

## MEETING OF THE PENSION FUND PANEL

23 FEBRUARY 2018

### REPORT OF THE SERVICE DIRECTOR - FINANCE

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#### 1. External audit of Northumberland County Council Pension Fund 2017/2018 accounts – Planning Report

##### Purpose of the report

The purpose of this report is to provide information about the external auditors' Planning Report for the 2017/2018 Northumberland County Council Pension Fund audit. EY will present the Planning Report at the meeting.

##### Recommendation

**The Panel is requested to accept the report.**

##### Key issues

- 1.1 Ernst & Young LLP (trading as EY) was appointed as external auditor to NCC with effect from 2015/2016, replacing Deloitte. Northumberland County Council Pension Fund's annual report and accounts is audited separately from Northumberland County Council's accounts. This means that the external auditors must sign a separate ("consistent with") audit opinion for the Fund's Financial Statements, and provide separate Planning and Final reports for the Fund.
- 1.2 The auditors use the phrase "those charged with governance (TCWG) of the Fund" to encompass the different ways administering authorities can delegate their responsibilities for the LGPS. In NCC, the governance of the Fund's financial statements is within the remit of the Pension Fund Panel, the Audit Committee and the Section 151 Officer. Therefore, the auditors present the Planning and Final reports each year to both the Panel and the Northumberland County Council Audit Committee.
- 1.3 Due to the implementation of new statutory guidelines for earlier publication of NCC's accounts (which the Fund accounts form part of), the auditors will now attend the February and June quarterly meetings of the Pension Fund Panel each year to present their Planning and Final reports to members.
- 1.4 EY's Audit Plan year ending 31 March 2018 for the Fund was not finalised in time to enclose with these papers so will be **tabled** at the meeting. Claire Mellons (Senior Audit Manager) will attend this meeting of the Pension Fund Panel to present the Audit Plan to the Panel.

## 1. External audit of Northumberland County Council Pension Fund 2017/2018 accounts – Planning Report

### BACKGROUND

- 1.5 Northumberland County Council Pension Fund is part of Northumberland County Council. The Pension Fund is **not** a separate **legal** entity, and as such, the financial statements of the Fund form part of the Northumberland County Council's annual report and accounts, and a separate audit of the Fund's accounts would not normally be required.
- 1.6 However, there is a requirement in England and Wales for local authorities administering the LGPS to produce a pension fund annual report (paragraph 57 of the Local Government Pension Scheme Regulations 2013, SI 2013 no. 2356), and therefore the auditors treat the Fund as a separate **reporting** entity. The equivalent regulation contained in the Local Government Pension Scheme Regulations (Administration) 2008 was first applied to the 2008/2009 financial statements.
- 1.7 For the 2017/2018 audit of the Pension Fund financial statements, Northumberland County Council's external auditor, Ernst & Young LLP (trading as EY), has prepared a (separate) Audit Plan. EY's Audit Plan was not finalised in time to enclose with these papers so will be **tabled** at the meeting.
- 1.8 Claire Mellons (Senior Audit Manager) of EY will attend this meeting to present the 2017/2018 Planning Report to the Panel.
- 1.9 Under the 2013 regulations the Pension Fund annual report for the year ended 31 March 2018 must be published before **1 December 2018**. The Fund accounts cannot be finalised prior to the completion of the audit of the County Council's accounts. As the audit opinion on the County Council accounts must be signed by 31 July 2018, it makes logistical sense to also have the Pension Fund accounts signed at the same time, and this approach was taken in previous years and will be taken again in 2018.
- 1.10 Therefore, the Pension Fund accounts will be signed at the Audit Committee meeting scheduled on 25 July 2018. EY will also attend the 22 June 2018 Panel meeting to report the audit findings in the audit Final Report.
- 1.11 The audit Planning and Final Reports are addressed to "those charged with governance" of the Pension Fund. Therefore, for Northumberland, it is appropriate that these reports are taken to the Northumberland County Council Audit Committee, as well as the Pension Fund Panel. The Planning Report will be taken to the Audit Committee meeting on 28 March 2018, and the Final Report will be taken to the 25 July 2018 Audit Committee.
- 1.12 The audit opinion included in the Pension Fund accounts is a "consistent with" opinion, because the "true and fair view of the financial position" opinion (which auditors are required to give) is included in Northumberland County Council's full Financial Statements.
- 1.13 The main part of the 2017/2018 audit work will be undertaken over spring and summer 2018.

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### 2. General Data Protection Regulation (GDPR)

#### Purpose of the report

This report provides an update to the Panel about the implications for NCC, as LGPS administering authority, of the General Data Protection Regulation (GDPR), which will take effect from 25 May 2018.

#### Recommendation

**The Panel is requested to accept the report.**

#### Key issues

- 2.1 The Panel received a report at the 24 November 2017 meeting, explaining the implications of GDPR. GDPR builds on the principles established by the Data Protection Act 1998 and raises the levels of personal data security and privacy protections across all data processors and controllers. GDPR compliance cannot be achieved quickly. There will be significant lead-in times required for ICT development, process development, risk assessment and staff training. The full implications of GDPR for the LGPS are still being worked through by national organisations, including the Local Government Pensions Committee (LGPC).
- 2.2 Implementation of the shared LGPS administration service between NCC and Tyne and Wear Pension Fund (TWPF) in January does not remove NCC's responsibilities under GDPR: for shared administration, NCC and TWPF are **joint data controllers** for LGPS data, and TWPF is also a data processor for NCC's LGPS data. NCC is also data controller for the other LGPS administration functions it has retained.
- 2.3 On 20 November 2017, the LGPS Secretariat circulated an opinion from the legal firm Squire Patton Boggs regarding some of the implications of GDPR for the LGPS. This advice is attached as **Appendix 1** to this report. Further advice and template information has been commissioned from Squire Patton Boggs, to be published in March 2018.
- 2.4 There remains a good deal more development to be done before 25 May 2018 for NCC, and for all LGPS administering authorities and scheme employers to be GDPR compliant. However, the early advice obtained from Squire Patton Boggs (at Appendix 1) indicates that, if implemented appropriately, the more onerous *potential* implications of GDPR legislation (such as obtaining **consent** for use of personal data) will **not be required** for LGPS processing. Further reports will be brought to the Panel to report progress on implementing GDPR.

## 2. General Data Protection Regulation (GDPR)

### BACKGROUND

#### GDPR in force from 25 May 2018

2.5 On 25 May 2018, the EU's General Data Protection Regulation (GDPR) comes into force containing new standards for the protection of individuals' personal data. The change will impact on the way pensions schemes can lawfully collect, use, retain and share information. GDPR applies to organisations that handle the personal data of EU residents and will replace the UK's Data Protection Act 1998 (DPA). Although it is EU legislation, UK organisations will still need to apply it, and after Brexit the UK is likely to adopt its own legislation to align with GDPR.

#### Implications of GDPR

2.6 A report on the implications of GDPR for NCC Pension Fund, in general terms, was brought to the Panel in November 2017. At that stage, there remained a lot of development work to be done at national level, so it was not possible to be specific about the full implications.

2.7 In summary, implementation of GDPR has the following implications:

- the scale of the financial penalties for non-compliance is much greater than under the DPA;
- authorities must create and maintain records of all personal data processing activities, to be presented to the Information Commissioner's Office (ICO) on demand;
- authorities must review and assess the adequacy of their data security measures in place, and use encryption where appropriate;
- authorities must review and update all relevant third party service and data sharing contracts to ensure GDPR compliance;
- authorities must revise privacy notices and consider whether member consent is required, though it is likely that authorities will be able to rely on the "performance of a legal obligation" exemption;
- authorities must establish (or update) their breaches management processes so that relevant breaches can be reported within 72 hours of becoming aware of the breach;
- authorities must appoint a Data Protection Officer (DPO);
- authorities must ensure processes are in place to cater for new individual rights, particularly the right to have personal data deleted; and
- authorities should consider whether to carry out a Data Protection Impact Assessment (DPIA).

2.8 The definition of personal data is wider under GDPR than under DPA. Personal data means any information about an individual where that person can be identified directly or indirectly from the data.

2.9 GDPR brings with it not just the need to comply with the new requirements, but also the need to **demonstrate** compliance, if requested by the ICO. The intention of GDPR is to raise the levels of personal data security and privacy protections across the board.

## National developments

2.10 The full implications of GDPR for the LGPS are still being worked through by national organisations, such as the Local Government Pensions Committee (LGPC, part of the Local Government Association). The LGPC July 2017 bulletin states:

*“We are aware that GDPR is an area that is getting increased attention across the LGPS and there are a number of crucial questions where there are different views, in particular:*

- a) the implications of GDPR for LGPS funds, and*
- b) the work that needs to be undertaken to ensure administering authorities are fully compliant by the time GDPR comes into force.*

*In general, we recommend that LGPS administering authorities which form part of a local authority discuss and become involved in the local authority’s broader project for the implementation of GDPR. However, at a national level, plans are also in place to help funds with their GDPR responsibilities:*

- a number of funds have joined together to form a GDPR group. The group, in consultation with the communications working group, plan to produced sample documentation for use by LGPS funds, and*
- the LGPC Secretariat will also be seeking a legal view on a number of specific questions that have been raised about GDPR in respect of the LGPS.*

*All information will be circulated to funds via the mailing list as and when this is available.”*

2.11 Tyne and Wear Pension Fund (TWPF) is represented on the LGPC Communications Working Group, and the GDPR Group (referred to in paragraph 2.10, above) is a subcommittee of that Group. Therefore, officers within TWPF are keeping up to date as LGPC guidance on GDPR is developed.

