	302,277	7.0	
-	-	M&G Global Dividend Fund	276,855	6.4	
-	-	Legal & General FTSE RAFI AW 3000 Index	270,730	6.2	
298,158	7.5	Legal & General Europe (Ex UK) Equity Index	223,027	5.1	
351,907	8.9	Legal & General UK Equity Index	121,015	2.8	
204,579	5.2	Legal & General Japan Equity Index	100,496	2.3	

11.4 Single investments in excess of 5% of any asset types

The Fund holds the following single investments at 31 March which are in excess of 5% of any asset class or type of security:

31 March 2013		Asset type / Asset name	31 March 2014	
£000	%		£000	%
UK QUOTED EQUITIES				
13,959	15.6%	Unilever plc Ord GBPO.031	14,820	11.5%
1,882	2.1%	WPP Plc Ord GBPO.10	12,355	9.6%
1,069	1.2%	Compass Group Ord GBPO.10	12,007	9.3%
1,035	1.2%	Lloyds Banking GP Ord GBPO.1	10,564	8.2%
9,511	10.6%	Sabmiller plc Ord USD0.10	8,969	7.0%
-	-	Pearson Ord GBPO.25	8,956	7.0%
2,981	3.3%	Arm Holdings Ord GBPO.0005	7,455	5.8%
5,962	6.7%	Aggreko	2,998	2.3%
UK INDEX LINKED BONDS				
18,997	7.2%	UK (Govt) Treasury IL Stock 2.5% 16 April 2020	19,684	5.7%
18,709	7.1%	UK (Govt) Treasury IL Stock 1.875% 22 Nov 2022	19,250	5.6%
18,168	6.9%	UK(Govt) Treasury IL Stock 2.5% 17 July 2024	18,436	5.3%
17,465	6.6%	UK (Govt) Treasury IL Stock 1.250% 22 Nov 2027	17,845	5.2%
15,539	5.9%	UK (Govt) Treasury IL Stock 1.250% 22 Nov 2055	16,960	4.9%
14,951	5.7%	UK (Govt) Treasury IL Stock 1.125% 22 Nov 2037	15,704	4.6%
14,625	5.5%	UK (Govt) Treasury IL Stock 2.0% 26 Jan 2035	15,095	4.4%
14,534	5.5%	UK (Govt) Treasury IL Stock 1.250% 22 Nov 2032	14,950	4.3%
PROPERTY				
15,575	8.0%	48-49 Chancery Lane, London	17,400	7.3%
13,425	6.9%	55-57 Dean Street, London	13,900	5.9%
11,200	5.7%	734-736 Seven Sisters Road, London	11,500	4.8%
11,060	5.7%	971 Great West Road, Brentford	11,300	4.8%
10,450	5.3%	74-82 Western Road, Brighton	10,400	4.4%

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31 March 2013		Asset type / Asset name	31 March 2014	
£000	%		£000	%
PROPERTY UNIT TRUSTS				
24,891	11.2%	Aviva Investors Property Fund	27,681	11.9%
15,165	6.8%	Blackrock UK Property Fund	16,156	7.0%
20,959	9.4%	Lothbury Property Fund	12,836	5.5%
6,372	2.9%	Industrial Property Investment Fund	12,802	5.5%
11,244	5.0%	Standard Life Property Fund Closed	12,651	5.5%
11,706	5.3%	Standard Life UK Shopping Centre	12,154	5.2%
PRIVATE EQUITY				
11,969	6.1%	New Mountain Partners	11,658	5.5%
8,225	4.2%	Avenue Europe Special Situations Fund II (Euro)	10,967	5.2%
11,140	5.7%	Providence Debt Opportunity Fund	10,477	4.9%
11,454	5.8%	Apollo Overseas Partners VII	7,578	3.6%
9,853	5.0%	Warburg Pincus Private Equity VIII	7,491	3.5%
INFRASTRUCTURE				
71,594	63.0%	Infracapital Partners	67,760	53.3%
37,905	33.4%	Partners Group Global Infrastructure 2009 S.C.A., SICAR	42,875	33.7%
-	-	Partners Group Global Infrastructure 2012 LP	10,117	7.9%
4,069	3.6%	Partners Group Global Infrastructure 2011 S.C.A., SICAR	6,484	5.1%
TIMBER				
30,972	100.0%	Stafford Timberland	34,705	100.0%
ACTIVE CURRENCY				
25,332	100.0%	Mellon Offshore Currency Opp Enhanced UK Equitized Fund	-	-
OTHER MANAGED FUNDS				
156,070	88.9%	M&G Alpha Opportunities Fund	166,007	89.7%
16,213	9.2%	M&G UK Companies Financing Fund	14,529	7.9%
CASH				
41,422	42.9%	BNP Paribas Investment Partners GBP	34,260	36.6%
16,645	17.3%	Northern Trust Liquidity Fund US\$	29,635	31.7%
24,007	24.9%	Northern Trust Liquidity Fund GBP	18,876	20.2%
5,695	5.9%	BNP Paribas Investment Partners EURO	2,744	2.9%

