

# Public Document Pack

## Lancashire County Council

### Pension Fund Committee

Friday, 10th December, 2010 at 10.00 am in Cabinet Room 'D' - County Hall,  
Preston

### Agenda

#### Part 1 (Open to Press and Public)

No.	Item	
-----	------	--

1.	<b>Disclosure of Personal and Prejudicial Interests</b>	
----	---	--

Members are asked to consider any Personal/Prejudicial Interests they may have to disclose to the meeting in relation to matters under consideration on the Agenda.

2.	<b>Minutes of the Meeting held on 16 July 2010</b>	(Pages 1 - 8)
----	--	---------------

To be confirmed and signed by the chair.

3.	<b>Audit Commission - Annual Governance Report</b>	(Pages 9 - 34)
----	--	----------------

4.	<b>The Results of the 2010 Actuarial Valuation of the Lancashire County Pension Fund</b>	(Pages 35 - 46)
----	--	-----------------

5.	<b>Urgent Business</b>	
----	------------------------	--

An item of urgent business may only be considered under this heading where, by reason of special circumstances to be recorded in the Minutes, the Chair of the meeting is of the opinion that the item should be considered at the meeting as a matter of urgency. Wherever possible, the Chief Executive should be given advance warning of any Member's intention to raise a matter under this heading.

6.	<b>Date of Next Meeting</b>	
----	-----------------------------	--

The next meeting of the Committee will be held on Friday **4 February 2011** at 10.00 a.m. at County Hall, Preston.

Members will be aware that the subsequent meeting has been moved from 25 March 2011 to **15 April 2011** at 10.00 a.m.

7.	<b>Exclusion of Press and Public</b>	
----	--------------------------------------	--

The Committee is asked to consider whether, under Section 100A(4) of the Local Government Act, 1972, it considers that the public should be excluded from the meeting during consideration of the following items of business on the grounds that there would be a likely disclosure of exempt information as defined in the appropriate paragraph of Part 1 of Schedule 12A to the Local Government Act, 1972, as indicated against the heading to the item.

**Part II (Not open to Press and Public)**

**8. Item 8 Investment and liability strategy**

(Pages 47 - 70)

I M Fisher  
County Secretary and Solicitor

County Hall  
Preston

# Agenda Item 2

## Lancashire County Council

### Pension Fund Committee

Minutes of the meeting held on Friday 16 July 2010 at 11.30am

#### Present:-

County Councillor D Westley - Chair

#### County Councillors:

T Aldridge	H Henshaw *
M Barron	R Lawrenson
M Brindle	M Parkinson
Mrs S Charles	S Riches
F De Molfetta	G Roper
	M Welsh

\* County Councillor H Henshaw replaced County Councillor T Pimblett

#### Co-opted Members:

Councillor P Goldsworthy	Lancashire Leaders' and Chief Executives' Group
R Harvey R Whittle	Trade Union Representatives
Mr P Hyett	HE/FE Sector Establishments

#### Independent Advisers - Panel Members:

E Lambert	N Mills
-----------	---------

Apologies for absence were presented on behalf of County Councillors M France and M Green, and Councillors P Doyle and S Huggill.

#### **Pension Fund Committee – Constitution: Chair and Deputy Chair; Members and Terms of Reference**

##### **1. Resolved:**

- i. That the constitution, membership and appointment of chair and deputy chair of the committee for 2010/101 together with the committee's terms of reference, as now reported, be noted.
- ii. That Mr R Harvey, and Councillor G Bell are reappointed to serve on the Pension Fund Administration Sub-Committee for 2010/11.

- iii. That Councillor P Doyle and Mr P Hyett are re-appointed to serve on the Pension Fund Appointments Sub-Committee for 2010/11.

### **Disclosure of Personal and Prejudicial Interests**

County Councillors D Westley, M Parkinson, G Roper, and M Brindle, and Mr P Hyett and Mr R Harvey disclosed personal non-prejudicial interests in this agenda as they were members of the Local Government Pension Scheme. County Councillors M Barron, F De Molfetta and T Aldridge also disclosed personal non-prejudicial interests in this agenda as they were members of the Lancashire Combined Fire Authority.

### **Minutes of the Meeting held on 26 March 2010**

The minutes of the meeting held on 26 March 2010 were presented.

2. **Resolved:** That the minutes of the meeting held on 26 March 2010 be confirmed and signed by the chair.

### **Pension Fund Administration Sub-Committee**

The Committee considered a report on the meeting of the Pension Fund Administration Sub-Committee held on 15 June 2010.

One of the matters considered by the Sub-Committee related to the proposed procurement process for the provision of actuarial services on behalf of the Fund and it was reported that the Sub-Committee had recommended the Pension fund Committee to authorise the Appointments Sub-Committee to make the appointment:

3. **Resolved:**
  - i. That the minutes of the Pension Fund Administration Sub-Committee meeting held on 15 June 2010 be noted.
  - ii. That the Appointments Sub-Committee be authorised to make an appointment for the provision of actuarial services on behalf of the Fund.

### **Internal Audit Annual Report 2009/10**

The Committee considered the 2009/10 internal audit annual report for the Lancashire County Pension Fund.

The Head of Internal Audit introduced the report and commented on the key issues which had arisen during the audit period. The Committee's attention was particularly drawn to the work which had been undertaken to identify the overpayment of management charges in respect of the hedge fund investment. The overpayment had been recovered and controls were now in place to prevent this occurring again.

The Committee was informed that based on the internal audit work undertaken during the year, the Audit Service was able to provide substantial assurance over the internal control environment for the Pension Fund and pension administration.

**4. Resolved:**

- i. That the 2009/10 internal audit annual report for the Lancashire County Pension Fund be noted.
- ii. That the Committee place on record its appreciation of the work undertaken by the internal audit service to identify and recover the overpayment of hedge fund management charges, and that the Committee's appreciation be conveyed to the officer involved with this piece of work.

**Audit Commission -  
Lancashire Pension Fund 2009/10 Opinion Plan**

The Committee considered a report on the Audit Commission's planned approach to the audit of the financial statements of the Lancashire County Pension Fund for 2009/10. The Plan included a reduction of the planned fee for completion of the audit work.

In addition to setting out the general approach to the audit they also identified the specific risks which the Auditors had identified which would be subject to specific testing as part of the audit.

- 5. Resolved:** That the Audit Commission's plans for the opinion audits of the Lancashire County Pension Fund and the revision of the fee for the completion of the Pension Fund 2009/10 audit be noted.

