

Royal Borough of Kensington and Chelsea Pension Fund Annual Report and Accounts

2015-16

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FOREWORD



Councillor Quentin Marshall

Chairman of the Investment Committee

On behalf of the the Investment Committee I am delighted to present The Royal Borough of Kensington and Chelsea Pension Fund (the Fund) Annual Report and Financial Statement for the year ending 31 March 2016.

This has been another year of major changes for the Local Government Pension Scheme (LGPS). April 2015 saw the introduction of the Fund's Pensions Board, whose role is to assist in the governance of the scheme, in particular with regards to compliance with regulations and legislation, following best practice and delivering an effective and efficient scheme. The Council established the Pension Board, its members being employer and member representatives, on 1 April 2015.

In the July 2015 budget, the government announced that it wants to see LGPS funds pool investments to reduce costs and facilitate improved LGPS governance while maintaining overall investment performance. The Royal Borough of Kensington and Chelsea (RBKC) has actively supported the establishment of the London Collective Investment Vehicle (CIV), the body that will provide London wide pooling and RBKC has responded to the pooling of assets consultation through CIV. Pooling will not change the committee's responsibility for setting investment policy and ensuring that it is effectively implemented.

The reforms to the State Pension and all public service pension schemes, alongside the introduction of auto enrolment and flexible access to pensions savings under the 'Freedom and Choice' initiative, will have an impact on the Fund and the staff who contribute to it.

Over the last year, the Fund's assets have increased by £15 million, with investments returning 2.28% for the year. It has been a mixed year for investments in a difficult year for markets: although the Fund has slightly underperformed its benchmark for the year, the medium to long term performance compared to its benchmark return has been good, standing at 9.89% compared to a benchmark of 8.97%.

It is also reassuring that, as at 31 March, the Fund's actuary assessed that during the year the funding position had improved by 1.9 percentage points to 102.7 per cent. This compares with 95 per cent at the 2013 actuarial valuation. This performance is mainly attributable to the excellent returns achieved from equities in the years since the restructuring of the Fund following the 2010 valuation.

Finally, I would like to take this opportunity to thank my colleagues on the Investment Committee, Pension Board, our advisers, employers and the Pension Fund team involved in the management of the Pension Fund during 2015-16.

1. GOVERNANCE AND MANAGEMENT

Governance Arrangements

The Royal Borough of Kensington and Chelsea Council has delegated decision making powers in respect of pensions to the Investment Committee (the Committee). During 2015-16, the Committee comprised six elected representatives of the Council – four from the majority party and two minority party. There were four Co-opted non-voting members of the Committee.

Investment Committee

The Committee meets at least four times a year, “To consider and decide all matters appertaining to the Council’s Superannuation Fund and to report annually, or otherwise as may be necessary, to the Council.” In practice, its remit includes the following responsibilities:

- To determine the overall investment strategy and strategic asset allocation of the Pension Fund;
- To appoint the investment manager(s), custodian, actuary and any independent external advisors felt to be necessary for the good stewardship of the Pension Fund;
- To monitor the performance of the custodians, actuary and external advisors to ensure that they remain suitable;
- To review on a regular basis the investment managers’ performance against established benchmarks, and satisfy themselves as to the managers’ expertise and the quality of their internal systems and controls;
- To prepare, publish and maintain the Statement of Investment Principles, and monitor compliance with the statement and review its contents;
- To prepare, publish and maintain the Funding Strategy Statement, the Governance Compliance Statement, and the Communications Policy Statement and revise the statements to reflect any material changes in policy;
- To approve the final accounts and balance sheet of the Pension Fund and approve the Annual Report;
- To receive actuarial valuations of the Pension Fund regarding the level of employers’ contributions necessary to balance the Pension Fund;
- To consider any proposed legislative changes in respect of the Compensation and Pension Regulations and to respond appropriately; and
- To receive and consider the external auditors’ report on the governance of the Pension Fund.

The Committee reports to the full Council annually on its activities. The Committee obtains and considers advice from the Town Clerk and from the Director of Treasury and Pensions, and as necessary from the Fund’s appointed actuary, advisors and investment managers.

The membership of the Investment Committee in 2015-16 was as follows:

Councillor Quentin Marshall	Chairman
Councillor Warwick Lightfoot	Vice Chairman
Councillor Harrison Littler	
Councillor Andrew Lomas	
Councillor Andrew Rinker	
Councillor Paul Warrick	

The four co-opted, non-voting members were:

Sir Michael Craig-Cooper
Hon Alderman John Cox
Mr Dominic Johnson
Mr Jonathon Read

Pensions Board

The Council has also established a Pensions Board as required by the Public Services Pensions Act 2013. The role of the local Pension Board is defined by section 5 of the Public Service Pensions Act 2013 and regulation 106 of the Local Government Pension Scheme (LGPS) Governance Regulations 2013. It assists the administering authority (the Council) with:

- Securing compliance with the LGPS Governance regulations and any other legislation relating to the governance and administration of the LGPS;
- Securing compliance with any requirements imposed by the Pensions Regulator in relation to the scheme; and
- Ensuring effective and efficient governance and administration of the scheme-recommendations to the Investment Committee.

The Board does not have a decision making role in relation to management of the Fund, but is able to make recommendations to the Investment Committee. It has meet three times.

The membership of the Board is as follows:

- Three employer representatives comprising one from an admitted or scheduled body and two nominated by the Council. There is one vacancy for an employer representative;
- Three scheme members representatives from the Council or an admitted or scheduled body.

The current membership of the Pensions Board is as follows:

Cllr Tim Ahern (Chairman)
Cllr Malcolm Spalding
Mr Charles Farrar
Mr Jago Williams (Vice Chairman)
Mr Kenneth Davison

Knowledge and Skills

During 2015-16 the following formal training sessions were arranged and attended by Investment Committee members, Board members and officers:

- Pension Fund Overview and Governance
- Actuarial Valuations

This was in addition to knowledge gained from various meetings with investment managers and individual attendance at conferences and seminars.

Governance Compliance Statement

The Local Government Pension Scheme Regulations 2013 require Pension Funds to prepare, publish and maintain a governance compliance statement; and to measure its governance arrangements against a set of best practice principles. This measurement should result in a statement of full, partial or non-compliance with a further explanation provided for any non or partial compliance.

The key issues covered by the best practice principles are:

- Formal committee structure;
- Committee membership and representation;
- Selection and role of lay members;
- Voting rights; and
- Training, facility time and expenses.

The Fund's published statements can be found by following the link:

<https://www.rbkc.gov.uk/council/how-council-manages-money/council-spending-and-finances/pension-fund-2014-15>

Scheme Management and Advisers

The City of Westminster, London Borough of Hammersmith & Fulham and The Royal Borough of Kensington and Chelsea have combined some operational areas to provide a more efficient service and greater resilience. This includes the Pensions and Treasury teams and is responsible for the management of the pension fund investments and the treasury operations across the three boroughs. The team is based at Westminster City Hall.

The Pension Fund continue to be managed separately in accordance with each borough's strategy and so each continues to have sovereignty over decision making. However, officers are continually seeking to improve efficiency and resilience and to minimise the cost of running the Pension Funds, in line with the tri-borough working aims.