11.5 Derivative contracts

11.5.1 Objectives and policies for holding derivatives

Most of the holdings in derivatives are to hedge liabilities or hedge exposure to reduce risk in the Fund. Derivatives may be used to gain exposure to an asset more efficiently than holding the underlying asset. The use of derivatives is managed in line with the investment agreement agreed between the Fund and the various investment managers.

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11.5.2 Futures

There were no outstanding exchange traded futures contracts as at 31 March 2014 and 31 March 2013.

11.5.3 Forward foreign currency

In order to maintain appropriate diversification and to take advantage of overseas investment returns, **53.1%** of the Fund's portfolio is in overseas stock markets as at 31 March 2014 (31 March 2013: 50.6%).

To reduce the volatility associated with fluctuating currency rates the Fund has a passive currency programme in place which is managed by Legal and General Investment Management. The Fund hedges **50%** of the US Dollar, Euro and Yen exposure within the portfolios managed by the growth managers.

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11.5.4 Open forward currency contracts

Settlement	Currency Bought	Local value 000	Currency sold	Local value 000	Asset value £000	Liability value £000	Net value £000
Up to one month	AUD	(81)	DKK	(6)	-	-	-
Up to one month	AUD	27,451	GBP	15,233	29	-	29
Up to one month	AUD	11	HKD	6	-	-	-
Up to one month	CAD	19,260	GBP	10,439	28	-	28
Up to one month	CHF	28,893	GBP	19,595	24	-	24
Up to one month	EUR	(194)	DKK	-	-	-	-
Up to one month	EUR	78,824	GBP	65,204	-	(40)	(40)
Up to one month	GBP	14,938	AUD	27,451	-	(323)	(323)
Up to one month	GBP	11,020	CAD	19,260	553	-	553
Up to one month	GBP	19,527	CHF	28,893	-	(92)	(92)
Up to one month	GBP	94,352	EUR	113,407	593	-	593
Up to one month	GBP	37	HKD	478	-	-	-
Up to one month	GBP	65,114	JPY	11,158,357	123	-	123
Up to one month	GBP	8,647	SEK	92,351	103	-	103
Up to one month	GBP	83	TRY	297	-	(1)	(1)
Up to one month	GBP	179,472	USD	294,317	2,933	-	2,933
Up to one month	GBP	144	ZAR	2,540	-	(1)	(1)
Up to one month	HKD	498	SGD	-	-	-	-
Up to one month	JPY	11,158,357	GBP	65,525	-	(535)	(535)
Up to one month	SEK	92,351	GBP	8,569	-	(25)	(25)
Up to one month	USD	(1)	AUD	-	-	-	-
Up to one month	USD	294,317	GBP	176,936	-	(397)	(397)
One to six months	GBP	44,692	AUD	83,132	-	(1,332)	(1,332)
One to six months	GBP	32,535	CAD	60,207	-	(147)	(147)
One to six months	GBP	58,382	CHF	86,349	-	(315)	(315)
One to six months	GBP	206,733	EUR	250,459	-	(411)	(411)
One to six months	GBP	183,764	JPY	31,277,962	1,421	-	1,421
One to six months	GBP	25,618	SEK	276,186	81	-	81
One to six months	GBP	527,543	USD	876,327	1,623	-	1,623
Open forward currency contracts at 31 March 2014					7,511	(3,619)	3,892
<i>Open forward currency contracts at 31 March 2013</i>					<i>5,696</i>	<i>(21,781)</i>	<i>(16,085)</i>

12. Additional Voluntary Contributions (AVC) Investments

AVC's are not included in the accounts in accordance with section 4(2) (b) of the Local Government Pension Scheme (Management and Investments of Funds) Regulations 2009 but are disclosed as a note only.

The AVC providers to the Fund are the Equitable Life Assurance Society, Prudential 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

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each receive an annual statement confirming the amounts held in their account and the movements in the year.

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, Prudential and Standard Life to the Fund is shown in the table below.