**Audit Commission -  
Proposed fees for the 2010/11 audit of the Lancashire County Pension Fund**

The Committee considered a report on the proposed fees for the external audit and inspection of the Lancashire County Pension Fund for 2010/11.

The Audit Commission's fees letter set out the main elements of the proposed audit and inspection work for 2010/11 and where appropriate, highlighted any specific risks which would be reviewed as part of this work.

- 6. Resolved:** That the Audit Commission's fees letter for the audit and inspection of the Lancashire County Pension Fund for the year ending 31 March, 2011 be noted.

## **Lancashire County Pension Fund Annual Report 2009/10**

The Annual Report and Accounts of the Pension Fund for 2009/10 were presented for consideration by the Committee.

The Committee was informed that the Pension Fund Statement of Accounts had been approved by the Audit Committee on 28 June 2010 and that the Statement of Accounts was currently being audited by the Audit Commission. The Audit Commission's auditor's opinion would be included in the published Annual Report when the audit was complete.

It was noted that the County Council's Constitution required the Pension Fund Annual Report to be approved by the Committee and submitted to the Full Council for information.

Members gave detailed consideration to the Annual Report and officers responded to a number of questions. In particular, Members commented on the need for more detailed information to be provided on:

- The advice received from Pensions Investment Research Consultants and the Local Authority Pension Fund Forum in respect social, environmental and ethical issues; and
- The issue of investment managers exercising the Fund's voting rights on the Committee's behalf.

Officers noted the points raised and agreed to provide more detailed information in future.

There was a discussion about the membership of the Committee and whether all key stakeholders were adequately represented on the Committee. It was agreed that a further report would be presented to the Committee on this matter.

### **7. Resolved:**

- i. That the 2009/10 Lancashire County Pension Fund Annual Report, as now presented, be approved for submission to the Full Council.
- ii. That a report on the membership of the Committee be presented to the next meeting.

### **Report of the Treasurer to the Pension Fund – Composition and Terms of Reference of the Investment Panel**

The Committee considered a report on proposals to amend the Composition and Terms of Reference of the Investment Panel. This followed a review which had been undertaken in light of the changed approach to the procurement of advisory services to the Fund and the evolution of the

operation of the Panel following the appointment of two new independent Advisers.

**8. Resolved:** That the revised Composition and Terms of Reference of the Investment Panel, as set out at Appendix 'B', be agreed.

### **Lancashire County Pension Fund – Business Plan 2010/11 Update**

The Committee received an update on progress against the 2010/11 Business Plan.

**9. Resolved:** That the update on the 2010/11 Business Plan be noted.

### **Duties, Responsibilities and Possible Liabilities of Members of the Pension Fund Committee**

The Committee considered a report on the duties, responsibilities and possible liabilities of members of the Pension Fund Committee.

A view was expressed that Members needed to be satisfied that adequate insurance cover was in place to protect them against claims for any wrong decision. There was no specific indemnity provided by the Council as the risk to Members was considered slight, no Local Government Pension Fund member having being the subject of any action of this type to date. In practice it would be very difficult for a scheme member or tax payer to sue a Committee member and it would be more likely that any action would be taken against those organisations who appoint to the Committee. Advice had been received that whilst it was possible to obtain specific insurance cover for trustees this tended to be so full of exemptions and exclusions that it was not worth purchasing.

Officers promised to circulate a statutory guidance note issued by Communities and Local Government. Amongst other things, the note explained the different legal status of public and private sector pension schemes including the roles and responsibilities of "trustees".

**10. Resolved:** That the report be noted.

### **Pension Fund Operating Budget**

The Committee at its meeting in January 2010 considered a report on the Operating Budget for the Pension Fund. Members requested a further report on how costs had moved over time and how they were arrived at.

A further report setting out the information requested by Members was presented, together with updated forecast costs and income for 2010/11. Members noted that comparative data for the overall costs of running Pension Funds was not widely available but information secured through the Fund's Performance Measurement Advisers (WM Company) indicated that investment management fees were relatively low, while the fees for

administration were pegged to the lower quartile through a Service Level Agreement.

It was also confirmed that costs of operating the Pension Fund were reviewed by the Fund's auditors as part of their role.

**11. Resolved:** That the report be noted.

### **Urgent Business**

The Committee considered a report on the appointment of a Panel of Transition Managers. It was reported that the Chair had agreed to the matter being dealt with at this meeting to enable the Panel to be appointed as quickly as possible.

The Committee at its meeting in March 2010 agreed that a procurement exercise be undertaken to form a Panel of Transition Managers from which competitive bids would be sought for individual transactions. Members were informed that a full procurement process had been run and nine tenders had been received. All applicants had passed quality and viability checks and it was recommended that all applicants be appointed to form the Panel.

**12. Resolved:** That all applicants, as set out at Appendix 'A', be appointed to form a Panel of Transition Managers from which competitive bids will be sought for individual transactions.

### **Date of Next Meeting**

It was noted that the next meeting of the Lancashire Pension Fund Committee would be held on Friday 19 November 2010 at 10.00am at the County Hall, Preston.

It was also noted that the meeting scheduled to take place on 25 March 2011 had been rearranged and would now be held on 15 April 2011.

### **Exclusion of Press and Public**

**13. Resolved:** That the press and members of the public be excluded from the meeting during consideration of the following items of business on the grounds that there would be a likely disclosure of exempt information as defined in the paragraph of Part 1 of schedule 12A to the Local Government Act, 1972, indicated against the heading to the item. It was considered that in all the circumstances the public interest in maintaining the exemption outweighed the public interest in disclosing the information.

### **Report of the Investment Panel**

(Exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act, 1972. It was considered that in all the



circumstances of the case the public interest in maintaining the exemption outweighed the public interest in disclosing the information.)

The Committee considered a report on matters considered by the Lancashire Pension Fund Investment Panel on 19 April and 14 June 2010, and by the Strategy Sub-Group on 10 May 2010.

It was reported that the Panel had discussed a broad range of issues relating to the current state of the Fund including specific manager performance, the investment context in which the Fund was operating, the future strategy and other business plan related matters.

**14. Resolved:** That the report be noted.

I M Fisher  
County Secretary and Solicitor

County Hall  
Preston



# Agenda Item 3

## **Pension Fund Committee**

Meeting to be held on 10 December 2010

**Part I - Item No. 3**

Electoral Division affected:  
All

## **Audit Commission**

### **Lancashire Pension Fund Annual Governance Report 2009/10**

(Appendix 'A' refers)

Contact for further information: Clive Portman and Fiona Blatcher,  
01772 534990, Audit Commission

#### **Executive Summary**

The Audit Commission is required to issue an annual governance report which summarises the conclusions of its audit work. The governance report for the year ended 31 March 2010 is attached at Appendix 'A'. This report has already been considered by the Council's Audit Committee at its meeting on 27 September 2010 where it considered the contents of the report, approved the letter of representation and agreed the action plan.