The officers responsible for running the Pension Fund and the external advisers who are contracted to assist are shown in the tables below

Officers

Town Clerk (section 151 officer) Tri-borough Director of Treasury and Pensions	Nicholas Holgate George Bruce
Tri-borough Pensions Team in 2015-16	Alex Robertson Nicola Webb Nikki Parsons Hasina Shah
Bi-borough Director of HR Bi-borough Pensions Manager	Debbie Morris Maria Bailey

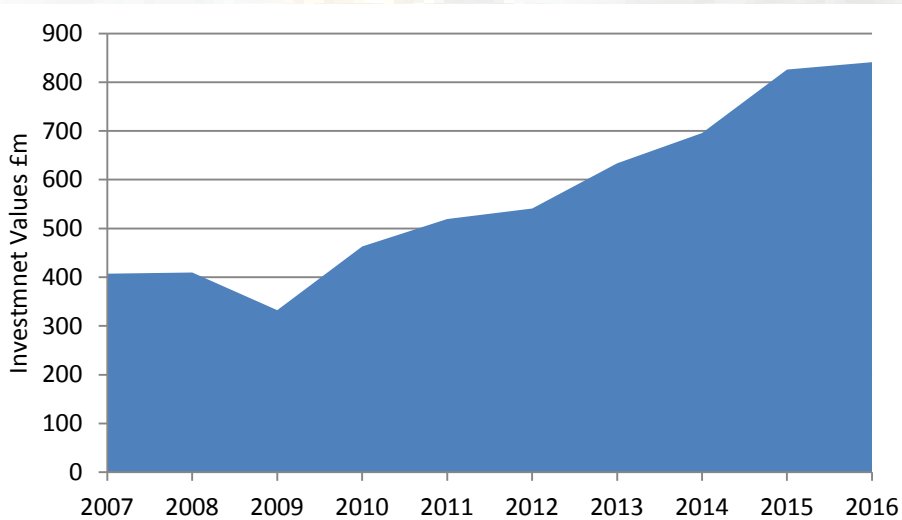
External Advisers

Investment Adviser	Hymans Robertson
Investment Managers	Adams Street Partners Baillie Gifford CBRE Global Investors Legal & General Investment Management Longview Asset Management Kames Capital Pyrford LLP
Custodian	Northern Trust
Banker	Nat West
Actuary	Barnett Waddingham
Auditor	KPMG
Legal Adviser	Eversheds
Scheme Administrators	Surrey County Council
AVC Providers	Prudential

Financial Summary and performance

The investment return in 2015-16 was positive both in absolute terms although it trailed the Fund's target. The annual return was 2.28 per cent following a difficult year for the equity markets, which is marginally below the target of 2.33 per cent set by the Fund. However, the medium and long-term returns were both above target at 9.89 per cent and 10.40 per cent respectively and impressive in absolute terms. As with all performance reported here, this was net of fees. The Investment Policy and Performance report in Section 2 provides more detail on the Fund's investments and performance.

At the beginning of the period, the market value of the Fund's investment assets was £825.9 million. By the end of March 2016, the value of those assets was £841.0 million, the increase of £15.1 million reflects net cash-flow and appreciation in market value. The graph below shows how the value of the Fund's investments has increased over time by showing the total value at 31st March every year for the last ten years, a period in which the fund value has more than doubled:



The main driver of investment return has been the equity portfolio, with all equity and private equity managers recording since inception returns in excess of 10 per cent per annum.

The Pension Fund Account, Net Assets Statement and Notes to the Accounts set out in section 5, which provides more detail about the financial transactions during the year and the value of assets at the end.

Risk Management

Risk management is the process of identifying risks, evaluating their likelihood and potential impact and determining the most effective methods of mitigating and controlling those risks.

A key element to risk management is the structured governance arrangements, set out in the preceding section, which ensure that the management of Fund administrative, management and investment risk is undertaken at the highest levels.

The Fund maintains a risk register and reviews the risks and mitigating actions on a regular basis. The register covers both strategic and operational risks and risks in relation to the investment, funding, governance and administration aspects of the Pension Fund.

The Fund has recognised that the most significant long term risk is that the Fund's assets are not sufficient to meet the liabilities. In light of this, the Fund has set a benchmark for the investments designed to out-perform the investment return assumed by the Fund Actuary in the actuarial valuation. In addition, the Investment Committee monitor the value of liabilities and progress of the funding level on a quarterly basis.

In order to achieve a level of investment performance in excess of the Fund Actuary's assumption, the Fund has invested in growth assets, the value of which can fluctuate significantly. To mitigate this risk, an investment strategy which covers a wide range of asset classes and geographical areas has been implemented, to ensure diversification. All of the investments are undertaken in line with the Local Government Pension Scheme (Management & Investment of Funds) Regulations 2009 and only following advice from the Fund's investment adviser. The investment performance is monitored on a quarterly basis by the Investment Committee and on a monthly basis by the officers.

All of the Fund's assets are managed by external investment managers and they are required to provide an audited internal controls report regularly to the Fund which sets out how they ensure the Fund's assets are managed in accordance with the Investment Management Agreement the Council has signed with each investment manager. A range of investment managers are used to diversify manager risk. All the Fund's segregated assets are held for safekeeping by the Fund's custodian, who is independent of all the investment managers. The pooled assets held by the Fund are also held by custodians independent of the investment managers responsible for investment decisions.

Risks associated with the operational payment of benefits and recording of member entitlement produces a complex set of risks, which are mitigated with the use of an IT system that is thoroughly and regularly tested, combined with the checking of output.

It is recognised that Fund services are very dependent upon third party contracts ranging from IT through to investment managers. All are subject to regular review and monitoring, with compliance visits targeted at the more significant risk areas.

2. INVESTMENT POLICY AND PERFORMANCE

Objective and Strategic Benchmark

The main objective for the Fund is to ensure that the Fund's assets and the future contributions are invested in such a manner that the benefits due can be paid as they arise. The Investment objective of the Fund is to maintain an appropriate funding level and to ensure growth above inflation in the value of the assets to facilitate low and stable contribution rates in the long term.

The Committee aims to achieve its investment objective by maintaining a high allocation to growth assets, mainly equity and other growth investments, which historically have provided a greater return than most fixed interest assets. The Fund's investment policy, objectives and strategy are set out in detail in the Statement of Investment Principles, which can be found at the link shown later in this section.

The strategic allocation and benchmark of the Fund is set out below.

Asset Class	Target Allocation	Benchmark
Global Equities	60%	MSCI world index plus 2%
Private Equity	5%	MSCI world index plus 2%
Absolute Return Fund	30%	RPI plus 5%
Property	5%	IPD UK all Balanced Funds plus 0.5%
Total	100%	

The target of the Fund as a whole is to outperform the overall benchmark by 2.3 per cent per annum on a rolling three-year basis.

Statement of Investment Principles

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 require Pension Funds to prepare, maintain and publish a statement setting out the investment policy of the Fund. In addition, Pension Funds are required to demonstrate compliance with the six "Myners Principles".

The "Myners Principles" are a set of recommendations relating to the investment of pension funds. The current version of the principles covers the following areas:

- Effective decision making;
- Clear objectives;
- Risk and liabilities;
- Performance Measurement;
- Responsible ownership; and
- Transparency and reporting.