2.12 The LGPC has commissioned advice from Squire Patton Boggs on a number of questions regarding the implications of GDPR for the LGPS. On 20 November 2017, LGPC circulated advice to LGPS administering authorities, which is attached as **Appendix 1**. The advice given includes:

- **consent:** in most circumstances consent for the processing of personal data to carry out basic administration of the LGPS is not required, because the processing is necessary for compliance with a legal obligation;
- **holding data where the LGPS fund no longer has a liability** for a member (for example, because the member opted out and received a refund): in most circumstances it would be acceptable to continue to hold data but the administering authority should keep market practice in relation to retention under review;
- **members’ right to erasure in respect of personal data held:** the administering authority would not be obliged to erase data needed for the administration of the scheme;
- **privacy by design:** this should not impact on the communications sent to members where there is a reasonable justification for including personal data in those communications; and

- **data controller:** the administering authority is a data controller and the employing authority is a data controller of the personal data it passes to the administering authority.
- 2.13 Squire Patton Boggs notes in its advice (at Appendix 1) that guidance from the ICO is awaited for a number of issues and that further development is required.
- 2.14 The LGPC, on behalf of LGPS administering authorities, has recently commissioned Squire Patton Boggs to produce the following documents:
- template privacy statements for LGPS administering authorities to use or adapt;
  - a detailed privacy notice, taking into account that the data will be obtained directly from both the employer and the member, to be published on the administering authority's website;
  - a summary privacy notice for use in newsletters, annual benefit statements etc.; and
  - a memorandum of understanding for employers setting out the data which participating employers in the LGPS can share with the LGPS administering authority without a data sharing agreement in place, quoting the relevant statutory references to inform an employer's data protection officer.
- These documents will be published in March 2018.

#### NCC Pension Fund's position

- 2.15 NCC's LGPS administration became part of the shared service with TWPF from the end of January 2018. NCC and TWPF are **joint data controllers** for NCC's LGPS function, following implementation of the shared administration service. The majority of NCC's obligations under GDPR as joint data controller will be discharged by TWPF, but NCC will retain some responsibility.
- 2.16 TWPF is a data processor for NCC and, under GDPR, the data controller may still remain liable for any breach of the law by the processor.
- 2.17 NCC appointed Fay Cooper as DPO late in 2017. Clare Gorman has kept Fay Cooper and NCC's Legal Team informed as the shared administration service for the LGPS was being implemented.
- 2.18 The letters which were sent out to all NCC Pension Fund's LGPS members in January to inform them of the start of the shared administration service made appropriate reference to the requirements of GDPR.
- 2.19 In carrying out the LGPS data processing functions (including those that will remain with NCC following implementation of shared services, such as the collection of contributions) officers must ensure they act in accordance with NCC's Information and Governance Framework, which is under development.

#### Privacy Impact Risk Assessment

- 2.20 A Privacy Impact Risk Assessment will be completed and shared with the DPO for NCC's LGPS administration function before the start of the shared administration service with TWPF.

### Third party contracts

- 2.21 Certain third party contracts will need to be updated to ensure they are GDPR compliant before May 2018. This includes the contract with the Fund's actuary, Aon Hewitt, and the Fund's AVC providers.
- 2.22 Aon Hewitt has indicated that it is not currently in a position to update the contract with NCC, but it has given assurances that it will issue a response to the new legislation early in 2018. Similarly, Prudential (the Fund's AVC provider) has indicated that its legal team is currently considering how the contract will be changed to ensure GDPR compliance.

### TWPF's data cleansing processes

- 2.23 TWPF is anticipating an increased focus on data cleansing and tracing missing members, as a result of GDPR. TWPF conducts a check on "common data" (as defined by the Pensions Regulator) in February each year, and this will include NCC's LGPS data from 2018. TWPF is also developing reports to check the "scheme specific data" during 2018, which will also be applied to NCC's LGPS data.

### Data retention policies

- 2.24 GDPR will require authorities to analyse the data they hold and consider the reasons for holding it and whether the authority has the right to hold it. This applies to data that is held on the authority's behalf. Data should only be retained when there is a legitimate reason.
- 2.25 Therefore, authorities will need to conduct an analysis of the data held, to ensure it is being retained no longer than necessary.
- 2.26 Pension schemes require data to be kept for a long time, and the advent of the LGPS 2014, a career average scheme, means that payroll data should be retained by employers for much longer than the standard retention period (which follows HMRC guidance and/or statute of limitations), and longer than was required under the LGPS 2008, a final salary scheme.
- 2.27 NCC will work with TWPF and the participating LGPS employers to provide guidance on data retention requirements.

### Next steps

- 2.28 GDPR compliance cannot be achieved quickly. There will be significant lead-in times required for ICT development, process development, risk assessment and staff training.
- 2.29 Clare Gorman will attend the TWPF biannual training event for the TWPF Pensions Committee and Board at the end of February. One of the topics to be covered is GDPR. Clare will work with Paul Cooper, Communications Manager at TWPF, to agree processes and responsibilities of both parties to the shared administration agreement, to prevent any GDPR requirement being missed.

2.30 Further reports will be brought to the Panel to update on progress made to implement the requirements of GDPR. Further LGPC guidance to administering authorities, when issued, will be brought to the Panel.

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### 3. Meeting with the Pensions Regulator held in December 2017

#### Purpose of the report

This report provides information to the Panel about the meeting of the Pensions Regulator (tPR) with representatives of the four North East LGPS funds held on 21 December 2017 at Durham County Council.

#### Recommendation

**The Panel is requested to accept the report.**

#### Key issues

- 3.1 A meeting took place on **21 December 2017**, at County Hall, Durham, for representatives of the four LGPS funds in the North East to meet tPR. Officers, Committee, Panel and Board members from the four funds were invited to attend.
- 3.2 This was the first event of this type held for North East funds and was well attended by a full range of representatives. The event was chaired by Gerard Moore, the Chair of NCC's LGPS Board.
  - Board members and an officer attended representing Durham.
  - Board members and officers attended representing Northumberland.
  - Committee and Board members and officers attended representing Tyne and Wear.
  - A Board member and the third party administrator attended representing Teesside.
- 3.3 Neil Wilson (standing in for Rebecca Woodley, Industry Liaison Manager) of tPR gave a presentation at the meeting, and was asked to cover:
  - tPR's next focus for public sector schemes;
  - implementation of GDPR;
  - cyber security;
  - practical steps for cleansing common and scheme specific data; and
  - what is and what is *not* of material significance to the Regulator.
- 3.4 Overall, the tone of meeting was positive and interactive, with all represented groups making contributions. Neil stated that it was difficult to envisage circumstances where a Board member could be held liable in the performance of his/her role, and that tPR's primary focus was to *support* Boards in their work.
- 3.5 Gerard Moore is taking part in an informal meeting with tPR, on 22 February, at which the effectiveness of a series of meetings of tPR and LGPS funds will be discussed. Gerard hopes to provide verbal feedback to the Panel at this meeting.



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### 4. Implementation of the Markets in Financial Instruments Directive (MiFID II)

#### Purpose of the report

This report updates members on the client status categorisations (MiFID II) confirmed by financial services providers for the services and promotions obtained by NCC, in its capacity as LGPS administering authority for NCC Pension Fund.

#### Recommendation

**The Panel is requested to accept the report**

#### Key issues

- 4.1 The Panel has received reports over the last year about the potential impact of MiFID II on investments held and financial services obtained by Northumberland County Council Pension Fund (NCCPF). Prior to 3 January 2018, LGPS administering authorities were *automatically* categorised as “**per se professional**” clients in respect of MiFID and non-MiFID scope business, enabling them to invest in a full range of asset classes. From 3 January 2018, administering authorities are given “**retail**” client status by default, unless they complete an opt up process to achieve “**elective professional**” status.
- 4.2 To achieve elective professional client status, NCC (in its capacity as LGPS administering authority) formally applied to its existing fund managers, custodian and investment advisers to be opted up, providing information to complete a standard template questionnaire for opt up, developed by the LGPS Scheme Advisory Board. Professional client status is achieved for each financial service provider only when the institution provides formal confirmation to NCCPF.
- 4.3 A status update for each financial institution showing the stage reached in the opt up process was provided by email to Panel and Board members late in December 2017, immediately before MiFID II’s implementation. This showed all necessary opt up confirmations had been received. The status update is a “live document” which can change, for example when opt up is required for a (new to NCC) fund manager to discuss a product with officers, where there is an element of service promotion in the discussions. The latest status update for MiFID II is attached as **Appendix 2**. A status update will be brought to the Panel at least annually from now on.
- 4.4 Authorities are not required to renew elections on a regular basis but will be required to review the information provided in the opt up process and notify all financial services firms of **any changes** in circumstances which **could affect their status**. Examples of relevant changes include pensions committee membership changes resulting in significant loss of experience, and terminating the relationship with the authority’s investment adviser.



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#### 5. Outcomes of the December 2017 meeting of the NCC LGPS Local Pension Board

##### Purpose of the report

This report provides information to the Panel about outcomes and proposals from the meeting of NCC's LGPS Local Pension Board held on 11 December 2017.