#### **Recommendation**

The Committee is asked to consider the matters raised in the report.

#### **Background and Advice**

Attached at Appendix 'A' is the Audit Commission's annual governance report for the year ended 31 March 2010. The report has been produced in accordance with the Audit Commission's statutory Code of Audit Practice for Local Government bodies.

Clive Portman and Fiona Blatcher, Audit Commission, will attend the meeting to present the report and answer any questions.

#### **Consultations**

N/A

#### **Implications:**

This item has the following implications, as indicated:

**Risk management**

No significant risks have been identified.

**Local Government (Access to Information) Act 1985  
List of Background Papers**

Paper	Date	Contact/Directorate/Tel
N/A		

Reason for inclusion in Part II, if appropriate

# Annual Governance Report

Lancashire County Pension Fund

Audit 2009/10

**The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.**

**Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.**

**As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.**

# Contents

<b>Key messages</b> .....	<b>3</b>
Audit opinion .....	3
Financial statements .....	3
Internal control environment .....	3
Independence .....	4
<b>Next steps</b> .....	<b>5</b>
<b>Financial statements</b> .....	<b>6</b>
Opinion on the financial statements .....	6
FRS17 assurance .....	6
Internal control .....	6
Letter of representation .....	8
Key areas of judgement and audit risk .....	8
<b>Glossary</b> .....	<b>10</b>
<b>Appendix 1 – Draft of independent auditor's report for the Lancashire County Pension Fund's annual report</b> .....	<b>11</b>
Independent auditor's report to the Members of Lancashire County Council .....	11
<b>Appendix 2 – Independent auditor's report to Members of Lancashire County Council</b> .....	<b>14</b>
Independent auditor's report to the Members of Lancashire County Council .....	14
<b>Appendix 3 – Draft letter of representation</b> .....	<b>16</b>
Lancashire Pension Fund, Local Government Pension Scheme Audit for the year ended 31 March 2010 .....	16
<b>Appendix 4 – Action Plan</b> .....	<b>20</b>

Ladies and Gentlemen

## **2009/10 Annual Governance Report**

I am pleased to present the final version of my report on the results of my audit work for 2009/10.

I agreed a draft of the report with the Treasurer to the Pension Fund.

My report sets out the key issues that you should consider before I complete the audit.

It asks you to:

- consider the matters raised in the report before approving the financial statements (pages 6 to 9);
- approve the letter of representation on behalf of the Council before I issue my opinion and conclusion (Appendix 3); and
- agree your response to the proposed action plan (Appendix 4).

Yours faithfully

Clive Portman  
District Auditor

Date 17 September 2010



# Key messages

**This report summarises the findings from the 2009/10 audit which is substantially complete. It includes the messages arising from my audit of your financial statements.**

Financial statements	Results	Page
Unqualified audit opinion	Yes	6
Financial statements free from material error	Yes	6
Adequate internal control environment	Yes	6-8

## Audit opinion

- 1 I will issue two audit reports on the financial statements of the Pension Fund. The two reports will cover:
  - the Pension Fund's financial statements as presented in the Lancashire Pension Fund Annual Report; and
  - the Pension Fund's financial statements included within the administering authority's accounts for Lancashire County Council.
- 2 My audit of the Pension Fund financial statements is substantially complete and I expect both reports to include an unqualified audit opinion by 30 September 2010.

## Financial statements

- 3 The financial statements have been completed to a good standard and are supported by comprehensive working papers. The presentation of the financial statements has also been improved to more closely match the disclosure requirements whilst also simplifying the information presented.

## Internal control environment

- 4 Whilst I am satisfied that there is an adequate control environment in place I have made recommendations in two areas for improvement:
  - action is needed by officers to provide greater assurance over private equity investment valuations; and
  - continued effort by officers is needed to achieve effective implementation of a separate bank account for the pension fund by 1 April 2011.

## Independence

5 I can confirm that the audit has been carried out in accordance with the Audit Commission's policies on integrity, objectivity and independence.

## Next steps

**This report identifies the key messages that you should consider before I issue my opinion on the pension fund's accounts, which forms part of my report on the Council's financial statements. It includes only matters of governance interest that have come to my attention in performing my audit. My audit is not designed to identify all matters that might be relevant to you.**

**6** I ask the Audit Committee to:

- consider the matters raised in the report before approving the financial statements (pages 6 to 9);
- approve the letter of representation on behalf of the Council before I issue my opinion and conclusion (Appendix 3); and
- agree your response to the proposed action plan (Appendix 4).

# Financial statements

**The Pension Fund's accounts are important means by which the Fund accounts for its stewardship of public funds. The Council has a final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.**

## Opinion on the financial statements

**7** Subject to satisfactory clearance of outstanding matters, I plan to issue two audit reports that include my unqualified opinion on the Pension Fund financial statements.

- Appendix 1 contains a copy of my draft audit report on the financial statements included in the Pension Fund Annual Report.
- Appendix 2 contains the relevant extract of my draft audit report for Lancashire County Council's financial statements.

## FRS17 assurance

**8** In addition, as the auditor for the Local Government Pension Scheme for Lancashire, under an Audit Commission protocol, I have provided the required audit assurance to auditors of the relevant Local Government Authorities as to the FRS17 accounting entries for the accounts of their audited bodies.

## Internal control

**9** Whilst the overall control environment operated by the Lancashire Pension Fund is considered to be adequate we have identified two areas for improvement. These relate to the limited review of private equity investment valuations and the lack of a separate bank account.

**10** The pension fund has £145 million invested in private equity funds. They include investments in over 70 separate funds. Such funds are not routinely traded on an open market and are inherently difficult to value. These investments are not covered by the global custodian arrangements the pension fund has for its other investments. The investment manager does not provide a SAS70 report which would provide some external verification of their control processes and valuation methods. Whilst the pension fund has information which enables it to check the book cost of these investments, no checking has been undertaken on the market values provided by the Fund Manager.

**11** The pension fund team has already begun to act on internal audit recommendations made in June 2010 to improve the level of checking of the information provided by the private equity fund manager. More detailed information is now being supplied by the private equity fund manager to the pension fund to enable the pension fund team to review and question the movements on individual investments.