2012/13 £000		2013/14 £000
5,809	Value of AVC fund at beginning of year	5,840
364	Employees contributions	413
509	Investment income and change in market value	320
(842)	Benefits paid and transfers out	(918)
<u>5,840</u>		<u>5,655</u>

13. Current assets and liabilities

13.1 Analysis of current assets

31 March 2013 £000		31 March 2014 £000 £000	
	Cash Balances		
5,742	Cash at bank	2,659	
11,534	Cash on short term deposits within 3 months	10,979	
<u>17,276</u>			<u>13,638</u>
	Debtors and payments in advance		
5,142	Contributions due – employees	4,027	
11,787	Contributions due – employers	11,073	
924	Sundry debtors	3,416	
<u>17,853</u>			<u>18,516</u>
<u>35,129</u>	Total		<u>32,154</u>

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13.2 Analysis of debtors

31 March 2013			31 March 2014	
Short term	Long term		Short term	Long term
£000	£000		£000	£000
1,381	8,868	Central Government	1,789	7,622
13,877	483	Other Local Authorities	11,275	235
-	-	NHS Bodies	52	-
646	63	Public Funded Bodies	1,826	50
1,949	-	Other	3,574	-
17,853	9,414	Total	18,516	7,907

13.3 Analysis of long term debtors

31 March		31 March
2013		2014
£000		£000
625	Financial strain instalments due	374
8,789	Other employer contributions due	7,533
9,414	Total	7,907

13.4 Contingent assets

To protect the Fund from employer default the Funding Strategy sets out safeguards to be in place on all new admission agreements. These can include a guarantee from another Fund employer with sufficient covenant strength, and a surety bond or other contingent asset.

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13.5 Analysis of current liabilities

31 March 2013 £000		31 March 2014 £000
	Unpaid benefits and other current liabilities	
(485)	Contributions due – employers	(2,570)
(3,415)	Investment manager fees payable	(4,176)
(3,090)	Benefits payable	(5,746)
(152)	Other	(433)
<u>(7,142)</u>	Total	<u>(12,925)</u>

13.6 Analysis of creditors

31 March 2013 £000		31 March 2014 £000
	Creditors and receipts in advance	
(276)	Central Government	(921)
(1,276)	Other Local Authorities	(6,501)
-	NHS Bodies	(20)
(276)	Public Funded Bodies	(361)
(5,314)	Other	(5,122)
<u>(7,142)</u>	Total	<u>(12,925)</u>

13.7 Contingent liabilities and contractual commitments

As at 31 March 2014, the Fund had a commitment to contribute a further **£314.8m** to its existing direct and indirect partnership investments, including private equity, infrastructure, timber and financing (31 March 2013: £201m). The amounts called by these funds are irregular in both size and timing over a period of between five to ten years from the date of each original commitment.

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14. Taxes on income

The table below provides a breakdown of the taxes paid by the Fund in the UK and overseas.

2012/13 £000		2013/14 £000
472	UK withholding tax	552
2,623	Overseas withholding tax	2,404
11	Payment to HMRC in respect of returned contributions	54
<u>3,106</u>		<u>3,010</u>

15. 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 negotiate freely with the Fund.

15.1 Administration of the Fund

The Essex Pension Fund is administered by Essex County Council.

The Council incurred costs of **£1.686m** in 2013/14 (2012/13: £1.438m) in relation to the administration of the Fund and was subsequently reimbursed by the Fund for these expenses. The Council is also the single largest employer of members of the Fund and contributed **£49.821m** to the Fund in 2013/14 (2012/13: **£50.062m**). No significant amounts were owing to and due to be paid from the Fund in the year.

Surplus cash is invested by the County Council's treasury management team on the sterling money markets, in accordance with the Essex Pension Fund treasury management policy and strategy as agreed by the Essex Pension Fund Board on **6 March 2013**. This service is provided to the Fund at a cost of **£26,000** (2012/13: £25,000).

During the year to 31 March 2014, the Pension Fund had an average investment balance of **£15.119m** (2012/13: £16.990m) earning **£98,000** interest (2012/13: £135,000).

15.2 Governance

None of the Essex Pension Board Members, Investment Steering Committee Members or Senior Officers undertook any material transactions with the Essex Pension Fund. There were no

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material contributions due from the employer bodies at the end of the year that remained outstanding after the due date for payment.

15.3 Members of the LGPS

Essex County Council administers the LGPS for its own employees and numerous other bodies. Under legislation introduced in 2003/04, Councillors are also entitled to join the Pension Fund. Those Members of the Essex Pension Board and Investment Steering Committee who, during 2013/14, were also members of the LGPS are listed below.