##### Recommendation

The Panel is requested to:

- (i) accept the proposals from the Local Pension Board meeting held on 11 December 2017, as set out in Appendix 3; and
- (ii) note the assurances gained by the Board at that meeting.

##### Key issues

- 5.1 The NCC LGPS Local Pension Board must meet at least twice a year, though in practice, it is now meeting four times a year. As set out in the remit of the Pension Fund Panel the Panel's functions include ensuring the proper administration of the Local Government Pension Scheme and the "*Board provides oversight of the governance and administration of the LGPS.*"
- 5.2 Since its first meeting in July 2015, the Board has made a number of recommendations to the scheme manager for changes to the LGPS administration arrangements. A formal mechanism for communicating Board proposals, to the next Panel meeting via a Report of the Board Chair, was adopted in September 2017, so all relevant Board meeting outcomes would be captured and considered by Panel as a separate agenda item.
- 5.3 The Report of the Board Chair, covering the outcomes of the Board meeting held on 11 December 2017, is attached as **Appendix 3** to this report. The Chair of the Board will provide further information about those outcomes at this meeting of the Panel.
- 5.4 Members should note that 11 December 2017 Board recommendations were all for officers to implement, and they have been adopted/will be adopted in the future.



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#### 6. Formal measurement of the performance of the investment adviser

##### Purpose of the report

The purpose of this report is to inform Panel members of the requirement to formally assess the performance of the Pension Fund Panel investment adviser in the year to 31 March 2018, and to enclose a “scorecard” for use in this process.

##### Recommendation

**The Panel is requested to accept the report.**

##### Key issues

- 6.1 The CIPFA guidance on decision making in the LGPS effectively recommends that pension committees should formally assess the performance of the investment adviser periodically.
- 6.2 The sixth such formal assessment of Mercer (the Fund’s investment adviser) took place a year ago, using a “scorecard” approach. Annual assessment is appropriate, and therefore the formal assessment for the work undertaken by Mercer in the year to 31 March 2018 is now due.
- 6.3 A scorecard, in the same format as last year’s is **enclosed** with these papers (**Enclosure 1**). Each Panel member and observer is asked to complete the scorecard enclosed with the Panel papers and return it to Craig Johnson before 6 April 2018. Page 1 of the scorecard lists the work undertaken by Mercer on the Fund’s behalf during 2017/2018.
- 6.4 The completed scorecards will be summarised and reported to the June 2018 Panel meeting, and feedback given to the adviser.

## 6. Formal measurement of the performance of the investment adviser

### BACKGROUND

#### CIPFA guidance on the formal assessment of the adviser

6.5 CIPFA (The Chartered Institute of Public Finance and Accountancy) issued a publication on 11 December 2009 called *Investment Decision-Making in the Local Government Pension Scheme: A Guide to the Application of the Myners Principles*.

6.6 **Principle 4** shown on **page 19** of CIPFA's investment decision-making guidance says:

*Arrangements should be in place for the formal measurement of the performance of the investments, investment managers and advisers. Administering authorities should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.*

#### Formal process followed

6.7 At the February 2011 Pension Fund Panel meeting, a formal process was agreed, using a "scorecard" approach similar to the standard version prepared by Pensions and Lifetime Savings Association (then the National Association of Pension Funds), amended to suit Northumberland County Council Pension Fund's requirements.

6.8 Given that the relationship with the adviser is expected to be for the medium to long-term, it was agreed that assessment should be carried out no more frequently than annually.

6.9 Each Panel member and observer is asked to complete a scorecard to cover the work undertaken by the adviser during the twelve months to 31 March of the year assessed, and the results are collated by officers and reported to the next Panel meeting. Feedback of the Panel's views is also given to the adviser. Panel members **can complete the scorecard anonymously**.

#### Formal assessment for work undertaken in the year to 31 March 2018

6.10 The investment adviser, Mercer, was selected and appointed by the Panel in March 2009, so has now been in place for nine years, during which time the adviser has undertaken significant projects on the Fund's behalf, such as the strategy and manager reviews. The adviser also provides on-going monitoring of the incumbent fund managers, which is an important risk control for the Fund.

6.11 The specific adviser assigned to the Northumberland County Council account during 2017/2018 was Joanne Holden, with Iain Campbell and Susan Greenwood (replacing Iain) as support. Catrina Arbuckle was the "alternate" standing in when Joanne was unavailable to attend a meeting.

- 6.12 A scorecard, in the same format as last year's, has been **enclosed** with these papers, i.e. **Enclosure 1**. Panel members and observers are asked to complete the scorecards and return them to Craig Johnson before 6 April 2018.
- 6.13 As an *aide memoire* the scorecard shows, on **page 1**, the range of work undertaken by Mercer on the Fund's behalf during 2017/2018.
- 6.14 The completed scorecards will be summarised and reported to the June 2018 meeting, and feedback given to the adviser.



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### 7. Formal assessment of the effectiveness of the Pension Fund Panel

#### Purpose of the report

This report is to inform Panel members of the requirement to formally assess the effectiveness of the Pension Fund Panel as a decision making body, and seeks approval for the drafted formal assessment attached as Appendix 4.

#### Recommendation

**The Panel is requested to approve the formal assessment of the Pension Fund Panel as a decision making body, as set out in Appendix 4.**

#### Key issues

- 7.1 The CIPFA guidance on decision making in the LGPS effectively recommends that a pension committee should assess its own effectiveness as a decision-making body, periodically, and report on this to Scheme members.
- 7.2 Annual assessment is appropriate, and the formal assessment for the work undertaken by the Panel in the year to 31 March 2018 is now due.
- 7.3 The significant work undertaken by the Panel in 2017/2018 includes:
- active participation in the development and establishment of the Border to Coast Pensions Partnership **pooling** arrangement;
  - implementation of **shared pensions administration** services with Tyne and Wear Pension Fund;
  - approval of NCC Pension Fund's **revised** Investment Strategy, Administration Strategy, Communications Policy, and Governance Policy and Compliance Statements, and **first** Administering Authority Discretions Policy; and
  - consideration of and approval given to enable NCC, as LGPS administering authority, to opt up to professional client status with financial institutions prior to **MiFID II** taking effect in January 2018.
- The NCC LGPS Local Pension Board and the Panel have **worked together** to maximise the benefit to the Fund of the current governance arrangements.
- 7.4 A formal assessment of decisions made (to date) has been drafted and attached as **Appendix 4** to this report. Members are asked to consider this assessment and make suggestions for changes if appropriate. The approach taken when drafting the assessment was to consider the 'controls' in place to help prevent poor decisions being made. The formal assessment will be included in the Pension Fund annual report and accounts for 2017/2018.

## 7. Formal assessment of the effectiveness of the Pension Fund Panel

### BACKGROUND

#### CIPFA guidance

7.5 CIPFA (The Chartered Institute of Public Finance and Accountancy) issued a publication on 11 December 2009 called *Investment Decision-Making in the Local Government Pension Scheme: A Guide to the Application of the Myners Principles*.

7.6 **Principle 4** shown on **page 19** of CIPFA's investment decision-making guidance says:

*Arrangements should be in place for the formal measurement of the performance of the investments, investment managers and advisers. Administering authorities should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.*

7.7 This guidance goes on to suggest issues to consider for decision-making bodies such as the Pension Fund Panel:

*The process of self-assessment involves both officers and members of the committee reviewing a range of items, including manager selection, asset allocation decisions, benchmarking decisions, employment of consultants and best value outcomes.*

*The objective of the reviews would be to consider whether outcomes were as anticipated, were appropriate, or could have been improved.*

*The committee should set out its expectations of its own performance in its business plan. This could include expected progress on certain matters, reviews of governance and performance and attendance targets. It should include standards relating to the administration of the committee's business such as:*

- *attainment of standards set down in CIPFA's knowledge and skills framework*
- *achievement of required training outcomes*
- *achievement of administrative targets such as target dates for issuing agendas and minutes.*

*This assessment should be included in the fund's annual report to its stakeholders.*

#### Formal assessment of the effectiveness of the Panel - process

7.8 The first step in assessing the decisions made was to consider the backdrop of events and changes in the year in which those decisions were made. This was the approach taken when the first formal assessment took place in February 2011 to assess the effectiveness of the Pension Fund Panel as a decision-making body, and it has been followed each year since then.

- 7.9 The current Panel members and Chair and Vice Chair of the Panel were appointed following the May 2017 local elections. Whilst two of the Panel members (Councillors Watson and Bawn) had served the previous Council term as Panel members, and two others (Councillors Kennedy and Swithenbank) had served in earlier Council terms, it is appropriate, for the 2017/2018 assessment, to consider the decisions made in the Council year 2017/2018. A summary of the decisions made by the Pension Fund Panel is presented to full Council in May each year, in any event, but it cannot be completed and brought to this (February) meeting.
- 7.10 When considering the effectiveness of decisions made, members are asked to consider whether the outcomes of decisions were as anticipated, were appropriate, or could have been improved.