**12** In response to the valuation challenges posed by the increasing volatility of global financial markets and the increased use of unquoted investments by pension funds, the Pensions Research Accountant's Group, (PRAG) published 'Guidance on Investment Valuations' in February 2010. This document provides guidance to the preparers of financial statements on considering the valuation of investments. It provides a framework for considering the valuation of investments and some suggestions as to the due diligence enquiries the preparers of pension scheme financial statements can make to specialist valuers to make a reasonable assessment of whether the requirements of the Pension Statement of Recommended Practice, (SoRP), have been met.

## Recommendation

**R1** The Pension Fund should implement more detailed checking of the asset valuations of its private equity investments. In doing so consideration should be given to:

- suggested due diligence procedures by PRAG;
- seeking assurance via a SAS70 report on the fund managers' control and valuation processes; and
- any future changes planned for custodian arrangements and their potential impact on the private equity fund portfolio.

**13** We made recommendations last year about setting up a separate bank account for the pension fund. Effective use of a separate bank account will:

- reduce the risk of the misallocation of monies between the pension fund and the County Council;
- provide additional controls assurance through the ability to complete a separate bank reconciliation to verify the pension fund cash; and
- result in a much clearer decision making process around cash surpluses invested by the County Council on the Pension Fund's behalf.

**14** The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 require from 1st April 2011, administering authorities to maintain a separate bank account for their pension funds. Plans are in place to implement a separate bank account for the pension fund by the required date. Effective use of the bank account will require changes to the current accounting records to enable a clear separation of pension fund transactions and the development of new arrangements for bank reconciliations and the processes for agreeing the level of any surpluses to be invested by the Council on behalf of the pension fund.

15 Implementation of the bank account will also require the completion of a clear reconciliation process to agree the initial opening balance on 1 April 2010. Some progress has already been made in this regard with the completion of a reconciliation of the balance at 31 March 2010 over the last few months. Action is now needed to carry this forward to enable agreement of the opening balance at 1 April 2011.

**Recommendation**

**R2** Ensure appropriate plans and preparations are in place to meet the regulatory requirement for a separate bank account and to implement supporting processes to achieve a strengthened control environment.

**Letter of representation**

16 Before I issue my opinion, auditing standards require me to ask you and management for written representations about your financial statements and governance arrangements. Appendix 3 contains the draft letter of representation.

**Key areas of judgement and audit risk**

17 In planning my audit I identified specific risks and areas of judgement that I have considered as part of my audit.

Table 1: **Key areas of judgement and audit risk**

Issue or risk	Finding
<p>Changes in key staff</p> <p>Two new postholders have been introduced to the Pension Fund during 2009/10. These include the Treasury Management and Head of Pension Fund and the Senior Accountant for the Pension Fund. The new Senior Accountant is also on maternity leave with the pension fund financial statements now being put together by a temporary appointment. There is continuity of staffing dealing with the day to day operation of the pension fund. The changes outlined above inherently increase the risk of material error or non-compliance with accounting standards within the financial statements for the pension fund.</p>	<p>No errors have been identified within the pension fund accounts and the statements comply with accounting standards. Improvements have been made to the presentation of the accounts.</p>

Issue or risk	Finding
<p>Lack of a separate bank account</p> <p>The pension fund does not yet operate its own separate bank account. Instead all of its income and expenditure flows through the County Council's bank account. Whilst the Council's own year end bank reconciliation provides some assurance about the completeness, occurrence and accuracy of revenue transactions across both organisations when combined - there is a residual risk that monies could be misallocated between the two organisations and therefore impacting on these assertions across both organisations.</p>	<p>Pension Fund staff have completed a detailed reconciliation of pension information to the ledger balance for pension fund cash in preparation for the introduction of a separate bank account in April 2011. Review of this reconciliation has provided me with significant assurance over the pension fund cash invested in LCC as at 31 March 2010.</p>
<p>Private equity investments</p> <p>The pension fund has £145 million invested in private equity funds. They include investments in over 70 separate funds. These are not covered by the global custodian arrangements the pension fund has for its other investments. The investment manager does not provide a SAS70 report which would provide some external verification of their control processes and valuation methods. Whilst the pension fund has information which enables it to check the book cost of these investments, no checking has been undertaken on the market values provided by the Fund Manager.</p> <p>There is therefore a residual risk around the valuation of these investments.</p>	<p>We have completed sample testing of these investment values by agreeing them back to audited accounts and records held by the pension fund in relation to in year transactions. No issues have been identified.</p>
<p>Icelandic bank investment</p> <p>Early in October 2008, the Icelandic bank, Landsbanki Islands hf, collapsed. The County Council had £10m deposited with Landsbanki at that time. The pension fund's share of this investment is £2.487 million.</p>	<p>I am satisfied that an appropriate assessment of the likely impairment of this investment has been made using the latest information available.</p>

# Glossary

## **Annual governance statement**

**18** A statement of internal control prepared by an audited body and published with the financial statements.

## **Audit closure certificate**

**19** A certificate that I have completed the audit following statutory requirements. This marks the point when I have completed my responsibilities for the audit of the period covered by the certificate.

## **Audit opinion**

**20** On completion of the audit of the accounts, auditors must give their opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question;
- whether they have been prepared properly, following the relevant accounting rules; and
- for local probation boards and trusts, on the regularity of their spending and income.

## **Qualified**

**21** The auditor has some reservations or concerns.

## **Unqualified**

**22** The auditor does not have any reservations.



# Appendix 1 – Draft of independent auditor's report for the Lancashire County Pension Fund's annual report

## **Independent auditor's report to the Members of Lancashire County Council**

I have audited the Pension Fund accounting statements for the year ended 31 March 2010. The Pension Fund accounting statements comprise the Fund Account, the Net Assets Statement and the related notes. The Pension Fund accounting statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the members of Lancashire County Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 49 of the Statement of Responsibilities of Auditors and of Audited Bodies published by the Audit Commission in April 2008.

### **Respective responsibilities of the Treasurer to the Pension Fund and auditor**

The Treasurer to the Pension Fund is responsible for preparing the pension fund accounting statements, in accordance with relevant legal and regulatory requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2009: A Statement of Recommended Practice. In preparing this Pension Fund accounting statements, the Treasurer to the Pension Fund is responsible for:

- selecting suitable accounting policies and then applying them consistently;
- making judgements and estimates that were reasonable and prudent;
- keeping proper accounting records which were up to date; and
- taking reasonable steps for the prevention and detection of fraud and other irregularities.