Representative of scheme members	County Councillors
<ul style="list-style-type: none">K. Blackburn	<ul style="list-style-type: none">Cllr D. M. Finch
Representative of small admitted bodies	<ul style="list-style-type: none">Cllr N. J. Hume
<ul style="list-style-type: none">J. Moore	<ul style="list-style-type: none">Cllr S. Barker
Representatives for Essex Police and Crime Commissioner	<ul style="list-style-type: none">Cllr M. C. Lager
<ul style="list-style-type: none">Cllr S. Walsh	
<ul style="list-style-type: none">C. Garbett	

As at 31 March 2014 Keith Neale, independent adviser to the Investment Steering Committee (ISC) was in receipt of pension benefits from the Fund during the financial year.

The employees of Essex County Council who hold key positions in the financial management of the Essex Pension Fund during 2013/14 were the Executive Director for Corporate Services and Customer Operations, the Director for Essex Pension Fund and the Head of Essex Pension Fund. During 2013/14 approximately **3%** (2012/13: 3%) of the Executive Director for Corporate Service and Customer Operation's time was spent on the Pension Fund, with other officers spending 100% of their time in this way. As a consequence, the short term benefits (i.e. pay) associated with the time spent by these staff working on the Fund during 2013/14 was **£141,000** (2012/13: £169,000). The 2013/14 current service cost in respect of these personnel was **£82,000** (2012/13: £81,000). The current service cost is the increase in the value of the Fund's future liabilities arising out of employees' on-going membership of the Fund.

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16. Financial Instruments

16.1 Classification of financial instruments

The following table analyses the carrying amounts of financial assets and liabilities by category and Net Asset Statement headings. No financial assets were reclassified during the accounting period.

31 March 2013			Asset type	31 March 2014		
Designated as fair value through profit and loss £000	Loans and receivables £000	Financial liabilities at amortised cost £000		Designated as fair value through profit and loss £000	Loans and receivables £000	Financial liabilities at amortised cost £000
Financial assets						
179,980	-	-	Fixed interest securities	186,598	-	-
2,427,887	-	-	Equities	2,644,294	-	-
264,371	-	-	Index linked securities	344,996	-	-
222,930	-	-	Pooled unit trusts	231,664	-	-
196,995	-	-	Private equity	212,033	-	-
109,498	-	-	Infrastructure	120,752	-	-
30,972	-	-	Timber	34,705	-	-
25,332	-	-	Active currency	-	-	-
175,598	-	-	Other managed funds	185,029	-	-
1,925	-	-	Derivative contracts	4,282	-	-
-	113,757	-	Cash deposits	-	107,146	-
10,570	-	-	Other investment balances	10,524	-	-
-	27,267	-	Debtors	-	26,423	-
3,646,058	141,024	-		3,974,877	133,569	-
Financial liabilities						
(18,010)	-	-	Derivative contracts	(390)	-	-
(3,191)	-	-	Other investments balances	(1,541)	-	-
-	-	(7,142)	Creditors	-	-	(12,925)
-	-	-	Borrowing	-	-	-
(21,201)	-	(7,142)		(1,931)	-	(12,925)
3,624,857	141,024	(7,142)	Balance at the end of the year	3,972,946	133,569	(12,925)
		3,758,739	Total			4,093,590

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16.2 Net gains and losses on financial instruments

Asset value as at 31 Mar 2013 £000		Asset value as at 31 Mar 2014 £000
	Financial assets	
392,897	Fair value through profit and loss	219,266
(28,959)	Loans and receivables	99,601
363,938	Total	318,867

16.3 Fair value of financial instruments and liabilities

31 March 2013			31 March 2014	
Carry value	Fair value		Carry value	Fair value
£000	£000		£000	£000
		Financial assets		
3,646,058	3,646,058	Fair value through profit and loss	3,974,877	3,974,877
141,024	141,024	Loans and receivables	133,569	133,569
3,787,082	3,787,082		4,108,446	4,108,446
		Financial liabilities		
(21,201)	(21,201)	Fair value through profit and loss	(1,931)	(1,931)
(7,142)	(7,142)	Financial liabilities measured at amortised cost	(12,925)	(12,925)
(28,343)	(28,343)		(14,856)	(14,856)
3,758,739	3,758,739	Total net financial assets	4,093,590	4,093,590

16.4 Valuation of financial instruments carried at fair value

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

- **Level 1** – Financial instruments where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Assets classified as Level 1 comprise equities, quoted fixed securities, quoted index linked securities and unit trusts. Listed investments are shown at bid prices. The bid value of the investments is based on bid market quotation of the relevant stock exchange.
- **Level 2** – Financial instruments where quoted market prices are not available, for example where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

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forecast cash flows. The Council manages these investment risks as part of its overall pension fund risk management programme.