The Fund's published statement can be found in the Pension Fund section of the following website:

<https://www.rbkc.gov.uk/council/how-council-manages-money/council-spending-and-finances/pension-fund-2014-15>

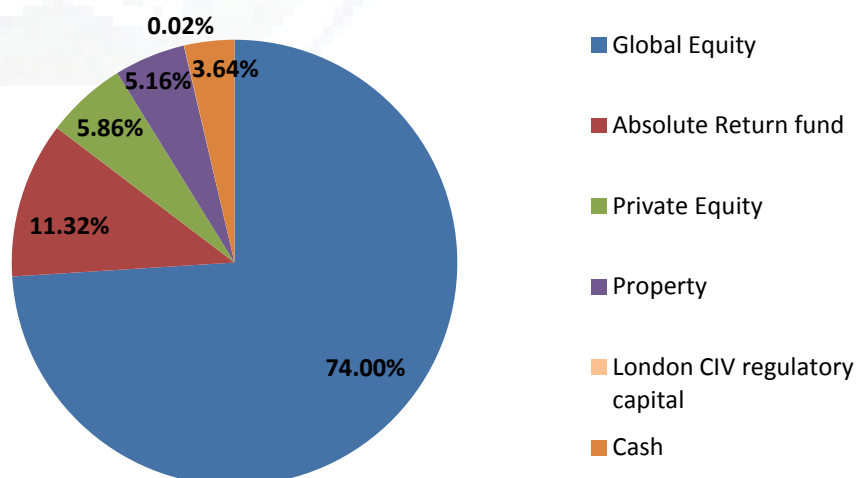
Investment Strategy

The investment strategy of the Fund is to have four main portfolios - Global Equity, Absolute Return, UK Property and Private Equity. The investment strategy is intended to provide diversification and specialisation to reduce exposure to market risk and achieve optimum return against the Fund's strategic benchmark.

As shareholders of London LGPS CIV Ltd. (the organisation set up to run pooled LGPS investments in London), the Fund has purchased £150,000 of regulatory capital. This is in the form of unlisted UK equity shares. See the later section for more detail on the London CIV.

The table and graph below show how the Fund was split between the portfolios at 31st March 2016.

Portfolio	Strategic Benchmark %	Market Value at 31/03/16		Market Value at 31/03/15	
		£000	%	£000	%
Global Equity	60	616,313	74.00	608,583	74.44
Absolute Return fund	30	94,316	11.32	92,702	11.34
Private Equity	5	48,798	5.86	45,901	5.61
Property	5	43,005	5.16	40,276	4.93
London CIV regulatory capital	0	150	0.02	-	-
Cash	0	30,286	3.64	30,118	3.68
Total	100	832,868	100	817,580	100



The table below shows how the investments were split at 31st March 2016 according to whether they are UK holdings, non-UK or global.

	UK	Non-UK	Global	Total
	£m	£m	£m	£m
Equities	23.7	238.8	393.1	655.6
Absolute Return Funds	-	-	94.3	94.3
Property	42.1	-	-	42.1
Cash and cash equivalents	40.8	-	-	40.8
Total	106.6	238.8	487.4	832.8

The gross investment income earned during 2015-16 is shown below also split according to whether it was earned from UK holdings, non-UK or global holdings. The income shown in the table is mainly earned from the segregated portfolios, as the majority of pooled fund income is re-invested in those funds and recorded as change in value rather than income.

Investment Income	UK	Non-UK	Global	Total
	£000	£000	£000	£000
Equities	4,090	149	-	4,239
Absolute Return Funds	-	-	1,299	1,299
Property	2,210	-	-	2,210
Cash and cash equivalents	37	-	-	37
Total	6,337	149	1,299	7,785

Investment Managers

The Fund has appointed external investment managers to manage the Fund's assets. The investment managers have clear benchmarks and targets, which place maximum accountability for performance on the manager. The detail of these is set out in the Statement of Investment Principles. The table below shows how the Fund's assets were allocated between the investment managers at 31st March 2016, and at 31st March 2015 for comparison.

Investment Manager	Market Value £000	% of Fund	Market Value £000	% of Fund
	As at March 16		As at March 15	
Baillie Gifford	174,080	20.9	176,326	21.6
Longview	223,011	26.8	213,867	26.2
Legal and General	249,327	29.9	248,420	30.4
Pyrford	94,316	11.3	92,702	11.3
Adams Street	48,798	5.9	45,901	5.6
KAMES	15,788	1.9	14,616	1.8
CBRE	27,217	3.3	25,660	3.1
London CIV	150	-	-	-
TOTAL	832,687	100.0	817,492	100.0

London CIV

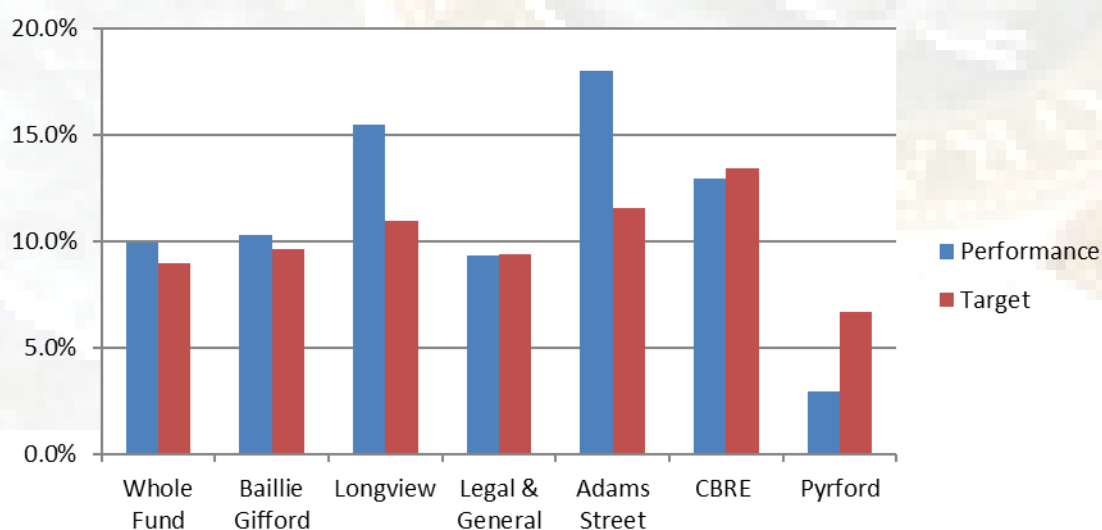
The Royal Borough of Kensington and Chelsea Pension Fund are shareholders of London LGPS CIV Ltd. The London LGPS CIV Limited has now been established as an Authorised Contractual Scheme (ACS) with approval from the Financial Conduct Authority. As shareholders the Fund has purchased £150,000 of regulatory capital in the form of unlisted UK equity shares to enable the ACS to operate.