My responsibility is to audit the Pension Fund accounting statements and related notes in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

**23** I report to you my opinion as to whether the Pension Fund accounting statements give a true and fair view, in accordance with relevant legal and regulatory requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2009: A Statement of Recommended Practice, of the financial transactions of the Pension Fund during the year and the amount and disposition of the fund's assets and liabilities, other than liabilities to pay pensions and other benefits after the end of the scheme year. I also report to you whether, in my opinion, the information which comprises the commentary on the financial performance included within the Pension Fund Annual Report, is consistent with the Pension Fund accounting statements. That information comprises the Accounts of the Fund, Administration of the Fund and Investment Policy and Performance.

I review whether the governance compliance statement published in the Pension Fund Annual Report reflects compliance with the requirements of Regulation 34(1) (e) of the Local Government Pension Scheme (Administration) Regulations 2008 and related guidance. I report if it does not meet the requirements specified by the Department of Communities and Local Government or if the statement is misleading or inconsistent with other information I am aware of from my audit of the financial statements. I am not required to consider, nor have I considered, whether the governance statement covers all risks and controls. Neither am I required to form an opinion on the effectiveness of the Authority's corporate governance procedures or its risk and control procedures.

I read other information published with the Pension Fund accounting statements and related notes and consider whether it is consistent with the audited Pension Fund accounting statements. This other information comprises the remaining elements of the Pension Fund Annual Report:

- management structure;
- overview of management and financial performance;
- actuarial valuation; and
- contacts.

I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the Pension Fund accounting statements and related notes. My responsibilities do not extend to any other information.

## **Basis of audit opinion**

I conducted my audit in accordance with the Audit Commission Act 1998, the Code of Audit Practice issued by the Audit Commission and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Pension Fund accounting statements and related notes. It also includes an assessment of the significant estimates and judgments made by the Authority in the preparation of the Pension Fund accounting statements and related notes, and of whether the accounting policies are appropriate to the Authority's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the Pension Fund accounting statements and related notes are free from material misstatement, whether caused by fraud or other irregularity or error. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the Pension Fund accounting statements and related notes.

## **Opinion**

In my opinion:

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

Clive Portman  
September 2010  
District Auditor  
Audit Commission  
2nd Floor  
Aspinall House  
Aspinall Close  
Middlebrook  
Bolton  
BL66QQ

## Appendix 2 – Independent auditor's report to Members of Lancashire County Council

Pension fund extract only

### **Independent auditor's report to the Members of Lancashire County Council**

I have audited the pension fund accounting statements for the year ended 31 March 2010 under the Audit Commission Act 1998. The pension fund accounting statements comprise the Fund Account, the Statement of Net Assets and the related notes. The pension fund accounting statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the members of Lancashire County Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 49 of the Statement of Responsibilities of Auditors and of Audited Bodies published by the Audit Commission in April 2008.

#### **Respective responsibilities of the Treasurer to the Pension Fund and auditor**

The Treasurer to the Pension Fund's responsibilities for preparing the pension fund accounting statements, in accordance with relevant legal and regulatory requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2009: A Statement of Recommended Practice are set out in the Statement of Responsibilities for the Statement of Accounts.

My responsibility is to audit the pension fund accounting statements and related notes in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the pension fund accounting statements give a true and fair view, in accordance with relevant legal and regulatory requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2009: A Statement of Recommended Practice, of the financial transactions of the pension fund during the year and the amount and disposition of the fund's assets and liabilities, other than liabilities to pay pensions and other benefits after the end of the scheme year.

I read other information published with the pension fund accounting statements and related notes and consider whether it is consistent with the audited pension fund accounting statements. This other information comprises the Explanatory Foreword. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the pension fund accounting statements and related notes. My responsibilities do not extend to any other information.

### **Basis of audit opinion**

I conducted my audit in accordance with the Audit Commission Act 1998, the Code of Audit Practice issued by the Audit Commission and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the pension fund accounts and related notes. It also includes an assessment of the significant estimates and judgments made by the Authority in the preparation of the pension fund accounting statements and related notes, and of whether the accounting policies are appropriate to the Authority's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the pension fund accounts and related notes are free from material misstatement, whether caused by fraud or other irregularity or error. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the pension fund accounting statements and related notes.

### **Opinion**

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

End of extract

## Appendix 3 – Draft letter of representation

Mr C Portman  
District Auditor  
Audit Commission  
2nd Floor Aspinall House,  
Aspinall Close,  
Middlebrook,  
Horwich,  
Bolton, BL6 6QQ

Dear Mr Portman

### **Lancashire Pension Fund, Local Government Pension Scheme Audit for the year ended 31 March 2010**

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of Lancashire Pension Fund and Lancashire County Council, the following representations given to you in connection with your audit of the Pension Fund's financial statements for the year ended 31 March 2010. All representations cover the Pension Fund accounts included within the Council's financial statements.

#### **Compliance with the statutory authorities**

I acknowledge my responsibility to you under the relevant statutory authorities and in accordance with the Code of Practice for Local Authority Accounting in the United Kingdom: A Statement of Recommended Practice 2009 and in accordance with the Statement of Recommended Practice for financial reports of Pension Schemes, which give a true and fair view of the financial position and financial performance of the Pension Fund, and for making accurate representations to you.

#### **Supporting records**

All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the Pension Fund have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all Pension Fund committee meetings, have been made available to you.

## **Irregularities**

I acknowledge my responsibility for the design and implementation of internal control systems to prevent and detect fraud or error.

There have been no:

- irregularities involving management or employees who have significant roles in the system of internal accounting control;
- irregularities involving other employees that could have a material effect on the financial statements; or
- communications from regulatory agencies concerning non-compliance with, or deficiencies on, financial reporting practices which could have a material effect on the financial statements.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements; and
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

## **Law, regulations, contractual arrangements and codes of practice**

There are no instances of non-compliance with laws, regulations and codes of practice, likely to have a significant effect on the finances or operations of the Pension Fund.

In all material respects, the funds recognised in the financial statements have been applied to purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

The Pension Fund has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance. There has been no non-compliance with requirements of regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.

## **Fair Values**

I confirm the reasonableness of the significant assumptions within the financial statements. For fair values of assets and liabilities I confirm:

- the appropriateness of the measurement method;
- the completeness and appropriateness under the financial reporting framework; and
- subsequent events do not require adjustment to the fair value measurement.

## **Assets**

The following have been properly recorded and, where appropriate, adequately disclosed in the financial statements:

- losses arising from sale and purchase commitments;
- agreements and options to buy back assets previously sold; and
- assets pledged as collateral.