Responsibility for the Fund's risk management strategy rests with the Investment Steering Committee (ISC). Risk management policies are established to identify and analyse the risks faced by the Council's pensions operations. Policies are reviewed regularly to reflect changes in activity and in market conditions.

17.2 Market risk

Market risk is the possibility that financial loss might occur as a result of fluctuations in equity and commodity prices, interest rates and foreign exchange. The level of risk exposure depends on market conditions, expectation of future price and yield movements and the asset mix.

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 institutional investment consultant, Hymans Robertson LLP, along with the Fund's independent adviser 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 which is available from the website www.essexpensionfund.co.uk. Investment risk and strategy are regularly reviewed by the Investment Steering Committee (ISC).

17.3 Other price risk

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

The Fund is exposed to share and derivative price risk. This arises from investments held by the Fund for which the future price is uncertain. All investments present a risk of loss of capital. The level of volatility will vary by asset class and also over time. The Fund has some 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 Fund's overall strategy. The LGPS investment regulations also contain prescribed limits to avoid over-concentration in specific areas.

17.4 Other price risk sensitivity analysis

In consultation with its institutional consultants, Hyman Robertson LLP, an analysis of historical data and expected return movements during the accounting periods in question was undertaken. The table below shows the potential price movements deemed possible for the accounting period 2013/14.

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The percentages shown in the following table are broadly consistent with a movement of one standard deviation in the value of the Fund's assets, and assumes that all other variables in particular foreign exchange rates and interest rates remain unchanged.

31st March 2013 Potential Market movement %	Asset type	31st March 2014 Potential Market movement %
10.0%	UK bonds	8.7%
15.5%	UK equities	16.1%
19.4%	Overseas equities	19.4%
7.9%	UK index linked bonds	6.5%
14.5%	Pooled property unit trusts	14.7%
27.5%	Private equity	28.0%
14.5%	Infrastructure funds	14.7%
14.5%	Timber	14.7%
14.5%	Property	14.7%
0.8%	Cash	0.6%
19.4%	Currency active	19.4%

Had the market price of the Fund investments increased/ (decreased) in line with the above assumptions the change in the net assets available to pay benefits would have been as follows:

31st March 2013 £000	Percentage change %	Value increase £000	Value decrease £000	Asset type	31st March 2014 £000	Percentage change %	Value increase £000	Value decrease £000
96,481	0.8%	97,253	95,709	Cash and equivalents	93,508	0.6%	94,069	92,947
				Investment portfolio assets				
179,980	10.0%	197,978	161,982	UK bonds	186,598	8.7%	202,832	170,364
89,363	15.5%	103,214	75,512	UK equities	128,633	16.1%	149,343	107,923
1,005,806	19.4%	1,200,932	810,680	Overseas equities	1,053,329	19.4%	1,257,675	848,983
351,907	15.5%	406,453	297,361	UK equities unit trusts	228,767	16.1%	265,598	191,936
980,811	19.4%	1,171,088	790,534	Overseas equities unit trusts	685,980	19.4%	819,060	552,900
-	19.4%	-	-	Global unit trusts	547,585	19.4%	653,816	441,354
264,371	7.9%	285,256	243,486	UK index linked bonds	344,996	6.5%	367,421	322,571
222,930	14.5%	255,255	190,605	Pooled property unit trusts	231,664	14.7%	265,719	197,609
196,995	27.5%	251,169	142,821	Private equity	212,033	28.0%	271,402	152,664
113,567	14.5%	130,034	97,100	Infrastructure	127,236	14.7%	145,940	108,532
30,972	14.5%	35,463	26,481	Timber	34,705	14.7%	39,807	29,603
25,332	19.4%	30,246	20,418	Active currency	-	19.4%	-	-
175,598	14.5%	201,060	150,136	Other managed funds	185,029	14.7%	212,228	157,830
195,665	14.5%	224,036	167,294	Property	237,300	14.7%	272,183	202,417
(16,085)	-	(16,085)	(16,085)	Net derivative assets	3,892	-	3,892	3,892
6,414	-	6,414	6,414	Investment income due	6,737	-	6,737	6,737
(2,990)	-	(2,990)	(2,990)	Amounts payable for purchases	(1,428)	-	(1,428)	(1,428)
4,156	-	4,156	4,156	Amounts receivable for sales	3,787	-	3,787	3,787
(201)	-	(201)	(201)	WHT payable	(113)	-	(113)	(113)
3,921,072		4,580,731	3,261,413	Total assets available to pay benefits	4,310,238		5,029,968	3,590,508

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17.5 Sensitivity of funding position

Market conditions and the underlying investment performance of the Fund's assets will have a direct impact on the funding position, albeit that a smoothed rather than spot rate methodology is used by the Fund's Actuary.