Investment Performance

Annualised return	2015-16	3 years	>30 Years
Performance	2.28%	9.89%	10.40%
Target	2.33%	8.97%	10.13%
Out / (under) performance against target	-0.05%	0.92%	0.27%

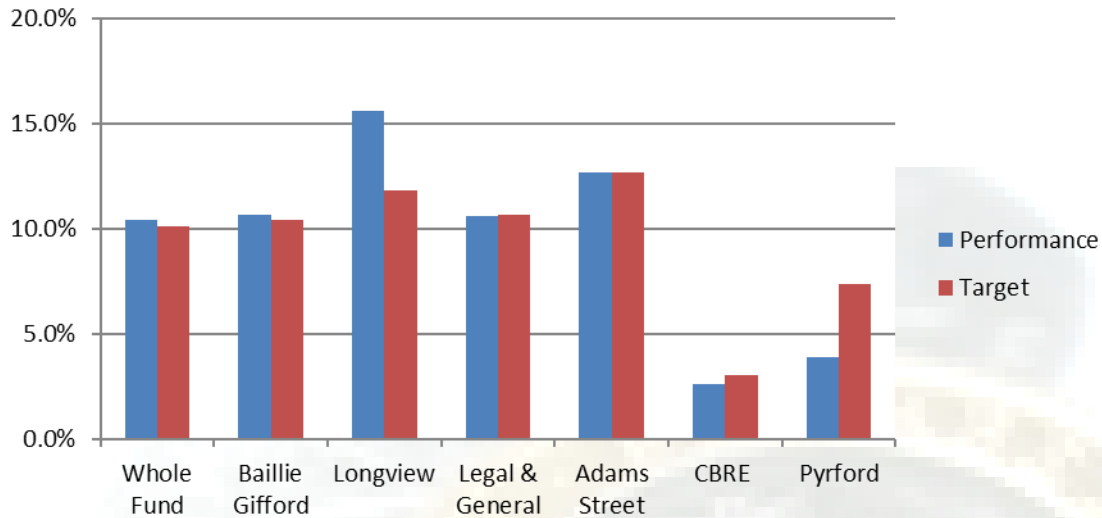
Each of the investment managers has a benchmark and target set within their Investment Management Agreements with the Fund. Performance is measured quarterly and reported to the Committee. The graphs below show the performance of the investment managers against their targets annualised over three years and longer term.

Three Years annualised performance against targets



The active equity managers, in particular Longview and Adam Street outperformed their targets in 2015-16, which delivered outperformance against target for the Fund as a whole over the three-year period. Pyrford's target is to beat the Retail Prices Index (RPI) by 5 per cent over a rolling three-year period which has been difficult with prevailing levels of inflation and low interest rates. However, the purpose of a diversified portfolio is to have portfolios that prosper in different economic conditions and the allocation to Pyrford balances the high equity weighting. Private equity valuations tend to lag behind the public markets against which Adams Street is measured, and the considerable improvement in their performance reflects the

improved opportunities to realise investments on appropriate markets. The overall performance over a longer period (>30 years) is similar, as shown below:



Responsible Investment

The Fund recognises that the neglect of corporate governance and corporate social responsibility may lead to poor or reduced shareholder returns. Following consideration of how to address the issue, and in the light of the resources available to the Fund, it has been decided to delegate responsibility for the consideration of responsible investment matters to the Fund’s investment managers. The Committee monitor the activity of fund managers in this area. All of the managers used by the Royal Borough Fund have signed up to the United Nations Principles for Responsible Investment.

Custody and Banking

Northern Trust is the global custodian for the Fund’s assets and is independent of the investment managers. Northern Trust is responsible for the safekeeping of all of the Fund’s investments as well as for the settlement of all investment transactions and the collection of income.

The Fund’s bank account is held at with NatWest (part of the RBS Group). Funds not immediately required to pay benefits are invested in a NatWest Business Reserve Account.

3. SCHEME ADMINISTRATION

The Local Government Pension Scheme (“LGPS”) is a statutory pension scheme governed by the Public Service Pensions Act 2013. The fund is administered in accordance with the following secondary legislation:

- The Local Government Pension Scheme Regulations 2013 (as amended);
- The Local Government Pension Scheme (Transitional Provision, Savings and Amendment) Regulations 2014 (as amended); and
- The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (as amended).

It is a defined benefit pension scheme and the benefits payable from the Fund are set out in the Local Government Pension Scheme regulations. Prior to 1st April 2014, the LGPS was a final salary scheme which paid pensions on the basis of final salary and length of service. Since 1st April 2014 the scheme has become a Career Average Revalued Earnings (CARE) scheme, so that a scheme member’s pension is based on their earnings throughout their career, rather than solely on their final salary. In summary the benefits payable are:

- A guaranteed pension based on career average re-valued earnings and length of service;
- The option to take up to 25 per cent of pension as a tax-free lump sum;
- Death and survivor benefits;
- Early payment of pensions in the event of ill health; and
- Pension increases in line with Consumer Price Inflation (CPI).

The Fund receives contributions from employees, the Council, the admitted and scheduled bodies and returns from the Fund’s investments. The employers’ contributions are set by the Fund’s actuary at the actuarial valuation, which is carried out every three years. The last valuation was done as at March 2013 and the next valuation as at March 2016 is being carried out currently.

Service Delivery

Although the LGPS is a national scheme, it is administered locally. The Royal Borough of Kensington and Chelsea has a statutory responsibility to administer the records of active and deferred members, as well as the pension benefits payable from the Pension Fund on behalf of the participating employers and the past and present members and their dependents. From 1st September 2015 the council entered into a not for profit section 101 agreement with Surrey County Council for them to undertake pensions administration on behalf of the council, replacing Capita.

To facilitate the move of administration responsibilities to Surrey County Council from Capita in 2015/16 pension member’s electronic data needed to be mapped across, cleansed and migrated. During the latter part of the year a strategy of targeted data improvements was agreed with Surrey County Council along with the creation and testing of electronic payroll interface data files from BT (the payroll provider for the Council) synchronising with the pensions data base.

It is anticipated that longer term these actions will drive consistency of data and other efficiencies within the pensions service. This strategy will also support the aim of implementing a pension member self-serve facility.

Membership of the Fund

The Fund provides pensions not only for employees of the Royal Borough of Kensington and Chelsea, but also for the employees from other organisations who participate in the LGPS as summarised below:

- **Scheduled Bodies:** These are statutorily defined bodies listed within the LGPS Regulations and have a statutory obligation to participate in the LGPS (e.g. academies, a further or higher education establishment).
- **Admitted Bodies:** These are typically charities or other not-for-profit public sector bodies providing a public service which has sufficient links with the administering employer to be regarded as having a community of interest and also private sector companies which will have taken on staff from a local authority as a result of an outsourcing of services. These organisations participate in the scheme via an admission agreement, which is a legal document made between the Council and the organisation.

The table below shows the number of employers with active contributing members in each of the last five years. The number of employers has been changing as some services have been outsourced and as new academies have been started or existing schools have taken on academy status. This has been offset by a number of employers exiting the Fund when all active members have left.

	2011/12	2012/13	2013/14	2014/15	2015/16
Active Employers	8	9	12	15	17

The next table shows the split of these employers by type at 31st March 2016 and also shows the number of employers who have ceased active membership of the Fund when either their contract has ended or the last active member has left.

	Active	Ceased
Administering Authority	1	-
Scheduled Body	9	-
Admitted Body	7	1
Total	17	1

The following is a list of the employers with current active contributing members.

Administering Authority: The Royal Borough of Kensington and Chelsea	
Scheduled Bodies	Admitted Bodies
Brunel Academy Cardinal Vaughan Academy Chelsea Academy Holland Park Academy Kensington Aldridge Academy Kensington and Chelsea College Latimer Academy Parkwood Hall Academy St. Charles Sixth Form College	Amey EPIC Hestia Octavia Opera Holland Park Tenant Management Organisation Westway Development Trust

The table below shows how the Fund's membership has changed over the last five years. The number of active contributing members in the Pension Fund has fallen by 5 per cent since 2012. In the same period, the number of pensioners and deferred members has risen, by 15 per cent and 19 per cent respectively. The active contributing members make up 31 per cent of the total membership.