## **Compensating arrangements**

There are no formal or informal compensating balancing arrangements with any of our cash and investment accounts. We have no other lines of credit arrangements.

There is no co-mingling of the Pension Fund bank balances, deposits and investments with the Council's money.

## **Contingent liabilities**

There are no other contingent liabilities, other than those that have been properly recorded and disclosed in the financial statements. In particular:

- there is no significant pending or threatened litigation, other than those already disclosed in the financial statements;
- there are no material commitments or contractual issues, other than those already disclosed in the financial statements; and
- no financial guarantees have been given to third parties.

## **Related party transactions**

I confirm the completeness of the information disclosed regarding the identification of related parties.

The identity of, and balances and transactions with, related parties have been properly recorded and where appropriate, adequately disclosed in the financial statements.

## **Post balance sheet events**

Since the date of approval of the financial statements by the Council, no additional significant post balance sheet events that have occurred which would require additional adjustment or disclosure in the financial statements.

The Pension Fund has no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.



I confirm that this letter will be discussed with the Audit Committee on 27 September 2010.

Signed

Name: Phil Halsall

Position: Executive Director of Resources

Date

## Appendix 4 – Action Plan

### Recommendations

#### Recommendation 1

The Pension Fund should implement more detailed checking of the asset valuations of its private equity investments. In doing so consideration should be given to:

- suggested due diligence procedures by PRAG;
- seeking assurance via a SAS70 report on the fund managers' control and valuation processes; and
- any future changes planned for custodian arrangements and their potential impact on the private equity fund portfolio.

<b>Responsibility</b>	Mike Jenson
<b>Priority</b>	3
<b>Date</b>	June 2011
<b>Comments</b>	<p>The Private Equity fund manager produces valuations of investments based on latest quarterly accounts received. In accordance with PRAG suggestions, the Pension Fund will review the valuations received by reference to annual audited fund accounts, checking valuation bases, audit reports, draw-downs and distributions.</p> <p>The Pension Fund will continue to seek assurance over the manager's control and valuation processes via a SAS70 report and to consider the implications of any change in custodian arrangements.</p>

#### Recommendation 2

Ensure appropriate plans and preparations are in place to meet the regulatory requirement for a separate bank account and to implement supporting processes to achieve a strengthened control environment.

<b>Responsibility</b>	Mike Jenson
<b>Priority</b>	3
<b>Date</b>	Ongoing
<b>Comments</b>	A project management team is in place to ensure that a separate pension fund bank account is up and running by 1 April 2011.

If you require a copy of this document in an alternative format or in a language other than English, please call:  
**0844 798 7070**

© Audit Commission 2010.

Design and production by the Audit Commission Publishing Team.

Image copyright © Audit Commission.

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors, members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
- any third party.



Audit Commission

1st Floor  
Millbank Tower  
Millbank  
London  
SW1P 4HQ

Telephone: 0844 798 3131

Fax: 0844 798 2945

Textphone (minicom): 0844 798 2946

[www.audit-commission.gov.uk](http://www.audit-commission.gov.uk)

September 2010



# Agenda Item 4

## Pension Fund Committee

Meeting to be held on 10 December 2010

**Part I – Item No. 4**

Electoral Division affected:  
All

## The results of the 2010 Actuarial Valuation of the Lancashire County Pension Fund (Appendix A refers)

Contact for further information:

Diane Lister, (01772) 534827, Resources Directorate

[Diane.lister@lancashire.gov.uk](mailto:Diane.lister@lancashire.gov.uk)

### Executive Summary

This report sets out the results of the 2010 Actuarial Valuation of the Lancashire County Pension Fund.

### Recommendation

The Committee is asked to note the results of the 2010 Actuarial Valuation of the Lancashire County Pension Fund.

### Background and Advice

The triennial Valuation of the assets and liabilities of the Lancashire County Pension Fund as at 31 March 2010 has been carried out by the Fund Actuary, Mercer. The results of the Valuation, including amendments to individual employer contribution rates, will be effective from 1 April 2011.

A detailed report of the results is attached at Appendix 'A' and this will be presented by the Actuary at the meeting.

The previous Valuation (effective from 1 April 2008) revealed a funding position of 84% and an average employer contribution rate of 17.8%. The 2010 Valuation has revealed a funding level of 80% and an average employer contribution rate of 19.4% which is a small worsening of the previous position. This result is largely due to the unfavourable changes in market conditions over the period but this has been offset to some extent by the impact of revised demographic assumptions adopted by the Actuary for the 2010 Valuation.

Individual employer contribution rates and the options available to mitigate the impact of increased contributions will be presented to Fund employers at a Briefing to be held at County Hall on 14 December 2010.

The formal Actuarial Valuation Report as at 31 March 2010 is expected to be available by 31 March 2011. A copy of the Report will be sent to all members of the Pension Fund Committee.

**Consultations**

N/A

**Implications:**

**Risk management**

See Appendix 'A'

**Local Government (Access to Information) Act 1985**

**List of Background Papers**

Paper	Date	Contact/Directorate/Ext
-------	------	-------------------------

N/A

Reason for inclusion in Part II, if appropriate

N/A

## Lancashire County Pension Fund

### Actuarial Valuation as at 31 March 2010

This paper sets out the preliminary results of the 2010 valuation for the whole Fund. The next step will be to determine contribution rates for the individual employers and begin the employer consultation process, although some further discussions may be required in relation to individual employers' circumstances before all the rates can be finalised.

#### Funding Strategy

The results have been based on the following key funding principles, which we would be happy to discuss further:

- The allowance for asset out-performance above gilt yields when assessing the past service funding position has been retained at the same level as the 2007 valuation.
- In determining an appropriate inflation assumption, on which to base pension increases and salary growth, an allowance for an inflation risk premium of 0.3% p.a. has been introduced. In addition, an allowance of 0.5% has been made for the change to CPI linking of pension increases (as announced in the Government's emergency budget in June). Our assumption for future pension increases (CPI) is therefore 0.8% per annum below the market implied level of RPI inflation as at 31 March 2010.
- The real salary growth assumption has been reduced by 0.25% p.a., from 1.75% p.a. above RPI as at the 2007 actuarial valuation to 1.5% p.a. above RPI at the 2010 actuarial valuation. For presentational purposes we propose to show the assumption as being 2% p.a. over and above CPI.
- The assumptions for life expectancy (including allowance for future improvements in longevity), proportions married and ill-health retirement have been revised based on the conclusions emerging from a study which we carried out for the Lancashire Fund.
- The results in this paper are based on the deficit being recovered over the remainder of the 22 year recovery period adopted at the 2007 valuation i.e. 19 years. However, consideration has also been given to allowing employers to adopt a longer recovery period (no more than 25 years) in order to achieve some increased stability of contribution rates. The results of these calculations (at a whole Fund level) are detailed in the sensitivities section.