#### Judging decisions made

- 7.11 Attempting to assess decisions made, after the event, is beset by problems. For example, if a decision is taken to allocate assets to corporate bonds shortly before corporate bonds fall in value, with the benefit of hindsight this decision would be judged to have been poor. However the decision may have been made based on the best available evidence at the time, and if judged **at the time** it was made would have been judged as good.
- 7.12 Another problem is the timescale applied to judge success or failure of a decision. For example, an active manager selected by the Panel may outperform its index in the first year of appointment and the decision to appoint would be judged a success, but if it then goes on to underperform over a three year period, is the decision now judged to be a failure? If it then goes on to outperform over a five year period, is the decision then a success?
- 7.13 Given the fact that pension fund investment is for the long term, there are strong arguments in favour of only measuring the success or failure of a decision after a long period of time, such as ten years. The make-up of the decision-making body is **very** likely to have changed in that time which means that the Panel would be judged on the decisions taken by a completely separate group of people.
- 7.14 Another problem for assessing decisions is that many of the decisions made by the Panel are not empirically or objectively measurable. For example, the decision to appoint the investment adviser cannot be measured objectively, as it is not possible to judge which of the decisions made subsequently by the Panel may have been made differently if another adviser had been selected instead.
- 7.15 The quality of the decisions made by the Panel with the input of the adviser depends greatly on the relationship, trust and understanding built up between the two, and this relationship can only be measured subjectively by the parties involved.

#### Assessing the effectiveness of the Panel

- 7.16 The guidance requires an assessment, and therefore a formal assessment has been drafted and attached as **Appendix 4** to this report. It has been purposefully kept short and succinct. Members are asked to consider this and make suggestions for changes if appropriate.

- 7.17 The approach taken when drafting the assessment was to consider the ‘controls’ in place to help prevent poor decisions being made. For example, one of the key ‘controls’ would be the presence of the adviser at each meeting to ensure that Panel decisions made comply with the LGPS and other regulations, coupled with the meetings being conducted in a manner to allow the adviser time and opportunity to give his/her advice.
- 7.18 The formal assessment considers the areas which help support the Panel in making effective decisions, such as the **continuity** of Panel membership. Continuity is recognised as being of vital importance as it takes time for Panel members to build up the knowledge and expertise necessary to feel confident in making decisions.
- 7.19 This assessment, once approved, should be reported to stakeholders; therefore it will be included in the Pension Fund annual report and accounts for 2017/2018 and published on the NCC website.

#### Matters considered in the year 2017/2018

- 7.20 The main substantive piece of work undertaken by the Panel in 2017/2018 was the active participation in the development and establishment of the Border to Coast Pensions Partnership (BCPP) pooling arrangement, including participation in the BCPP Joint Committee.
- 7.21 The list below is a reminder of some of the matters considered in 2017/2018:
- active participation in the development and establishment of the Border to Coast Pensions Partnership pooling arrangement;
  - implementation of shared pensions administration services with Tyne and Wear Pension Fund;
  - consideration and approval of NCC Pension Fund’s
    - revised Investment Strategy Statement,
    - revised Administration Strategy,
    - revised Communications Policy,
    - revised Governance Policy and Compliance Statement, and
    - first Administering Authority Discretions Policy;
  - consideration of and approval given to enable NCC, as LGPS administering authority, to opt up to professional client status with financial institutions prior to MiFID II taking effect in January 2018;
  - introduction of a formal Training Needs Analysis for all Panel and Board members;
  - consideration of further joint working with pooling partners;
  - review of Pension Fund accounts and external audit planning and results;
  - review of quarterly fund manager performance and impact of currency hedging; and
  - consideration of GDPR and the potential implications for the Fund.
- 7.22 The NCC LGPS Local Pension Board and the Panel have worked together to maximise the benefit to the Fund of the current governance arrangements.

## MEETING OF THE PENSION FUND PANEL

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#### 8. NCC Pension Fund's Objectives

This report seeks Panel approval for the Statement of NCC Pension Fund's Objectives, as set out in Appendix 5 attached to this report.

#### Recommendation

**The Panel is requested to approve the Statement of NCC Pension Fund's Objectives attached as Appendix 5 to this report.**

#### Key issues

- 8.1 To comply with LGPS Regulations, the Pensions Regulator's code of practice and other related guidance, NCC already has policies in place relating to LGPS governance, funding strategy, pension administration, communications and investment strategy. All such policies require the Fund to **set objectives**, and a **Statement of Objectives** for the Fund, collating all stated objectives within the Fund's policy statements in one document, was approved by the Panel in February 2016. Periodic review of the Fund's Statement of Objectives is appropriate.
- 8.2 Policies relating to **governance** and **administration** were updated in November 2017 by the Panel, as part of the preparation and alignment required for the efficiency of the shared administration service with South Tyneside Council. The policy relating to **communication** has been updated and brought to this meeting of the Panel for approval. Members should note that in adopting a format to align with Tyne and Wear Pension Fund's Administration Strategy, Northumberland County Council Pension Fund's Administration Strategy no longer **sets out** the objectives in the statement, but the objectives remain valid and the principles espoused are incorporated in the Fund's Strategy.
- 8.3 A review of the Fund's objectives indicates that they remain appropriate following implementation of the shared administration service with South Tyneside Council. The only change made to the Statement of Objectives already in place is to replace the name of the Department for Communities and Local Government (DCLG) with the Ministry of Housing, Communities and Local Government (MHCLG). This report seeks approval from the Panel to approve the Fund's Statement of Objectives, attached as **Appendix 5** to this report. The purpose of this report is to consider the objectives contained in the Fund's policies and seek Panel approval for the Statement of Objectives.

## 8. NCC Pension Fund's Objectives

### BACKGROUND

#### LGPS regulatory requirements

- 8.4 The Local Government Pension Scheme (LGPS) Regulations require administering authorities to have in place and **maintain** certain policy statements relating to the LGPS pension fund in place. The policy statements required by LGPS Regulations 2013 are:
- Regulation 55: governance compliance statement;
  - Regulation 58: funding strategy statement;
  - Regulation 59: administration strategy; and
  - Regulation 61: statement of policy concerning communications with members and Scheme employers.
- 8.5 The Fund has all of these policies in place, as well as an Investment Strategy Statement (ISS) as required by the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. The requirement for administering authorities to prepare their first ISS by 31 March 2017 replaced the requirement to prepare and maintain a Statement of Investment Principles (SIP). The ISS covers the same information as the SIP, with nuanced differences in the requirements, and a requirement to set out the Fund's approach to pooling.
- 8.6 All of the above noted policy statements require the Fund to set objectives.

#### Northumberland County Council Pension Fund objectives

- 8.7 A statement showing all the current **Fund objectives** is attached as **Appendix 5** to this report. The purpose of this statement (at Appendix 5) is to collate the objectives contained within the various policy statements in one succinct document. The intention is that a Fund Objectives Statement is maintained and updated every time there is a change to one of the policies which involves a change to an objective.
- 8.8 The Fund Objectives Statement was first approved by the Panel in February 2016, and both the Fund's Governance Compliance Statement and its Administration Strategy have been reviewed and changed in 2017. At this meeting, the Panel is being asked to approve changes to the Communication Strategy, so it is appropriate to review the Fund objectives at this stage.
- 8.9 It should be noted that the objectives relating to **governance, communications and administration** are straightforward and closely follow the requirements set out in the LGPS Regulations and the Pensions Regulator's code of practice number 14 "*Governance and administration of public service pension schemes*". In contrast, the objectives relating to **funding and investments** (though also prescribed, to some extent, in the LGPS Regulations) are less straightforward and **subject to judgement**.
- 8.10 Therefore, it is appropriate that the objectives are reconsidered periodically by the Pension Fund Panel, and the purpose of this report is to seek Panel approval for the Fund objectives, as set out in Appendix 5.

- 8.11 Note that the Fund's policies relating to **governance** and **administration** were updated in November 2017, to reflect changes which would take place following implementation of the shared administration service with South Tyneside Council in January 2018. The *objectives* relating to **governance** were not changed when the compliance statement was reviewed and approved by the Panel on 3 November 2017. The *objectives* relating to **administration** were **followed** in the revised strategy (also reviewed and approved on 3 November 2017) but, to align with the Tyne and Wear Pension Fund format, are no longer **set out** in the statement.
- 8.12 The objectives relating to **communications** have been carried forward unchanged into the revised policy which has been brought to this meeting of the Panel for consideration.
- 8.13 The funding and investment objectives, as set out in Appendix 5 are:
- 8.13.1 To comply with Regulation 62 of the 2013 Regulations and specifically to set employer contributions at an appropriate level to ensure the Fund's solvency while taking account of the desirability of maintaining as nearly a constant contribution rate as possible and the long-term cost-efficiency of the Fund;
- 8.13.2 To ensure that the Fund has sufficient resources available to meet all liabilities as they fall due;
- 8.13.3 To manage employers' liabilities effectively and minimise any unrecoverable deficit from an employer exit. (This means ensuring that the Fund is not exposed to undue risk in relation to individual employers by setting appropriate funding targets and recovery plans relative to the features of each employer);
- 8.13.4 To aspire to a funding ratio for the Fund, as measured at triennial valuations, remaining within the middle range of LGPS Funds in terms of its relative position on a standardised funding basis or other measure as set out by the Scheme Advisory Board / MHCLG. To ensure that, should the Fund's relative position fall towards the bottom quartile, action is taken with the aim of restoring the position but also to ensure it does not fall below that level;
- 8.13.5 To achieve a long term return on the Fund's assets which:
- ensures that, together with employer and member contributions, the Fund can meet its long term liabilities;
  - aims to maximise returns within acceptable risk parameters; and
- 8.13.6 To ensure that the degree of funding and investment risk for individual employers takes into account:
- the administering authority's view of the likelihood of their exit leaving unmet liabilities; and
  - affordability constraints.