	31st March 2012	31st March 2013	31st March 2014	31st March 2015	31st March 2016
Contributors	3,385	3,202	3,097	3,271	3,255
Pensioners & Dependents	2,430	2,515	2,656	2,693	2,798
Deferred	3,706	3,966	4,305	4,421	4,990
Total Membership	9,521	9,683	10,058	10,385	11,043

Communication policy statement

The Local Government Pension Scheme Regulations 2013 require Pension Funds to prepare, publish and maintain a communication policy statement. This statement sets out the methods used by the Fund to communicate with the various stakeholders, including scheme members, employers and their representatives.

The Fund's Communication policy statement can be found on the following link: <https://www.rbkc.gov.uk/council/how-council-manages-money/council-spending-and-finances/pension-fund-2014-15>

A revised version of this policy is currently out for consultation.

Sources of information

Further information about the benefits payable from the Pension Fund can be found on the national Local Government Pension Scheme website www.lgps.org.uk. For further information about the administration of the scheme in Kensington and Chelsea, visit the Fund's website:

<https://www.rbkc.gov.uk/council/how-council-manages-money/council-spending-and-finances/pension-fund-2014-15>

Internal Dispute Resolution Procedure

Members of pension schemes have statutory rights to ensure that complaints, queries and problems concerning pension rights are properly resolved.

To facilitate this process, an Internal Disputes Resolution Procedure has been established. If an issue cannot be resolved informally, a stage 1 appeal may be made to Maria Bailey, Bi-borough Pensions Manager via email to pensions@rbkc.gov.uk and thereafter, if necessary a further appeal may be made to Debbie Morris, Bi-borough Director of HR for Hammersmith & Fulham and Kensington and Chelsea.

If the problem remains unresolved, members then have the right to refer the matter to The Pensions Advisory Service (TPAS) which has a network of pension advisers who will try to resolve problems before they are referred on to the Pensions Ombudsman. However, the TPAS service may be invoked at any stage of the appeal process. Both TPAS and the Pensions Ombudsman can be contacted at: 11 Belgrave Road, London, SW1V 1RB.

Additional Voluntary Contributions

The Fund's AVC provider is Prudential Assurance. The AVC provider secure benefits on a money purchase basis for those members electing to pay AVCs. Members of the AVC schemes each receive an annual statement confirming the amounts held in their account and the movements in the year. In accordance with Regulation 4(2) (b) of the Pension Scheme (Management and Investment of Funds) Regulations 2009 the contributions paid and the assets of these investments are not included in the Pension Fund Accounts, but are recorded in a disclosure note.

4. ACTUARIAL INFORMATION

Funding Strategy Statement

The Local Government Pension Scheme Regulations 2013 require Pension Funds to prepare a funding strategy statement which sets out how the Fund will manage its liabilities and return to full funding. The strategy is considered by the Fund Actuary when undertaking the triennial valuation and setting the employer contribution rates. The statement is reviewed every three years in conjunction with the actuarial valuation.

The Fund's published statement can be found by following this link:

<https://www.rbkc.gov.uk/council/how-council-manages-money/council-spending-and-finance/pension-fund-2014-15>

Actuary's Statement

Introduction

The last full triennial valuation of the Royal Borough of Kensington and Chelsea Pension Fund ("the Fund") was carried out as at 31 March 2013 in accordance with the Funding Strategy Statement of the Fund. The results were published in the triennial valuation report dated March 2014. This statement gives an update on the funding position as at 31 March 2016 and comments on the main factors that have led to a change since the full valuation.

2013 Valuation

The results for the Fund at 31 March 2013 were as follows

- The Fund as a whole had a funding level of 95 per cent i.e. the assets were 95 per cent of the value that they would have needed to be to pay for the benefits accrued to that date, based on the assumptions used. This corresponded to a deficit of £33 million which is lower than the deficit at the previous valuation in 2010.
- To cover the cost of new benefits and to also pay off the deficit over a period of 7 years, a total contribution rate of 17.8 per cent of pensionable salaries would be needed.
- The contribution rate for each employer was set based on the annual cost of new benefits plus any adjustment required to pay for their share of the deficit.

Principal Actuarial Assumptions used to value the liabilities

Full details of the methods and assumptions used are described in the 2013 valuation report. The key financial assumptions adopted for the 2013 valuation were as follows:

Assumption	31 March 2013
Discount rate	5.9% p.a.
Pension increases	2.7% p.a.
Salary increases	1.0% until 31 March 2016 then 4.5% p.a.
Mortality	S1PA* tables with future improvements in line with the CMI 2012 Model with a long term rate of improvement of 1.5% per annum.
Commutation	Members will convert 50% of the maximum possible amount of pension into cash

Updated position

Using assumptions consistent with those adopted at the 2013 valuation, we estimate that the funding position at 31 March 2016 has improved compared to the position as at 31 March 2013.

The next formal valuation will be carried out as at 31 March 2016 with new contribution rates set from 1 April 2017.

Graeme D Muir FFA
Partner, Barnett Waddingham LLP

5. PENSION FUND ACCOUNTS

This section sets out the full audited financial statements of the Royal Borough of Kensington and Chelsea Pension Fund for the year ended 31st March 2016.

The Council's Responsibilities

The Council is required to:

- Make arrangements for the proper administration of its financial affairs and to secure that one of its officers has the responsibility for the administration of those affairs. In this Council, that officer is the Town Clerk.
- Manage its affairs to secure economic, efficient and effective use of resources and to safeguard its assets, and
- Approve the Statement of Accounts.

The Town Clerk's Responsibilities

The Town Clerk is responsible for the preparation of the Council's Statement of Accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom ("the Code").

In preparing this Statement of Accounts, the Town Clerk has:

- Selected suitable accounting policies and applied them consistently;
- Made judgements and estimates that were reasonable and prudent; and
- Complied with the Code.

The Town Clerk has also:

- Kept proper accounting records which were up to date; and
- Taken reasonable steps for the prevention and detection of fraud and other irregularities.

Certificate of the Town Clerk

I certify that the Pension Fund Accounts 2015-16 gives a true and fair view of the financial position of The Royal Borough of Kensington and Chelsea Pension Fund as at 31 March 2016 and income and expenditure for the year for the year ended 31 March 2016.

Nicholas Holgate, Town Clerk

The Pension Fund Account

	2015-16	2014-15	Notes
Dealings with members, employers and others directly involved in the fund	£'000	£'000	
Contributions	(23,685)	(24,664)	7
Individual Transfers in from other pension funds	(2,741)	(1,240)	
	(26,426)	(25,904)	
Benefits	26,861	26,028	8
Payments to and on account of leavers	26	54	
Individual transfers out to other pension funds	1,689	2,279	
	28,576	28,361	
Net (Additions)/withdrawals with members	2,150	2,457	
Management expenses	4,692	3,733	9
Returns on investments			
Investment income	(7,785)	(8,410)	10
Other income	(2)	(30)	
Taxes on income	71	102	
Profit and loss on disposal of investments and changes in the market value of investments	(14,245)	(128,086)	
Net return on investments	(21,961)	(136,424)	
Net (increase) / decrease in the net assets available for benefits during the year	(15,119)	(130,234)	
Opening Net Assets of the Scheme	(825,896)	(695,662)	
Closing Net Assets of the Scheme	(841,015)	(825,896)	

The Pension Fund Net Assets Statement

	31 March 2016	31 March 2015	
	£'000	£'000	
Investment Assets	822,325	808,111	12
Cash	10,543	9,469	12
Net value of investment assets	832,868	817,580	
Current assets	10,417	9,530	21
Current liabilities	(2,270)	(1,214)	22
Net assets of the fund available to fund benefits at the period end	841,015	825,896	

* The Fund's financial statements do not take account of liabilities to pay pensions and other benefits after the period end. The actuarial present value of promised retirement benefits is disclosed in Note 20.