Barnett Waddingham's approach adopted at the 2013 Actuarial Valuation includes the following features:

- Financial assumptions such as inflation and the discount rate are based on smoothed market indicators from around the valuation date, specifically over the six month period from 1 January 2013 to 30 June 2013. The discount rate is based on the expected investment return from the Fund's assets.
- The market value of assets at 31 March 2013 is then adjusted to also be smoothed over the same six month period so that a consistent comparison can be made with the liabilities.

17.6 Interest rate risk

The Fund's investments are subject to interest rate risk (i.e. to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates). 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. The Fund has three bond mandates; a passive bond mandate with Legal & General and bond mandates with M&G Investments (M&G) and Goldman Sachs Asset Management (GSAM) in which exposure is actively managed.

The Fund's direct exposure to interest rate movements is shown below. The underlying assets are shown at their fair value.

Asset value as at 31 Mar 2013 £000	Asset type	Asset value as at 31 Mar 2014 £000
96,481	Cash and cash equivalents	93,508
17,276	Cash balances	13,638
179,980	Fixed interest securities	186,598
264,371	Index-linked securities	344,996
558,108	Total assets	638,740

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17.7 Interest rate risk sensitivity analysis

Interest rates over the last 24 months have remained constant but this is not always the case and can vary as a result any variation in interest rates affects the level of income achievable and the value of the net assets of the Fund to pay benefits. The Fund's institutional consultants, Hymans Robertson, has undertaken a sensitivity analysis and advised that it is reasonable in today's climate that a movement increase/(decrease) of not more than 100 basis points on a year to year basis is possible based on past experience.

The table below shows the effect in the year on the net assets available to pay benefits of an increase/(decrease) of 100 basis points change in interest rates assuming all other factors remain unchanged.

Asset value as at 31 Mar 2013 £000	Change in year in the net assets to pay benefits		Asset type	Asset value as at 31 Mar 2014 £000	Change in year in the net assets to pay benefits	
	+100 BPS £000	-100 BPS £000			+100 BPS £000	-100 BPS £000
96,481	965	(965)	Cash and cash equivalents	93,508	935	(935)
17,276	173	(173)	Cash balances	13,638	136	(136)
179,980	1,800	(1,800)	Fixed interest securities	186,598	1,866	(1,866)
264,371	2,644	(2,644)	Index-linked securities	344,996	3,450	(3,450)
558,108	5,582	(5,582)	Total change in assets available	638,740	6,387	(6,387)

17.8 Currency risk

Currency risk is the extent to which the fair value of future cash flows of a financial asset/liability will fluctuate due to changes in exchange rates. The Fund is exposed to currency risk on all assets that are denominated in any currency other than sterling, its reporting currency. To reduce the volatility associated with fluctuating currency rates the ISC has for the Fund put in place a passive currency overlay programme which is managed by Legal and General Investment Management. The Fund hedges 50% of the US Dollar, Euro and Yen exposure within the portfolios managed by the growth managers.

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The following table summarises the Fund's currency exposure as at 31 March 2014 and prior year:

31 Mar 2013 £000	Asset type	31 Mar 2014 £000
1,005,806	Overseas equities quoted	1,053,329
980,811	Overseas unit trusts	685,980
-	Global unit trusts	547,585
196,613	Overseas private equity	211,611
41,973	Overseas infrastructure	59,476
30,972	Overseas timber	34,705
2,256,175	Total overseas assets	2,592,686

17.9 Currency risk sensitivity analysis

In consultation with the Fund's institutional consultant, Hymans Robertson the Fund considers the likely volatility associated with exchange rate movements to be in the region of **13%** (2012/13: 12%) (approximately one standard deviation) assuming other factors remain constant.