- 8.14 The first three objectives and the sixth (at 8.13.1, 8.13.2, 8.13.3 and 8.13.6) appear in NCC's Funding Strategy Statement (FSS) and are managed by the administering authority and the Fund actuary, though there is a cross over with the Fund's investment risk and returns.
- 8.15 The fourth objective (at 8.13.4) was added to the Fund objectives before the 2016 valuation was carried out, specifically so that Panel members could consider whether this wording reflected their views.
- 8.16 The fifth objective (at 8.13.5) is included in the Fund's ISS and has been drafted to allow flexibility for the Panel to set and change the Fund's asset allocation.

#### Statement of Objectives update

- 8.17 All of the Fund's objectives remain appropriate following implementation of the shared administration service with South Tyneside Council; therefore, the only change made to the Objectives Statement is to update the title for the LGPS Responsible Authority from the Department for Communities and Local Government (DCLG) to Ministry of Housing, Communities and Local Government (MHCLG).
- 8.18 The Panel is requested to approve the Statement of Objectives attached as **Appendix 5** to this report.

#### Review of Statement of Objectives

- 8.19 The Fund's Statement of Objectives will be reviewed periodically, including when any of the related policy statements or strategy documents are revised.

## MEETING OF THE PENSION FUND PANEL

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### REPORT OF THE SERVICE DIRECTOR - FINANCE

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#### 9. NCC Pension Fund's Communication Strategy Statement

This report seeks Panel approval for a revised and updated NCC LGPS Communication Strategy Statement, to be tabled at the meeting.

#### Recommendation

**The Panel is requested to approve the revised NCC LGPS Communication Strategy Statement, to be tabled at the meeting.**

#### Key issues

- 9.1 The Pension Fund Panel first approved a Communication Strategy Statement for NCC Pension Fund in 2006, to comply with a (then) newly introduced LGPS regulatory requirement. Regulation 61 of the LGPS Regulations 2013 has since replaced the original regulatory requirement.
- 9.2 With advice from Aon Hewitt, the Communication Strategy Statement was revised with effect from 1 January 2016, and only minor changes have been made since then. Implementation of the shared administration service with South Tyneside Council (STC) from January 2018 requires significant revision of the Fund's Communication Strategy to reflect the new working arrangements. The majority of the Fund's contact with LGPS members and participating employers will now be delivered by STC in the shared administration service. At the time of finalising this report, work (with STC) on the revised NCC Communication Strategy had not been completed. Therefore, the revised Communication Strategy will be tabled at the meeting.
- 9.3 There is no legal requirement to consult on the Communication Strategy, but it is best practice to do so, therefore, once approved by the Panel, the Statement will be sent to all participating employers and the relevant trades unions for consultation. The Statement will be updated every three years or sooner, if necessary.

## 9. NCC Pension Fund's Communication Strategy Statement

### BACKGROUND

#### LGPS regulatory requirement

- 9.4 The Local Government Pension Scheme Regulations 2013 (SI 2013 No. 2356) contain the following Regulation:

***“Statements of policy concerning communications with members and Scheme employers***

**61.** —(1) *An administering authority must prepare, maintain and publish a written statement setting out its policy concerning communications with—*

- (a) members;*
- (b) representatives of members;*
- (c) prospective members; and*
- (d) Scheme employers.*

*(2) In particular the statement must set out its policy on—*

- (a) the provision of information and publicity about the Scheme to members, representatives of members and Scheme employers;*
- (b) the format, frequency and method of distributing such information or publicity; and*
- (c) the promotion of the Scheme to prospective members and their employers.*

*(3) The statement must be revised and published by the administering authority following a material change in their policy on any of the matters referred to in paragraph (2).”*

- 9.5 The Local Government Pension Scheme (Amendment) (No 2) Regulations 2005 contained an identical requirement, with the first policy to be published by 1 April 2006. Therefore, NCC Pension Fund's first Communication Strategy Statement was approved by the Pension Fund Panel in February 2006, and regularly undated thereafter.

- 9.6 With advice taken from Aon Hewitt in 2015, the Strategy was revised with the most notable changes being the addition of:
- the role of the LGPS Local Pension Board; and
  - a formal way of measuring success of the communication objectives. (i.e. the effectiveness of the communication).

- 9.7 Significant revisions are now required to set out the implications of the new working arrangements following implementation of the shared administration service with South Tyneside Council.

- 9.8 At the time of finalising this report, work (with STC) on the revised NCC Communication Strategy had not been completed. Therefore, the revised Communication Strategy will be tabled at the meeting and Panel approval sought.
- 9.9 Once approved, the Statement will then be sent to all participating employers and the relevant trades unions for consultation.
- 9.10 There is no legal requirement to consult on the Communication Strategy Statement, but it is best practice to do so.
- 9.11 Once finalised, the Strategy will be published on NCC's website.
- 9.12 The Communication Strategy Statement will be updated every three years or sooner, if necessary.



## MEETING OF THE PENSION FUND PANEL

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### REPORT OF THE SERVICE DIRECTOR - FINANCE

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#### 10. Action Plan 2018 for NCC Pension Fund

##### Purpose of the report

The purpose of this report is to:

- provide the NCC Pension Fund Action Plan 2018 for members' consideration and approval; and
- monitor progress made against the Action Plan 2017.

##### Recommendation

**The Panel is requested to approve the Fund's proposed Action Plan 2018 attached as Appendix 6, and review progress made against the Fund's Action Plan 2017, attached as Appendix 7.**

##### Key issues

- 10.1 In March 2017, an **Action Plan 2017** for the Fund was approved by the Panel (under a delegation). At the Panel's request, the Fund now has an annual Action Plan instead of an annual Business Plan because the Action Plan is a shorter, more succinct document, which was seen as more user friendly.
- 10.2 The Action Plan is updated annually and brought to the Panel for approval at the beginning of each year. The **Action Plan 2018** is attached as **Appendix 6** to this report. The progress made to date, against the Action Plan 2017, is set out in **Appendix 7**.
- 10.3 The **Action Plan 2018** follows the same format as earlier plans, shown under four headings:
- A** Specific items to be considered/actioned by the Panel in 2017/18;
  - B** Reviews to be undertaken by the Panel in 2017/18 and beyond;
  - C** Quarterly meetings – agenda items: usual pattern; and
  - D** Past reviews carried out by the Panel.
- Its purpose is **not** to set a rigid framework that cannot be deviated from, but instead just to set out current expectations of future actions.
- 10.4 The Action Plan 2018 is intended to act as a checklist and progress monitoring tool for one-off and regular items to be brought to the Pension Fund Panel in the next year and beyond.
- 10.5 An article published recently in Pensions Age is attached as **Appendix 8** to this report. This sets out Aon Hewitt's view of the key challenges facing LGPS funds in 2018.



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### REPORT OF THE SERVICE DIRECTOR - FINANCE

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#### 11. Reports on internal controls operated by fund managers and the custodian

##### Purpose of the report

The purpose of this report is to provide information to the Panel about the most recently available internal control reports provided by Northumberland County Council Pension Fund's custodian and its investment managers.

##### Recommendation

**The Panel is requested to accept the report.**

##### Key issues

- 11.1 Internal control reports, known as ISAE 3402, AAF 01/06, or an equivalent, are prepared at least annually by the Fund's custodian and fund managers, to describe the internal controls each has in place to protect the interests of clients.
- 11.2 ISAE 3402 (International Standards for Assurance Engagements) and AAF 01/06 (Audit and Assurance Faculty) are frameworks for assurance reports on the internal controls of service organisations. Both are issued by the Institute of Chartered Accountants in England and Wales. They provide guidance to fund managers and custodians on reporting internal controls to clients. The internal control report is independently verified by an accountant who tests the internal controls described in the reports.
- 11.3 The purpose of the internal control report is to provide comfort to clients and their auditors on the security of assets held by custodians and managed by fund managers. It is produced on a voluntary basis, and all of Northumberland County Council Pension Fund's managers and custodian have provided a report or a suitable substitute.
- 11.4 The most up to date reports available have been obtained and reviewed by officers. The reporting accountants noted no significant control weakness, except for the Schroders' report, where the auditors gave a qualified opinion in respect of one control tested. The report details Schroders' management response which sets out new procedures to be implemented to prevent recurrence of that control weakness.
- 11.5 The Fund's external auditors (EY) review the most recent internal control reports as part of their year-end audit work, as well as the Pension Fund Panel meeting minutes, which show that the control assurance reports have been reviewed by officers and reported (annually) to the Panel.