Notes to the Pension Fund Account

1. Description of the Fund

The Royal Borough of Kensington and Chelsea (RBKC) Pension Fund (“the fund”) is part of the Local Government Pension Scheme (LGPS) and is administered by The Royal Borough of Kensington and Chelsea Council. The Council is the reporting entity for this pension fund.

The following description of the fund is a summary only. For more detail, reference should be made to the earlier sections in this report.

(a) General

The Fund is governed by the Public Service Pensions Act 2013. The fund is administered in accordance with the following secondary legislation:

- The Local Government Pension Scheme Regulations 2013 (as amended);
- The Local Government Pension Scheme (Transitional Provision, Savings and Amendment) Regulations 2014 (as amended); and
- The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (as amended).

It is a contributory defined benefits scheme established in accordance with statute, which provides pensions and other benefits to employees and former employees of the Council and the admitted and scheduled bodies to the Fund.

(b) Membership

Membership of the LGPS is voluntary and employees are free to choose whether to join the scheme, remain in the scheme or make their own personal arrangements outside the scheme. Organisations participating in the Fund include:

- **Scheduled bodies**, these are statutorily defined bodies listed within the LGPS Regulations, which are local authorities and similar bodies whose staff are automatically entitled to be members of the fund.
- **Admitted bodies**, these are other organisations that participate in the Fund under an admission agreement between the Fund and the relevant organisation. Admitted bodies include voluntary, charitable and similar bodies or private contractors undertaking a local authority function following outsourcing to the private sector.

The following table summarises the membership numbers of the scheme:

	31 March 2016	31 March 2015
	No.	No.
Active members	3,255	3,271
Pensioners receiving benefits	2,798	2,693
Deferred Pensioners	4,990	4,421
Total	11,043	10,385

(c) Funding

The Fund is financed by contributions and from interest and dividends on the Fund's investments. Contributions are made by active members of the Fund in accordance with the Local Government Pension Scheme Regulations 2013 and range from 5.5 per cent to 12.5 per cent of pensionable pay. Employer contributions are set based on the triennial actuarial funding valuation and the current contribution rates range from 12 per cent to 27 per cent of pensionable pay.

(d) Benefits

These benefits include retirement pensions, early payment of benefits on medical grounds and payment of death benefits where death occurs either in service or in retirement. The benefits payable in respect of service from 1 April 2014 are based on career average revalued earnings and the number of years of eligible service. The benefits payable in respect of service prior to 1 April 2014 are based on an employee's final pensionable pay and the number of years of eligible service. Pensions are increased each year in line with the Consumer Price Index.

(e) Governance

Investment Committee

The Council has delegated the investment arrangements of the scheme to the Investment Committee (the Committee), which decides on the investment policy most suitable to meet the liabilities of the Fund and has ultimate responsibility for the investment policy.

The Committee is made up of six elected representatives of the Council, including two opposition party representative, each of whom has voting rights. In addition, there are up to four co-opted members who may attend committee meetings, but have no voting rights.

The Committee reports to the full Council and has full delegated authority to make investment decisions. The Committee obtains and considers advice from the Town Clerk and, as necessary, from the Fund's appointed investment advisers, managers and actuary.

Pension Board

In line with the provisions of the Public Service Pensions Act 2013, the Council has set up a Pension Board to oversee the governance arrangements of the Pension Fund. The Board meets twice a year and has its own Terms of Reference. Board members are independent of the Investment Committee.

(f) Investment Policy

The *Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 2009 as amended* require administering authorities to

prepare and review from time to time a written statement of Investment Principles. This statement provides details of the Fund's investment policies including the types of investment to be held, Risk measurement and management and compliance with the Myner's principles of investment management.

The latest *Statement of Investment Principles* (SIP) was approved in February 2015 by the Investment Committee and is available on Council's website at: <https://www.rbkc.gov.uk/council/how-council-manages-money/council-spending-and-finances/pension-fund-2014-15>

The Fund's investment objective is to ensure that its assets are invested in a way that maximises the likelihood that benefits will be paid to members as they fall due and to ensure the continued long-term financial support from the sponsoring employers.

The Committee has delegated the management of the Fund's investments to 7 professional investment managers (see note 11) appointed in accordance with the regulations, and whose activities are specified in detailed investment management agreements and monitored on a quarterly basis.

Northern Trust act as the Fund's global custodian. They are responsible for safe custody and settlement of all investment transactions, collection of income and the administration of corporate actions.

2. Basis of the Preparation of the Financial Statements

The Statement of Accounts summarises the Fund's transactions for 2015-16 and its position at year end as at 31 March 2016. The Statement of Accounts has been prepared in accordance with the *Code of Practice on Local Authority Accounting in the United Kingdom 2015-16* (The Code) issued by the Chartered Institute of Public Finance and Accountancy ("CIPFA") which is based on International Financial Reporting Standards (IFRS) as amended for the UK public sector.

The accounts do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year, nor do they take into account the actuarial present value of promised retirement benefits.

3. Summary of Significant Accounting Policies

Fund Account – Revenue Recognition

(a) Contribution Income

Normal contributions, both from the members and from the employer, are accounted for on an accruals basis at the percentage rate recommended by the actuary in the payroll period to which they relate.

Employer deficit funding contributions are accounted for on the due dates on which they are due under the schedule of contributions set by the actuary or on receipt if earlier than the due date.

Employer's augmentation and pension strain contributions are accounted for in the period in which the liability arises. Any amount due in year but unpaid is classed as a current financial asset.

(b) Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the LGPS Regulations. Individual transfers in and out are accounted for when received or paid, which is normally when the member liability is accepted or discharged. Bulk (group) transfers are accounted for on an accruals basis in accordance with the terms of the transfer agreement.

Transfers in from members wishing to use the proceeds of their additional voluntary contributions to purchase Scheme benefits are accounted for on a receipts basis.

(c) Investment Income

Dividends from quoted securities are accounted for when the security is declared ex-dividend.

Investment income is reported gross of withholding taxes which are accrued in line with the associated investment income. Investment income arising from the underlying investments of the Pooled Investment Vehicles is reinvested within the Pooled Investment Vehicles and reflected in the unit price.

Interest income is recognised in the fund account as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination.

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is recognised as a current financial asset.

Fund Account – Expense Items

(d) Benefits Payable

Pensions and lump-sum benefits payable include all amounts known to be due as at the end of the financial year. Lump sums are accounted for in the period in which the member becomes a pensioner. Any amounts due, but unpaid, are disclosed in the net assets statement as current liabilities.

(e) Taxation

The Fund is an exempt approved fund under Section 1(1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. As the Council is the administering authority for the Fund, VAT input tax is recoverable

on all Fund activities, including investment expenses. Where tax can be reclaimed, investment income in the accounts is shown gross of UK tax. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax is accounted for as a Fund expense as it arises.

(f) Management Expenses

The Code does not require a breakdown of management expenses, however disclosure of expenses in accordance with the CIPFA guidance "Accounting for Local Government Pension Scheme Management costs" is provided in the interests of greater transparency.