The table below shows the effect of a **13%** (2012/13: 12%) strengthening/weakening of the pound against the investments the Fund holds in various other currencies. The increase/ (decrease) on the net assets of the Fund are as follows:

Asset value as at 31 Mar 2013 £000	Change in year in the net assets to pay benefits		Asset type	Asset value as at 31 Mar 2014 £000	Change in year in the net assets to pay benefits	
	+12% £000	-12% £000			+13% £000	-13% £000
1,005,806	1,126,503	885,109	Overseas equities quoted	1,053,329	1,190,262	916,396
980,811	1,098,508	863,114	Overseas unit trusts	685,980	775,157	596,803
-	-	-	Global unit trusts	547,585	618,771	476,399
196,613	220,207	173,019	Overseas private equity	211,611	239,120	184,102
41,973	47,010	36,936	Overseas infrastructure	59,476	67,208	51,744
30,972	34,689	27,255	Overseas timber	34,705	39,217	30,193
2,256,175	2,526,917	1,985,433	Total change in assets available	2,592,686	2,929,735	2,255,637

17.10 Credit Risk

Credit risk is the possibility that the counterparty to a transaction or a financial instrument might fail in its obligation to pay amounts due to the Pension Fund resulting in a financial loss. The market value of investments reflects an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the Fund's financial assets and liabilities.

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The Fund is exposed to credit risk in all its operational activities through forward currency contracts, derivative positions (futures) and treasury management activities. However, the selection of high quality counterparties, brokers and financial institutions minimises credit risk that may occur through the failure to settle a transaction in a timely manner.

17.11 Commercial

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.

Monthly receipt of contributions is closely monitored by the Employer team. In addition, member records are updated throughout the year with any new information provided to them. At the end of the financial year employers are required to provide an annual return which is used to reconcile both member information and the contributions paid over in the year by both the employee and the employer.

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 2014 is provided in Note 13.

17.12 Forward currency contracts

Forward currency contracts are undertaken by Legal & General for the passive currency overlay programme and by the Fund's 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 2014 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 11.

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Exposure at 31 March 2013		Counterparty	Exposure at 31 March 2014	
£000	%		£000	%
148,850	8.7%	Barclays Capital	210,137	11.6%
225,711	13.3%	BNP Paribas Capital Markets	66,410	3.7%
-	-	Citigroup	266,650	14.8%
133,072	7.8%	Australian Commonwealth Bank	-	-
201,007	11.8%	Credit Suisse AG	198,546	11.0%
187,096	11.0%	Deutsche Bank AG	179,669	9.9%
181,720	10.7%	J P Morgan Securities	234,581	13.0%
82,881	4.9%	Lloyds	26,148	1.4%
-	-	Merrill Lynch	59,057	3.3%
140,605	8.3%	RBC Europe	90,418	5.0%
-	-	RBS	118,333	6.6%
4,349	0.3%	SEB	-	-
194,796	11.5%	SG Securities	100,508	5.6%
184,288	10.8%	UBS	40,831	2.3%
16,162	0.9%	Westpac Bank Corp	213,637	11.8%
1,700,537	100.0%	Total	1,804,925	100.0%

17.13 Futures

There were no open future contracts as at 31st March 2013 or 31st March 2014.

17.14 Bonds

Credit risk will also 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 the passive manager, Legal & General, the Fund has two active bond managers M&G and GSAM the former also manage a financing fund.

Both M&G and GSAM manage pooled assets against a LIBOR plus benchmark. At 31 March 2014, the average credit quality of the M&G bond mandate was **BBB+** rated (**A** rated as at 31 March 2013) and the portfolio had suffered four defaults since inception, none have been experienced in the financial year ended 31 March 2014. The average credit rating of the financing fund was **BB+** rated as at 31 March 2014 (**BB** rated as at 31 March 2013), and the portfolio has not suffered any defaults since inception. The portfolio managed by GSAM as at 31 March 2014 had an average credit quality of **AA+** (**AA** rated as at 31 March 2013) and has suffered two defaults since inception, both occurring 2011/12.

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17.15 Cash held on deposit and current accounts

Cash managed internally – The Fund has operated a separate bank account since 1 April 2010 with Lloyds TSB Bank plc, which is also banker to the Administering Authority. The bank holds an **A-** (A in 2012/13) long term credit rating with Standard and Poor. Cash is invested with Lloyds TSB and 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 following tables. At 31 March 2014 **£13.638m** (31 March 2013: £17.276m) 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.

Cash managed externally – The majority of the cash held by the Fund's custodian, the Northern Trust 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 2014, the total balance held in the Sterling, US dollar and Euro AAA money market funds was **£85.515m** with a smaller balance of **£7.748m** held in the custodian current account (31 March 2013: £87.769m and £8.342m respectively). 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.