## 11. Reports on internal controls operated by fund managers and the custodian

### BACKGROUND

- 11.6 ISAE 3402, AAF 01/06, and SSAE16 (i.e. the US equivalent of AAF 01/06) reports are obtained by the Pensions Accounting Team from the fund managers and custodian, normally on an annual basis, though sometimes more frequently. The above are all frameworks through which a report is prepared by the fund manager, or custodian, describing the control environment and control objectives for UK managed clients, and the policies and procedures established to meet these objectives. It is produced for third parties (i.e. clients) to provide assurance on the control environment operated by the service provider. The report also contains the opinion of the reporting accountant who has tested the internal controls described in the report. AAF 01/06 replaced the previous guidance for reporting accountants contained in FRAG 21. SSAE16 stands for Standards of Attestation Engagements number 16, and this replaced SAS 70 reports.
- 11.7 The internal control report is intended to provide comfort to clients and their auditors regarding the security of assets held by custodians and managed by fund managers, in a consistent reporting standard. AAF 01/06 (**Audit and Assurance Faculty**) and ISAE 3402 (**International Standards for Assurance Engagements**) internal controls reports are both produced under the guidance issued by the Institute of Chartered Accountants in England and Wales. This guidance is for both directors and reporting accountants and recommends that the report covers certain key controls. The internal control report is the responsibility of the directors of the entity reported on.
- 11.8 There is no legal obligation on fund managers or custodians to provide an internal control report, however, all of the managers that manage the Northumberland Fund and the Fund's custodian have provided one, or a suitable substitute.
- 11.9 Prior to preparing this report, officers requested the most recent internal control reports from the Fund's custodian, its managers and each managers' own custodian. The internal control reports received are as follows:
- Assurance Report on Internal Controls for the year ended 31 December 2016 for **Legal & General** Investment Management (Holdings) Limited, plus PMC Custody of Assets Briefing Note (not a control report), providing a position statement as at April 2015 (the latest statement currently available to Legal and General), relating to Legal & General's custodian;
  - Internal Controls Report for the year ended 31 December 2016, for **Schroder** Investment Management Limited;
  - Report on Internal Controls for the year ended 30 September 2016 for **BlackRock**;
  - Report on the Suitability of the Design and Operating Effectiveness of Controls as of 30 September 2016, for **Morgan Stanley**;
  - Service Organization Control (SOC) 1 Report for the period 1 January 2016 to 31 December 2016 for **NB Alternatives** Investments;

- Internal Controls of the Investment Management Activities for the year ended 31 October 2016 for **Wellington**;
- Internal Controls of the Investment Management Activities for the year to 31 December 2016 for **Antin**;
- Controls Placed in Operation Relating to Investment Advisory and Management Activities for the year to 30 September 2017 for **Pantheon**;
- Custody and Fund Services – Service Organisation Control Report for the year ended 30 September 2017 for **Northern Trust**.

11.10 **GIP** does not have an AAF 01/06, ISAE 3402 or equivalent report, but has sent a report from its custodian, J.P. Morgan, on the Suitability of the Design and Operating Effectiveness of its Controls, referring to its internal controls for the six months to 30 September 2016.

11.11 With the exception of Schrodgers, for the reports listed above, the reporting accountants noted no significant control weakness. However, in the Internal Controls Report for the year ended 31 December 2016, for **Schroder** Investment Management Limited, the auditors gave a qualified opinion. The service auditors assurance report states

*“For the period from 1 January 2016 to 31 December 2016, management did not consistently provide evidence to demonstrate the independent review performed by authorised personnel of client reports for accuracy, completeness and compliance with client and portfolio requirements prior to dispatch. As a result, we were not able to conclude that the control was operating effectively to achieve the objective “Client reporting in respect of portfolio transactions, holdings and performance, commission and voting is complete and accurate and provided within required timescales” during this period.”*

11.12 The Schrodgers internal control report 2016 sets out that for 5 out of a sample of 90 client reports there was no evidence of review prior to dispatch. The response from Schrodgers outlined that management had:

- performed a review to confirm that no errors had been made in those client reports where the review was not evidenced.
- undertaken a process review in January 2017 to identify and implement control enhancements to ensure that the review of client reports was evidenced in the future.

Officers have reviewed the management response and made further enquiries with Schrodgers. It appears that Schrodgers’ management has responded quickly and appropriately to the service auditor’s findings and taken action to enhance the control environment operated. Officers have requested early sight of the internal control report for the year to 31 December 2017.

11.13 Copies of the internal control reports are held by the Pensions Accounting Team, and can be made available upon request.

### Mercer's manager research

- 11.14 The Fund obtained Mercer's Operations and Implementation Risk reports, prepared in March 2011 regarding BlackRock, and in February 2011 regarding Legal & General.
- 11.15 Mercer conducts ongoing research and monitoring of the Fund's managers, and informs clients where it has any concerns. The information within Mercer's Operations reports is fed into the overall research notes and manager ratings which Mercer provides to NCC in the quarterly monitoring report.

# MEETING OF THE PENSION FUND PANEL

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## REPORT OF THE SERVICE DIRECTOR - FINANCE

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### 12. Investment Strategy Statement

#### Purpose of the report

This report seeks Panel approval to update NCC's LGPS Investment Strategy Statement.

#### Recommendation

The Panel is requested to:

- (i) approve the NCC LGPS Investment Strategy Statement (ISS) attached as Appendix 9 to this report; and
- (ii) delegate authority to the Service Director - Finance in consultation with the Chair and Vice Chair of the Panel to make any further changes required as a result of consultation with the participating employers and trade unions.

#### Key issues

- 12.1 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 require administering authorities to have an Investment Strategy Statement (ISS) in place. These Regulations replaced the earlier requirement to have a Statement of Investment Principles in place. The 2016 Investment Regulations removed the prescribed limits on types and weightings of investments and replaced them with a requirement to invest in a "wide variety" of investments and set out the authority's approach to matters such as risk, **pooling**, environmental, social and corporate governance issues and exercise of voting rights. The ISS must be prepared in accordance with MHCLG's guidance which is attached as **Appendix 10**.
- 12.2 Regulation 8 of the 2016 Investment Regulations allows the Secretary of State to intervene directly in the investment management of a LGPS fund should an administering authority fail to act in accordance with MHCLG's guidance. This is widely interpreted as meaning that the Secretary of State will intervene, if necessary, to ensure **all LGPS funds commit to a pooling** arrangement.
- 12.3 NCC's first ISS was in place (as required) by 1 April 2017. It must be reviewed at least every three years, and it is appropriate to review now so the up to date version can be included in the 2017/2018 annual report for NCC Pension Fund. The updated version is attached as **Appendix 9**. The changes made include:
  - adding references to the Fund's new investments in Legal and General's currency hedged units, and Pantheon's private equity fund of funds; and
  - updating the information about BCPP pooling arrangement to reflect the Fund's legal commitment made in June 2017.Consultation on the revised ISS will take place following this meeting, therefore a delegation is sought to ensure any changes required can be made quickly.

## 12. Investment Strategy Statement

### BACKGROUND

#### NCC Pension Fund's Statement of Investment Principles

12.4 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 required administering authorities to have a Statement of Investment Principles (SIP) in place. Until February 2016, NCC Pension Fund's SIP was reviewed and approved by the Panel at least annually.

#### The 2016 Investment Regulations

12.5 The 2009 Investment Regulations were revoked and replaced by the 2016 Investment Regulations, with effect from 1 November 2016. The 2016 Investment Regulations introduced a requirement to formulate an Investment Strategy Statement (ISS) which replaced the requirement to have a SIP in place.

12.6 The requirements of the ISS and SIP are very similar. Unlike the 2009 Investment Regulations, the 2016 Investment Regulations do not set **prescribed limits** for the type of investments which LGPS funds may hold or the weighting of different asset classes within the investment portfolio. Instead of complying with limits, under Regulation 7, each administering authority will be required, in the ISS, to **outline its approach** to investing. Certain parameters are set out in the Regulations, for example, the ISS must include a requirement to invest in a "wide variety" of investments, and must set out the authority's approach to matters such as risk, pooling of investments, environmental, social and corporate governance (ESG) considerations and the exercise of voting rights.

12.7 The ISS must comply with MHCLG's guidance, and the authority must take "proper advice" when preparing it. NCC Pension Fund's first ISS was published before the deadline of **1 April 2017** and there is a requirement to review and revise it at least every **three** years.

12.8 The most controversial provision in the 2009 Regulations is Regulation 8, which allows the Secretary of State to intervene **directly** in the investment management of a LGPS fund in the event that an administering authority fails to act in accordance with the Secretary of State's guidance.

12.9 The Secretary of State's Guidance on preparing and maintaining an ISS was issued **15 September 2016** and is attached as **Appendix 10** to this report.

12.10 The 2016 Investment Regulations provide a prudential framework within which the investment strategy can be implemented and managed, rather than the more prescriptive approach that was previously in place. The **extra freedom** given to administering authorities comes with the **quid pro quo** of greater **power of intervention** given to MHCLG.

- 12.11 The Guidance on preparing and maintaining an ISS includes the requirement that all authorities must commit to a suitable pool to achieve benefits of scale. Administering authorities must confirm their chosen investment pool meets the investment reform and **criteria** published in **November 2015**, or that they have received confirmation from Government to continue with pooling proposals that do not.
- 12.12 The November 2015 criteria states that authorities must submit **proposals** which describe pooling arrangements which “*have regard to*” each of four criteria, namely:
- A. Asset pool(s) that achieve the benefits of scale;
  - B. Strong governance and decision making;
  - C. Reduced costs and excellent value for money; and
  - D. An improved capacity to invest in infrastructure.
- 12.13 NCC Pension Fund’s chosen pooling arrangement, BCPP, **received confirmation** from Government in December 2017 that it’s pooling proposal (submitted to Government in July 2016) meets the November 2015 criteria.