All expenses are accounted for on an accruals basis to ensure costs for the full accounting period are accounted for in the Fund account. Staff costs associated with the running of the Fund (including administration and oversight and governance) are charged to the Fund along with an element of management, accommodation and overhead charges.

The fees of the Fund's external investment managers reflect their differing mandates. Management fees are usually linked to the market value of the Fund's investments and therefore may increase or reduce as the value of the investment changes. Fees are also payable to the Fund's custodian and other advisers.

Net Assets Statement

(g) Financial Assets

Financial assets are included in the net assets statement on a fair value basis as at the reporting date. Quoted securities and Pooled Investment Vehicles have been valued at the bid price ruling on the final day of the accounting period. Quoted securities are valued by Northern Trust, the Fund's custodian.

The values of the private equity investments are based on valuations provided by the general partners to the private equity funds. Valuations are usually undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

(h) Foreign Currency Transactions

Where appropriate, market values, cash deposits and purchases and sales outstanding listed in overseas currencies are converted into sterling at the rates of exchange ruling at the reporting date.

(i) Cash and Cash Equivalents

Cash and cash equivalents comprise cash in hand and deposits with financial institutions that are repayable on demand without penalty.

(j) Financial Liabilities

The Fund recognises financial liabilities at fair value as at the reporting date. A financial liability is recognised in the net assets statement on the date the Fund

becomes party to the liability. From this date, any gains or losses arising from changes in the fair value of the liability are recognised by the Fund.

(k) Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits is assessed by the scheme actuary in accordance with the requirements of IAS19 and relevant actuarial standards. As permitted under the Code, the fund has opted to disclose the actuarial present value of promised retirement benefits in Note 20.

(l) Additional Voluntary Contributions

Members of the Fund may choose to make Additional Voluntary Contributions (AVCs) into a separate scheme run by Prudential Assurance in order to obtain additional pensions benefits. The company is responsible for providing the investors with an annual statement showing their holding and movements in the year. AVCs are not included within the accounts in accordance with Regulation 4 (2)(b) of the LGPS (Management and Investment of Funds) Regulations 2009 . They are disclosed in Note 23.

4. Critical Judgements in Applying Accounting Practices

In applying the accounting policies set out in Note 3 above, the Council has had to make certain critical judgements about complex transactions or those involving uncertainty about future events.

Pension Fund Liability

The Pension Fund liability is calculated triennially by the appointed actuary with annual updates in the intervening years. The methodology used the intervening years follows generally agreed guidelines and is in accordance with IAS19. These assumptions are summarised in Note 20. The estimates are sensitive to changes in the underlying assumptions underpinning the valuations.

Unquoted Private Equity Investments

The fair value of private equity investments is unavoidably subjective. The valuations are based on forward-looking estimates and judgements involving many factors. Unquoted private equity assets are valued by the investment managers in accordance with industry standards. The value of private equity investments at the balance sheet date was £48.8 million (31 March 2015:£45.8 million).

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

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the amounts reported for assets and liabilities at the year-end and the amounts reported for income and expenditure during the year. Estimates and assumptions are made taking into account historical experience, current trends and other relevant factors. However, the nature of estimation means that the actual results could differ from the assumptions and estimates.

The items in the Net Asset Statement at 31 March 2016 for which there is a significant risk of material adjustment in the forthcoming financial year are summarised in the table overleaf.

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of promised retirement benefits	Estimation of the net liability to pay pensions depends on a number of complex judgments relating to the discount rates used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets. A firm of consulting actuaries is engaged to provide the fund with expert advice about the assumptions to be applied.	The effects on the net pension liability of changes in assumptions can be measured. For instance, <ul style="list-style-type: none"> • a 0.5 per cent increase in the discount rate assumption would result in a decrease in the pension liability of £90.9 million. • a 0.2 per cent increase in assumed earnings would increase the value of liabilities by approximately £4.3 million. • a one-year increase in assumed life expectancy would increase the liability by approximately £30.8 million.
Private Equity Investments	The fair value of private equity investments is unavoidably subjective. The valuations are based on forward-looking estimates and judgments involving many factors. Unquoted private equity assets are valued by the investment managers in accordance with industry standards.	The value of private equity investments at the balance sheet date was £48.8 million. There is a risk that this investment may be under or overstated in the accounts.

6. Events after the Balance Sheet Date

The result of the referendum on EU membership held on 23rd June 2016 was in favour of the UK to leave the EU. The long term financial impacts of “Brexit” cannot, as yet, be easily ascertained, however given that this condition did not exist at the balance sheet date, any such impacts insofar as they could be ascertained, constitute a non-adjusting event. In the shorter term, at 31st July 2016, the market value of the investments of the Fund had increased to approximately £932 million compared to the value placed on the net assets statement as at the reporting date of 31 March 2016. This mainly reflects global equity market movements.

7. Contributions Receivable

By category:	2015-16	2014-15
	£'000	£'000
Employees' contributions	6,523	6,374
Employer's contributions:		
Normal Contributions	13,211	13,346
Deficit recovery contributions	2,888	4,568
Augmentation Contributions	1,063	376
Total Employer's contributions	17,162	18,290
Total	23,685	24,664

By authority	2015-16	2014-15
	£'000	£'000
Administering authority	19,453	19,362
Scheduled bodies	1,866	1,289
Admitted bodies	2,366	4,013
Total	23,685	24,664

8. Benefits Payable

By category:	2015-16	2014-15
	£'000	£'000
Pensions	22,150	21,391
Commutation and lump sum retirement benefits	3,797	4,104
Lump sum death benefits	914	533
Total	26,861	26,028

The Fund paid benefits to members of the scheme who were previously employed by the bodies set out below (the summary excludes lump sum retirement benefits and death benefits for 2014-15 as this information is not held at employer level).

By authority	2015-16	2014-15
	£'000	£'000
Administering authority	24,844	19,740
Scheduled bodies	341	175
Admitted Bodies	1,676	1,476
Total	26,861	21,391

9. Management Expenses

	2015-16 £'000	2014-15 £'000
Administrative costs	598	233
Investment management expenses (see below)	3,885	3,277
Oversight and governance costs	209	223
Total	4,692	3,733

	2015-16 £'000	2014-15 £'000
Management fees	3,786	3,213
Transaction costs	60	23
Custody fees	39	41
Total	3,885	3,277

10. Investment Income

	2015-16 £'000	2014-15 £'000
Equity dividends	5,538	7,259
Pooled property investments	2,210	1,095
Private equity income	-	3
Interest on cash deposits	37	53
Total	7,785	8,410

11. Investments Analysed by Fund Manager

Fund Manager	31 March 2016		31 March 2015	
	Market Value £'000	%	Market Value £'000	%
L and G Liquidity	30,286	3.6	30,118	3.7
Baillie Gifford	174,080	20.9	176,326	21.6
Longview	223,011	26.8	213,867	26.2
L and G Equities	219,041	26.3	218,302	26.7
Pyrford	94,316	11.3	92,702	11.3
CBRE	27,217	3.3	25,660	3.1
KAMES	15,788	1.9	14,616	1.8
Adams Street	48,798	5.9	45,901	5.6
London CIV	150	-	0	-
Total Fund Managers	832,687	100	817,492	100
Investment income due	181		88	
Total Investments	832,868		817,580	

Although several allocations exceed 5 per cent of the Fund's value, all of the allocations to pooled funds are made up of underlying investments, each of which represents substantially less than 5 per cent.