## Data

The membership data as at 31 March 2010 used for the valuation calculations, as supplied by the Fund, is summarised briefly as follows:

	Number	Annual Salaries/Pensions (£000s)
Pensionable employees	50,595	847,620
Preserved Pensioners	39,547	43,067
Current pensioners (including spouses and dependant pensioners)	36,269	146,373

### Notes:

1. Annual salaries include actual amounts for part-time employees.
2. Preserved pensioners include frozen refunds and leaver options pending.

The Fund asset value used is the market value notified to us of £3,962 million.

### Benefits and Contributions

The benefits valued are based on the LGPS (Benefits, Membership and Contributions) Regulations 2007 (as amended) which became effective from 1 April 2008. As mentioned, allowance has been made for the change to CPI linking of pension increases which will come into effect from 1 April 2011. No allowance has been made in the calculations for any potential changes to the LGPS which may arise from the report of the Hutton Commission, as the extent and timing of any such changes has not yet been determined.

### Method and Assumptions

As in previous valuations, the actuarial method adopted is the projected unit method which implicitly allows for new entrants.

The actuarial assumptions used are summarised in Appendix A. We would draw attention to the following points:

- The assumed asset out-performance over and above gilts is unchanged from the 2007 actuarial valuation at 2.5% p.a. pre-retirement and 1.0% p.a. post-retirement.
- As mentioned above, the assumed rate of long-term earnings growth is 2.0% p.a. above CPI (compared with 1.75% p.a. above RPI at the 2007 actuarial valuation).



- An "inflation adjustment" of 0.8% per annum has been included to reflect the introduction of an inflation risk premium since 2007, and also a change to CPI linking of pension increases.
- Despite the falls in the index-linked gilt yield market of 0.7% per annum between 2007 and 2010, the effect of the "inflation adjustment" means that the overall strength of the financial basis for determining the value of the past service liabilities has decreased slightly (giving rise to slightly lower liabilities).
- The financial basis for future service has been maintained at the same real levels i.e. 3.75% above price inflation to reflect the long term approach (as opposed to full market yields approach) adopted for determining the future service assumption.
- The revised mortality assumption allows for greater life expectancy than in 2007 due to a greater allowance for future improvements in longevity. This has served therefore to increase the value of the liabilities (and also the future service contribution rate). However, the revised assumptions for proportions married and ill-health retirement have served to offset this increase and therefore overall, the revised demographic assumptions serve to reduce both the value of the past service liabilities and also the required future service contribution rate.

## Results

The past service results are as follows:

	£m
Assets	3,962
Liabilities	
- Pensionable employees	2,220
- Preserved pensioners	614
- Current pensioners	2,121
Total	4,955
Surplus (Deficit)	(993)
Funding level	80%

The funding level of 80% is a small worsening from the 84% funding level as at the 2007 valuation. The largest impact has been due to the unfavourable changes in market conditions over the period (lower than expected investment returns and higher than expected liabilities), but this has been offset to some extent by the impact of the inflation adjustment, the revised demographic assumptions adopted, and other elements of favourable experience. An analysis of this can be seen in Appendix B.

The results for future service are as follows:

Contribution rate for:	% of Pensionable Pay
▪ Pension and death-in-service benefits	18.5
▪ Administrative expenses	0.4
Total contribution rate	18.9
Average employee contribution rate	6.4
Common Contribution Rate	12.5

The Common Contribution Rate identified at the previous valuation was 13.3% of Pensionable Pay. The decrease in the rate is largely due the favourable impact overall of the changes in demographic assumptions as a result of our analysis.

If the deficit of £993 million is spread over 19 years (the remainder of the 2007 recovery plan) then the addition required to the contribution rate would be 6.9% of Pensionable Pay. The average target employer contribution rate would therefore be 19.4% of Pensionable Pay. This compares to 17.8% at the 2007 valuation, an increase of 1.6% of Pensionable Pay.

The above contribution rates are average ones across the whole of the Fund, and the impact on individual employers will vary significantly, particularly for the smaller employers.

### Sensitivity of Results

For information, we set out below the impact on the provisional whole Fund results of changing some of the key assumptions, as follows:

- Increasing the past service pre-retirement asset out-performance allowance (AOA) by 0.5% p.a.
- Using a deficit recovery period of 25 years instead of 19.
- Increasing the real salary inflation assumption (for past and future service) by 0.25% p.a.
- Adjusting the mortality assumption by assuming that life expectancy increases by approximately by 1 year.

The impact on the target average employer contribution rate for each item is shown below (all contribution rates are percentages of Pensionable Pay for ease of comparison). By way of background, the long-term target contribution rate emerging from the 2007 actuarial valuation was 17.8% of Pensionable Pay).

	<b>Funding level</b>	<b>Common Contribution Rate</b>	<b>Past service additional rate*</b>	<b>Target average employer rate</b>
		<b>% p.a.</b>	<b>% p.a.</b>	<b>% p.a.</b>
Base results	80%	12.5	6.9	19.4
Increase pre-retirement past service AOA by 0.5%	83%	12.5	5.7	18.2
Adopting a recovery period of 25 years	80%	12.5	5.4	17.9
Increase real salary inflation by 0.25%	79%	13.1	7.3	20.4
Increase in life expectancy of 1 year	78%	12.8	7.5	20.3

\*to be expressed as increasing lump sum contributions

It can be seen from the above that some relatively small changes in actuarial assumptions and/or deficit recovery period can help to achieve some increased stability in contribution rates at a whole Fund level.

#### **Increased Investment Return Allowance**

At the 2007 actuarial valuation, when assessing the individual employer contributions payable under the recovery plan, the same assumptions as those used to calculate the funding target were adopted with the exception that, for certain employers, the required contributions were adjusted to allow for an increased investment return (IIR) assumption on existing assets and future contributions during the period of the recovery plan.

The effect of the IIR is to reduce the required total contribution input from employers over the deficit recovery period. Effectively, the higher level of returns being assumed is used to subsidise the contributions that would otherwise be certified (subject to the minimum contribution levels mentioned below).