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

31 March 2013			31 March 2014	
Rating	£000		Rating	£000
		Cash managed externally		
		Cash held on deposit		
AAA	47,117	BNP Paribas Investment Partners	AAA	37,004
AAA	40,652	Northern Trust	AAA	48,511
		Cash held in Current Account		
AA	4	The Bank of New York Mellon	AA	-
AA-	8,342	Northern Trust	AA-	7,748
A+	366	Barclays plc	A	245
	96,481	Total cash managed externally		93,508
		Cash managed internally		
		Cash held on deposit		
A+	3	Barclays Bank	A	2
AA-	6,510	HSBC	AA-	7,473
AAA	-	IGNIS	AAA	1,502
A	5,019	Royal Bank of Scotland Group	BBB	2,001
		Cash held in Current Account		
A	5,744	Lloyds TSB Bank plc	A-	2,660
	17,276	Total cash managed internally		13,638
	113,757	Total		107,146

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The following table summarises the maximum exposure to credit risk of the cash held with Northern Trust and other financial institutions.

31 March 2013		31 March 2014	Maximum limit per Financial Institution	Historical risk of default	Estimated maximum exposure to default and uncollectability
£000		£000	£000	%	£000
Cash managed externally					
Deposit with bank and other financial institutions					
87,769	AAA Rated	85,515	-	-	-
8,346	AA Rated	7,748	-	0.02%	2
366	A Rated	245	-	0.09%	-
<u>96,481</u>	Total cash managed externally	<u>93,508</u>			<u>2</u>
Cash managed internally					
Deposit with bank and other financial institutions					
-	AAA Rated	1,502	10,000	-	-
6,510	AA Rated	7,473	10,000	0.02%	1
10,766	A Rated	2,662	5,000	0.09%	2
-	BBB Rated	2,001	5,000	0.20%	4
<u>17,276</u>	Total cash managed internally	<u>13,638</u>			<u>7</u>
<u>113,757</u>	Total cash	<u>107,146</u>			<u>9</u>

17.16 Liquidity Risk

Liquidity risk is the possibility that the Fund might not have adequate cash resources available to meet its financial commitments as they fall due.

The ISC reviews its strategy on a yearly basis and where necessary takes steps to ensure that the Fund has adequate readily realisable resources to meet its financial commitments. 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 alternative investments, which are relatively illiquid, was as a result of a review of strategic asset allocation on **26 February 2014**, **24.5%** 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 illiquid investments to increase diversification, minimise risk and improve long-term investment performance.

The Fund as at 31 March 2014 had immediate access to its pension fund cash holdings held internally and externally of **£107.146m** (31 March 2013: £113.757m). These monies are primarily invested on an overnight basis on the money market.

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Officers of the Fund prepare periodic cash flow forecasts to understand and manage the timing of the Funds cash flows. The Statement of Investment Principles outlines the appropriate strategic level of cash balances that the Fund can hold. More detail can be found in the Pension Fund Annual Report and Accounts. In consultation with its institutional consultants, Hymans Robertson, the Fund is currently preparing a future cash flow forecast modelling tool which will incorporate the effects of the potential regulatory changes to the future of the scheme which is due to take effect in 2014/15.

17.17 Refinancing Risk

Refinancing risk is the risk of the Fund replenishing a significant proportion of its financial assets at a time of unfavourable interest rates. The Fund is not subject to this particular risk as it does not hold any assets that would require refinancing in the future.

17.18 Custody

In 2012 the Fund appointed Northern Trust as a global custodian, replacing the Bank of New York Mellon, with responsibility for safeguarding the assets of the Fund. As at 31 March 2014 Northern Trust had **\$5.58 trillion** of assets under custody (31 March 2013: \$5.02 trillion) and had a credit rating of **AA-** (31 March 2013: AA-). Monthly reconciliations are performed between the underlying records of the custodian and all investment managers and partnerships of the Fund.

17.19 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 ISC on a quarterly basis. The Fund makes use of the custodian's performance measurement service to monitor performance. In addition to presenting to the ISC, managers also meet with Fund officers and advisers to review progress.

17.20 Post Balance Sheet Event

As at 31 March 2014 the transfer of probation services from Probations Trusts to Community Rehabilitation Companies and National Probation Services is due to take place on 1 June 2014. As part of the transfer probation services liabilities will transfer to the Greater Manchester Pension Fund for administration by Tameside Metropolitan Borough Council.

All membership will transfer as with effect from the transfer date the liability to pay benefits or a refund of contributions under the Scheme to and in respect of these members will transfer to the Greater Manchester Pension Fund. Early calculations estimate that approximately £55m will be transferred.

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As at 31st March 2013, there were no post balance sheet events.

18. Further information

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

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