#### Requirement to formulate and publish an ISS

- 12.14 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 require each administering authority to formulate and publish a statement of its investment strategy.
- 12.15 Regulation 7 of the LGPS (Management and Investment of Funds) Regulations 2016 sets out:

#### ***“Investment strategy statement***

***7.—(1) An authority must, after taking proper advice, formulate an investment strategy which must be in accordance with guidance issued from time to time by the Secretary of State.***

***(2) The authority’s investment strategy must include—***

- (a) a requirement to invest fund money in a wide variety of investments;***
- (b) the authority’s assessment of the suitability of particular investments and types of investments;***
- (c) the authority’s approach to risk, including the ways in which risks are to be assessed and managed;***
- (d) the authority’s approach to pooling investments, including the use of collective investment vehicles and shared services;***
- (e) the authority’s policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and***
- (f) the authority’s policy on the exercise of the rights (including voting rights) attaching to investments.***

*(3) The authority's investment strategy must set out the maximum percentage of the total value of all investments of fund money that it will invest in particular investments or classes of investment.*

*(4) The authority's investment strategy may not permit more than 5% of the total value of all investments of fund money to be invested in entities which are connected with that authority within the meaning of section 212 of the Local Government and Public Involvement in Health Act 2007.*

*(5) The authority must consult such persons as it considers appropriate as to the proposed contents of its investment strategy.*

*(6) The authority must publish a statement of its investment strategy formulated under paragraph (1) and the first such statement must be published no later than 1st April 2017.*

*(7) The authority must review and if necessary revise its investment strategy from time to time, and at least every 3 years, and publish a statement of any revisions.*

*(8) The authority must invest, in accordance with its investment strategy, any fund money that is not needed immediately to make payments from the fund."*

#### NCC Pension Fund's first ISS (1 April 2017)

12.16 The Fund's first ISS was prepared by officers with advice from the Fund's adviser, Mercer. Officers in the Border to Coast Pensions Partnership (BCPP) Officer Operations Group (OOG) collaborated on part of the drafting of each administering authority's ISS, to ensure consistency in the references made to the approach to pooling.

12.17 Officers also consulted on the ISS with the Fund's investment managers, and (following approval for consultation by the Panel) consulted with the Fund's participating employers and relevant trade unions

#### ISS update

12.18 NCC's first ISS was in place (as required) by 1 April 2017. Whilst there is a legal requirement to review it at least every three years, it is appropriate to review now so the up to date version can be included in the Fund's 2017/2018 annual report, which is published and widely distributed to the Fund's stakeholders.

12.19 The updated ISS is attached as **Appendix 9**. The changes made to the original (1 April 2017) version are minimal, and include:

- adding references to the Fund's new investments in Legal and General's currency hedged units in North America and Europe (ex UK), and in Pantheon's private equity fund of funds; and
- updating the information about BCPP pooling arrangement to reflect the Fund's legal commitment made in June 2017.

#### Approval and consultation

12.20 Members are asked to review and approve the updated draft ISS (attached as Appendix 9) for consultation.

- 12.21 The authority must **consult** over the ISS with “persons it considers appropriate”, therefore, following Panel approval for the draft ISS at this meeting, the Fund’s participating employers and relevant trade unions will be consulted. This report also seeks delegated authority to the Service Director - Finance in consultation with the Chair and Vice Chair of the Panel to amend the ISS, if appropriate, as a result of comments received from the consultation process.
- 12.22 Any **significant** revisions to the ISS, following consultation, will be brought back to the Panel meeting on 22 June 2018, for information.



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## REPORT OF THE SERVICE DIRECTOR - FINANCE

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### 13. Training records

#### Purpose of the report

The purpose of this report is to enable the Panel to conduct an annual review of the training records of Pension Fund Panel and Local Pension Board members and key officers.

#### Recommendation

**The Panel is requested to review the training records attached as Appendix 11 to this report and assess the adequacy of knowledge and skills acquired by Panel members to fulfil Panel duties.**

#### Key issues

- 13.1 In May 2015, the Pension Fund Panel adopted a formal Training Policy for NCC Pension Fund which explicitly applied to:
- Pension Fund Panel members;
  - Local Pension Board Members; and
  - the supporting officers involved in the administration of the LGPS.
- Adopting a formal policy of this type was intended to **demonstrate** compliance with the spirit of the guidance from the Pensions Regulator (tPR) and CIPFA.
- 13.2 An individual training log showing training undertaken by each of the Panel and Board members as well as key officers was first brought to the May 2015 Panel meeting for review. Training records are reported to the Panel and reviewed on an annual basis.
- 13.3 A formal Training Needs Analysis (TNA) procedure was introduced for Panel and Board members at the September 2017 Panel meeting, and following its introduction, responsibility for assessing the knowledge and understanding acquired individually by **Board members** has been assumed by the Board itself.
- 13.4 In order to assess the adequacy of the knowledge and understanding acquired using current practices, the training records for **Panel** members, together with the results of the TNA for Panel members (as reported to the 24 November 2017 Panel meeting), are shown in **Appendix 11** attached to this report, for members' review. For information, the training record for key officers is attached as **Appendix 12** to this report.
- 13.5 Panel members are asked to review the training records for Panel members:
- to confirm completeness; and
  - to assess the evidence of adequacy for ensuring that Panel members, *collectively*, have sufficient knowledge and understanding to fulfil Panel duties.



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### 14. Additions to the NCC Pension Fund risk register

#### Purpose of the report

This report provides information to the Panel about recent additions to the NCC risk register, to update for new risks faced by NCC as administering authority for the LGPS.

#### Recommendation

**The Panel is requested to accept the report.**

#### Key issues

- 14.1 It is good practice for LGPS administering authorities to maintain a risk register which recognises the risks faced in administering the pension fund. The risk register should be regularly updated and new risks added as soon as they become apparent.
- 14.2 NCC's corporate risk register is maintained by the Risk Management Officer on the Magique Galileo software. NCC Pension Fund has its own Risk Management Policy, adopted in February 2016, drafted to tie in with NCC's corporate risk management framework and risk scoring system. The Fund's Risk Management Policy was reported to the 14 November 2017 Panel meeting.
- 14.3 At the request of the Panel, at its meeting held on 11 December 2017 the Board reviewed potential new risks identified for inclusion in the risk register. The risks to the Fund, set out in **Appendix 13**, considered by the Board in December were:
- cyber security risk;
  - GDPR legislation;
  - LGPS membership records' accuracy following transition to shared administration service with Tyne and Wear Pension Fund;
  - performance standards of shared administration service (post 29 January 2018);
  - potential increased costs or reduced performance arising from pooling;
  - failure to achieve/maintain elective professional status (under MiFID II) with financial institutions; and
  - retention of LGPS administration expertise (pre 29 January 2018).
- The Board's review was carried out on the understanding that the risks considered would be brought to this meeting of the Panel, for information and review.
- 14.4 Following the Board's review, the risks (at Appendix 13) were incorporated in NCC's corporate risk register. The last risk shown in paragraph 14.3 above (i.e. retention of LGPS administration expertise) was removed from the register in February 2018.



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### 15. Reporting breaches: progress and quarterly monitoring report

#### Purpose of the report

This report provides information about breaches of the law which have occurred in the quarter to 31 December 2017.

#### Recommendation

**The Panel is requested to accept the report.**

#### Key issues

- 15.1 Oversight of the LGPS by the Pensions Regulator (tPR) from 1 April 2015 brought with it the requirement for administering authorities to enforce the LGPS Regulations and supporting law and guidance more assiduously than before due to the requirement to record and (potentially) report breaches of LGPS Regulations. Since April 2015, NCC has reported some breaches to the Panel, quarterly, and considered the *material significance to the Regulator*. Since April 2016, all other known breaches have also been reported to the Panel.
- 15.2 In the quarter to 31 December 2017 there were two breaches of the requirement to pay contributions within 19 days of the month end, which are detailed in **Appendix 14**. The amounts due were paid later.
- 15.3 Records of breaches prepared by the Pensions Administration Team are **enclosed** with these papers for the:
- quarter ended 31 December 2017 (an A3 spreadsheet);
  - quarter ended 30 September 2017 (a separate A3 spreadsheet), showing brought forward breaches that had not been resolved when reported to the November 2017 Panel meeting;
  - quarter ended 30 June 2017 (a separate A3 spreadsheet), showing brought forward breaches that had not been resolved when reported to the September 2017 and November Panel meetings;
  - quarter ended 30 September 2016 (a separate A3 spreadsheet), showing brought forward breaches that had not been resolved when reported to the November 2016, February 2017, July 2017, September 2017 and November 2017 Panel meetings.
- Diane Taylor, Manager at Tyne and Wear Pension Fund, will attend this Panel meeting to provide further information about these breaches records.
- 15.4 Panel members are reminded that, following implementation of the shared administration service in January 2018, information about breaches within the administration function **in the current format** will no longer be provided from 1 January 2018. However, breaches that occur within the functions retained by NCC, including collection of contributions from employers, will continue to be reported quarterly to the Panel.



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#### 16. Key Performance Indicators (KPIs) for LGPS administration

##### Purpose of the report

The purpose of this report is to provide information to the Panel about the Fund's KPIs in the quarter to 31 December 2017.