Overall, an effective return as at the 2007 valuation date of 7.4% p.a. was allowed reflecting the underlying investment strategy of the scheme and, in particular, including the assets of the scheme that underlie the pensioner as well as the non-pensioner liabilities. This return represented an overall asset out-performance assumption (AoA) of 3.0% p.a. relative to gilt returns. Overall the average IIR contribution offset across the eligible fund employers at the 2007 valuation was of the order of 2.8% of payroll.

Key features of this IIR approach are:

- The overall effective return to be used (the IIR) needs to be reconsidered and determined as at the 2010 valuation date. This should reflect the long term investment strategy of the Fund, and be consistent with the funding target assumptions used for the valuation, and market conditions at the valuation date.
- The investment return assumed for the contributions under the recovery plan is taken to apply throughout the recovery period. As a result, any change in investment strategy which would act to reduce the expected future investment returns could invalidate these assumptions and therefore the funding strategy.
- The variation to assumptions in relation to the recovery plan can only be applied for those employers which the Administering Authority deems to be of sufficiently high covenant to support the anticipation of investment returns, based on the current investment strategy, over the entire duration of the recovery period.
- No such variation in the assumptions can apply in any case to any employer which does not have a funding deficit at the valuation (and therefore for which no recovery plan is applicable).
- The resultant total contribution rates implemented following the 2007 valuation were also subject to a minimum of both:
  - the contribution rates originally planned for 2008/09 onwards based on the 2004 actuarial valuation, and
  - the normal future service contribution rate for the employer concerned.

The equivalent minimum contribution underpins would again be applied in allowing the IIR offset to contributions at the 2010 valuation.

It is proposed again to allow for those employers of sufficiently high covenant to adopt an AoA of up to 3.0% during the period of the recovery plan. This allowance is, however, still subject to confirmation pending finalisation of some details in connection with the investment strategy of the Fund and its expected return characteristics. For illustration purposes, adopting the same higher 3.0% AoA and IIR model as for the 2007 valuation would reduce the average contribution rate across all employers by about 3-4% of pensionable pay. This is before applying the underpins referred to in the previous paragraph.

A higher level of IIR (than the 3.0% AoA illustrated above) would increase the potential offset effect, and vice versa. However, as referred to above, any level of IIR to be adopted

must be justified by analysis of the long term investment return expectations that can be supported by the Fund's investment strategy going forward.

### **Conclusion and Next Steps**

Whilst the results and assumptions outlined in this paper and appendices have been discussed with Fund Officers, we would be happy to discuss these with the Committee as required in order that the principles can be agreed. If the valuation principles as set out in this paper and Appendix A are acceptable, then we will proceed to determine contribution rates for each of the employers.

*This paper is addressed to the Administering Authority only on the understanding that:*

- *its observations and conclusions are based on fund information provided by third parties. No representation or warranty, express or implied, is made or given by Mercer as to the accuracy or completeness of the information obtained from non-Mercer sources. Whilst reasonable attempts have been made by Mercer to ensure that the information and data has been obtained from reliable and up-to-date sources, Mercer has not conducted any verification as to whether the information and data from third party sources is true, accurate or complete. Mercer accepts no responsibility or liability (including for indirect, consequential or incidental damages) for any error, omission or inaccuracy in such information.*
- *No person other than the Administering Authority may use or rely on this paper without Mercer's prior written consent. Mercer does not owe a duty of care or other liability in respect of this paper to any person other than the Administering Authority nor does Mercer accept liability of the Administering Authority if the paper is used for any purpose other than that stated.*

*This paper contains actuarial advice and forms a component report on the actuarial valuation as at 31 March 2010.*

*"Technical Actuarial Standard R: Reporting Actuarial Information" and "Technical Actuarial Standard D: Data" issued by the Board for Actuarial Standards also apply to this paper and it complies with their requirements where relevant.*

## Lancashire County Pension Fund

### Summary of key assumptions used for calculating preliminary whole Fund valuation results as at 31 March 2010

<b>Long-term gilt yields</b>	
Fixed interest	4.5% p.a.
Index linked	0.7% p.a.
Market Implied RPI price inflation	3.8% p.a.
Inflation Adjustment	(0.8%) p.a.
Implied CPI price inflation	3.0% p.a.
<b>Past service financial assumptions</b>	
Pre-retirement investment return	7.0% p.a.
Post-retirement investment return	5.5% p.a.
Salary increases	5.0% p.a.
Pension increases	3.0% p.a.
<b>Future service financial assumptions</b>	
Investment return	6.75% p.a.
CPI price inflation	3.0% p.a.
Salary increases	5.0% p.a.
Pension increases	3.0% p.a.
<b>Demographic assumptions</b>	
Non-retired members' mortality	Based on SAPS P & D tables with CMI [1%] future improvements (+3 for ill health retirees)
Retired members' mortality	Based on SAPS P & D tables with CMI [1%] future improvements (+3 for ill health retirees)
Proportions Married	Based on analysis of LGPS experience
Ill-Health Retirement	Based on analysis of LGPS experience
Other demographics	As for 2007 valuation

**Lancashire County Pension Fund**

**Whole Fund Valuation Results as at 31 March 2010**

**Analysis of movement in past service funding position**

<b>Analysis</b>	<b>£m</b>
Deficit as at 31 March 2007	(710)
Investment Gain/(Loss) versus valuation assumption	(671)
Change in market "real" yields	(422)
CPI/IRP/earnings increase assumption	529
Revision of demographic assumptions	131
Effect of deficit contributions and other miscellaneous member movements	150
Deficit as at 31 March 2010	(993)

Section 4

INVESTMENT PORTFOLIO

As of 12/31/2010

Assets of the Fund

Asset	Value
U.S. Government Securities	100.00
U.S. Corporate Bonds	100.00
U.S. High Yield Bonds	100.00
U.S. Equity	100.00
U.S. International Equity	100.00
U.S. Real Estate	100.00
U.S. Commodity	100.00
U.S. Alternative	100.00
U.S. Cash	100.00



# Agenda Item 8

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A of the Local Government Act 1972. It is considered that all the circumstances of the case the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

Document is Restricted



By virtue of paragraph(s) 3 of Part 1 of Schedule 12A of the Local Government Act 1972. It is considered that all the circumstances of the case the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

Document is Restricted



By virtue of paragraph(s) 3 of Part 1 of Schedule 12A of the Local Government Act 1972. It is considered that all the circumstances of the case the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

**Document is Restricted**



By virtue of paragraph(s) 3 of Part 1 of Schedule 12A of the Local Government Act 1972. It is considered that all the circumstances of the case the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

**Document is Restricted**