##### Recommendation

**The Panel is requested to accept the report.**

##### Key issues

- 16.1 The NCC LGPS Administration Strategy in place until 29 January 2018 refers to Key Performance Indicators (KPIs) for the NCC pensions administration function. These KPIs have been reported to the Panel on a quarterly basis since the quarter to 31 December 2016.
- 16.2 **Appendix 15** sets out the KPIs and the achievements for the quarter ended 31 December 2017 compared with the previous three quarters.
- 16.3 Compared to previous quarters, in the quarter to 31 December 2017, the KPI re:
- receipt of employer contributions has deteriorated due to two isolated breaches;
  - notification of benefits on retirement has met the Fund target and improved against earlier quarters;
  - notification of dependents of death benefits has improved against earlier quarters.
- These achievements are in spite of the additional volume of work NCC's Pensions Administration Team was dealing with in October, November and December 2017 in preparing for the shared administration service.
- 16.4 The NCC LGPS Administration Strategy approved at the 3 November 2017 Panel meeting in readiness for the shared administration service with Tyne and Wear Pension Fund, became effective from 29 January 2018. This Strategy was purposefully drafted to align with Tyne and Wear Pension Fund's Strategy, for the efficient operation of the shared service. NCC's new Administration Strategy does not specify KPIs.
- 16.5 Quarterly **performance information** is reported to South Tyneside Council's Senior Management Team and Pensions Committee. From 29 January 2018, NCC will receive the equivalent performance information in relation to the NCC Pension Fund. Such information will be reported to the Panel on a quarterly basis.



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### 17. Tyne and Wear Pension Fund's quarterly regulatory report

#### Purpose of the report

This report provides information to the Panel about Tyne and Wear Pension Fund's quarterly regulatory report, which is provided to South Tyneside Council's Pensions Committee to keep members up to date with relevant LGPS regulatory changes.

#### Recommendation

**The Panel is requested to accept the report.**

#### Key issues

- 17.1 Tyne and Wear Pension Fund's (TWPF) Head of Pensions Administration prepares a report ("the regulatory report"), each quarter, to update the Pensions Committee on relevant LGPS regulatory changes and other related matters.
- 17.2 The most recent regulatory reports taken to South Tyneside Council's Pensions Committee over the last year are attached as **Appendices 16, 17, 18 and 19** to this report.
- 17.3 It is good practice to provide such information on a regular basis to those charged with governance. From now on, the TWPF's quarterly regulatory report will also be brought to Northumberland County Council's Pension Fund Panel, so Panel and Board members can be kept up to date of all relevant regulatory changes.
- 17.4 Items of particular note in the regulatory reports:
- |                                  |  |
|----------------------------------|--|
| Appendix 16<br>7 March 2017      | <ul style="list-style-type: none"><li>• Proposed public sector exit payment reforms</li><li>• Delays to the proposed LGPS (Amendment) Regulations 2016</li><li>• Consultation on GMPs, including TWPF's response</li></ul> |
| Appendix 17<br>13 June 2017      | <ul style="list-style-type: none"><li>• Scheme Advisory Board's consultation on academies</li></ul>  |
| Appendix 18<br>14 September 2017 | <ul style="list-style-type: none"><li>• Scheme Advisory Board's consultation on Local Pension Boards (and on academies)</li><li>• Brewster judgement</li></ul>   |
| Appendix 19<br>24 November 2017  | <ul style="list-style-type: none"><li>• Scheme Advisory Board's consultation on "tier three" employers</li><li>• Pensions Regulator's annual scheme return</li></ul>   |



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### 18. Fund performance and total Fund value

#### Purpose of the report

The purpose of this report is to provide information to the Panel about the Fund's performance in the quarter to 31 December 2017 and the total Fund value at that date.

#### Recommendation

**The Panel is requested to accept the report.**

#### Key issues

- 18.1 The total Fund value (externally managed) was **£1,386** million as at 31 December 2017, compared to £1,330 million as at 30 September 2017, reflecting the positive investment returns over the quarter, offset by some cash outflow in the quarter.
- 18.2 Performance information for the Fund as a whole for the quarter and year to 31 December 2017 was not available in time to be included with this report.
- 18.3 Further detail of annual and quarterly performance by manager and asset class for the period ending 31 December 2017 (i.e. the "*Quarterly Risk and Return Analysis*" provided by Portfolio Evaluation Ltd, the Fund's performance measurement service provider) will be emailed to Panel and Board members as soon as it is available, and tabled at the meeting.

## 18. Fund performance and total Fund value

### BACKGROUND

#### Total Fund value

18.4 The total value of the Fund at the last four quarter ends is as follows:

	as at <u>31 December</u> <u>2016</u> £m	as at <u>31 March</u> <u>2017</u> £m	as at <u>30 September</u> <u>2017</u> £m	as at <u>31 December</u> <u>2017</u> £m
<b>Legal and General</b> <i>Index tracker</i>	<b>1008.96</b>	<b>1051.55</b>	<b>1074.89</b>	<b>1125.48</b>
<b>Wellington</b> <i>Active corporate bonds</i>	<b>98.30</b>	<b>99.91</b>	<b>102.48</b>	<b>103.36</b>
<b>Schroder</b>	25.94	25.11	26.84	27.47
<b>BlackRock</b>	24.27	26.35	25.85	26.44
<i>Property</i> <b>subtotal</b>	<b>50.21</b>	<b>51.46</b>	<b>52.69</b>	<b>53.91</b>
<b>Morgan Stanley</b>	35.67	34.71	27.66	26.48
<b>NB Crossroads</b>	21.09	26.17	20.74	21.10
<b>Pantheon</b>			0.81	4.55
<i>Private equity</i> <b>subtotal</b>	<b>56.76</b>	<b>60.88</b>	<b>49.21</b>	<b>52.13</b>
<b>GIP</b>	31.07	32.11	31.32	32.52
<b>Antin</b>	18.34	17.93	19.28	19.04
<i>Infrastructure</i> <b>subtotal</b>	<b>49.41</b>	<b>50.04</b>	<b>50.60</b>	<b>51.56</b>
<b>Total</b>	<b>1,263.64</b>	<b>1,313.84</b>	<b>1,329.87</b>	<b>1,386.44</b>

Note that capital calls and capital repayments have been made during the year to 31 December 2017 for private equity and infrastructure investments. Extra funding, when needed, came out of cash held by the Pension Fund for the day-to-day expenditure incurred in administering the Scheme and by disinvesting from Legal and General. Capital repayments have been transferred to Legal and General to invest, or when timing can be matched, used to pay other capital calls.

18.5 Further detail of annual and quarterly performance by manager and asset class for the period ending 31 December 2017 (i.e. the “*Quarterly Risk and Return Analysis*” provided by Portfolio Evaluation Ltd, the Fund’s performance measurement service provider) will be emailed to Panel and Board members as soon as it is available, and tabled at the meeting.

Fund performance

18.6 The Fund’s performance is measured by Portfolio Evaluation Ltd (formerly, until 31 March 2016 by the WM Company, later known as State Street/GS Performance Services). Shown below are the annual returns achieved by the Fund for the five years to 31 March 2017 and for the latest four quarters. Also shown are the annualised returns achieved by the Fund for the five years to 31 March 2017.

**18.7 Annual returns**

	Financial Year Ended 31 March				
	2013	2014	2015	2016	2017
	%	%	%	%	%
Fund	14.0	3.8	13.2	-0.7	24.2
Benchmark	14.2	3.7	13.1	-1.2	24.1

**18.8 Quarterly returns**

	-- 2016/17 --		----- 2017/18 -----	
	Quarter 1 2017 to 31 Mar 17	Quarter 2 2017 to 30 Jun 17	Quarter 3 2017 to 30 Sep 17	Quarter 4 2017 to 31 Dec 17
	%	%	%	%
Fund	4.0	0.3	1.7	N/A
Benchmark	4.3	0.4	1.8	N/A

**18.9 Annualised returns**

	All Financial Years Ended 31 March		
	2012/17	2014/17	2017
	%	%	%
Fund	10.6	11.8	24.2
Benchmark	10.4	11.6	24.1
	5 years	3 years	1 year



## IMPLICATIONS ARISING OUT OF THE REPORT

This applies to items 1. to 18. (inclusive) in this report

<b>Policy:</b>	Policy decisions are requested in reports 9 and 12, only.
<b>Finance and value for money:</b>	All investment decisions and funding strategy decisions could have an implication for the future employer contribution rates payable by employers participating in the Pension Fund. There are no investment decisions arising directly from these reports.
<b>Human Resources:</b>	None
<b>Property:</b>	None
<b>Equalities:</b>	None
<b>Risk Assessment:</b>	A risk assessment is performed as part of the asset liability modelling study undertaken periodically (usually every three years) to set the Fund's asset allocation strategy. There is no change to investment strategy contained within these reports. Updates to the administering authority's risk register are shown in report 14.
<b>Sustainability:</b>	None
<b>Crime &amp; Disorder:</b>	None
<b>Customer considerations:</b>	None
<b>Consultation:</b>	None
<b>Electoral divisions:</b>	All

## Report sign off

Finance Officer	N/A
Monitoring Officer/Legal	N/A
Human Resources	N/A
Procurement	N/A
I.T.	N/A
Service Director - Finance	AE
Portfolio Holder(s)	N/A

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