12. Reconciliation in Movements in Investments

Market Value	1 April 2015	Purchases during the year and derivative payments	Sales during the year and derivative receipts	Net assets / liabilities movement	Changes in market value during the year	31 March 2016
2015-16	£'000	£'000	£'000	£'000	£'000	£'000
Sterling liquidity pooled fund (Legal & General)	30,118	-	-	-	168	30,286
Pooled active global equities (Baillie Gifford)	176,326	-	(55)	-	(2,191)	174,080
Active global equities (Longview)	213,867	48,602	(44,555)	-	5,097	223,011
Pooled passive global equities (Legal and General)	218,302	-	-	-	739	219,041
Pooled active global absolute return fund (Pyrford)	92,702	868	-	-	746	94,316
Pooled UK property fund (CBRE)	25,660	3	-	-	1,554	27,217
Pooled UK property fund (Kames)	14,616	439	-	-	733	15,788
Global private equity fund (Adams Street)	45,901	3,981	(8,267)	-	7,183	48,798
London CIV	0	150	-	-	-	150
Investment income due	88	-	-	93	-	181
Sub-Total	817,580	54,043	(52,877)	93	14,029	832,868
Current assets	142	-	-	2,799	-	2,941
Current liabilities	(1,214)	-	-	(556)	-	(1,770)
Cash deposits	9,388	-	-	(2,128)	216	7,476
Cash Overdraft	-	-	-	(500)	-	(500)
Net Investment Assets	825,896	54,043	(52,877)	(292)	14,245	841,015

Market Value	1 April 2014	Purchases during the year and derivative payments	Sales during the year and derivative receipts	Net assets / liabilities movement	Changes in market value during the year	31 March 2015
2014-15	£'000	£'000	£'000	£'000	£'000	£'000
Sterling liquidity pooled fund (Legal & General)	-	45,000	(15,000)	-	118	30,118
Pooled active global equities (Baillie Gifford)	145,279	-	-	-	31,047	176,326
Active global equities (Longview)	166,624	19,954	(16,222)	-	43,511	213,867
Pooled passive global equities (Legal and General)	139,979	45,000	-	-	33,323	218,302
Pooled active global absolute return fund (Barings)	89,656	35	(92,273)	-	2,582	-
Pooled active global absolute return fund (Pyrford)	86,607	3,385	(417)	-	3,127	92,702
Pooled UK property fund (CBRE)	22,781	-	-	-	2,879	25,660
Pooled UK property fund (Kames)	-	15,025	-	-	(409)	14,616
Global private equity fund (Adams Street)	33,500	8,563	(8,070)	-	11,908	45,901
Investment income due	103	-	-	(15)	-	88
Sub-Total	684,529	136,962	(131,982)	(15)	128,086	817,580
Current assets	1,540	-	-	(1,398)	-	142
Current liabilities	(451)	-	-	(763)	-	(1,214)
Cash deposits	10,044	-	-	(656)	-	9,388
Net Investment Assets	695,662	136,962	(131,982)	(2,832)	128,086	825,896

13. Classification of Financial Instruments

The following table shows the classification of the Fund's financial instruments and also shows the split between UK and overseas. All investments are quoted unless otherwise stated.

	31 March 2016			31 March 2015		
	Designated as fair value through profit and loss	Loans and receivables	Financial liabilities at amortised cost	Designated as fair value through profit and loss	Loans and receivables	Financial liabilities at amortised cost
Financial Assets						
Equities						
United Kingdom quoted	23,658			35,873		
United Kingdom unquoted	150			-		
Overseas	189,677			168,642		
Pooled funds - investment vehicles						
UK pooled liquidity fund	30,286			30,118		
Pooled global equities	393,121			394,628		
Pooled global absolute return funds	94,316			92,702		
Pooled property investments	42,138			40,251		
Pooled private equity funds (unquoted)	48,798			45,809		
Investment income due	181			88		
Cash		18,019			18,857	
Debtors		2,941			142	
Financial Liabilities						
Creditors			(1,770)			(1,214)
Cash Overdraft			(500)			-
Subtotal	822,325	20,960	(2,270)	808,111	18,999	(1,214)
Total		841,015			825,896	

The carrying value is the same as the fair value for all financial instruments held by the Fund.

14. Net Gains and Losses on Financial Instruments

	31 March 2016	31 March 2015
	£'000	£'000
Financial Assets		
Designated at fair value through profit and loss	14,096	128,104
Loans and Receivables	149	(18)
Net Gains and Losses	14,245	128,086

15. Valuation of Financial Instruments carried at fair value

The valuation of financial instruments has been classified into three levels, according to the quality and reliability of information used to determine fair values. The definitions of the levels are detailed below and the table showing the analysis is overleaf.

Level 1 – Quoted market price

Fair values are derived from unadjusted quoted prices in active markets for identical assets and liabilities. Examples are quoted equities, quoted index linked securities and unit trusts. All level 1 investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Level 2 – Using observable inputs

Quoted prices are not available for financial instruments at this level. The valuation techniques used to determine fair value use inputs that are based significantly on observable market data.

Level 3 – With significant unobservable inputs

Financial instruments at Level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data e.g. private equity investments.

The values of the private equity investments are based on valuations provided by the General Partners to the private equity funds. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which follow the valuation principles of IFRS and US GAAP. Valuations are undertaken annually at the end of December and cashflow adjustments are used to roll forward the valuations to 31 March as appropriate.

	31 March 2016			31 March 2015		
	Quoted market price Level 1	Using observable inputs Level 2	With significant unobserva ble inputs Level 3	Quoted market price Level 1	Using observable inputs Level 2	With significant unobserva ble inputs Level 3
Financial Assets						
Financial assets at fair value through profit and loss	731,238	42,139	48,948	722,051	40,251	45,809
Loans and receivables	20,960	-	-	18,999	-	-
Total Financial Assets	752,198	42,139	48,948	741,050	40,251	45,809
Financial Liabilities						
Financial liabilities at amortised cost	(2,270)	-	-	(1,214)	-	-
Total Financial Liabilities	(2,270)	-	-	(1,214)	-	-
Net Financial Assets	749,928	42,139	48,948	739,836	40,251	45,809
Total		841,015			825,896	

16. Nature of Risk Arising from Financial Instruments**Risk and Risk Management**

The Fund's primary long-term risk is that the Fund's assets will fall short of its liabilities. The Fund's liabilities are sensitive to inflation via pension and pay increases, to interest rates and to mortality rates.

The aim of investment risk management is to minimise the risk of an overall reduction in the value of the Fund and to maximise the opportunity for gains across the whole Fund portfolio. The Fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) and credit risk to an acceptable level. In addition, the Fund manages its liquidity risk to ensure there is sufficient liquidity to meet the Fund's forecast cash flows.

Responsibility for the Fund's investment strategy rests with the Investment Committee and is reviewed on a regular basis, along with the Pension Fund Risk Register. In order to meet the Fund's objective of being fully funded within 7 years of the 2013 actuarial valuation, the fund managers have been set differing targets appropriate to the types of assets they manage. The overall target for the scheme is to outperform a weighted average of these benchmarks by 2.3 per cent on a rolling three-year basis.

(a) Market Risk

Market risk is the risk of loss from fluctuations in equity and commodity prices, interest and foreign exchange rates and credit spreads. The level of risk exposure depends on market conditions, expectations of future price and yield movements and the asset mix.

The objective of the Fund's risk management strategy is to identify, manage and control market risk exposure within acceptable parameters, whilst optimising the return on risk.

Price Risk

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

The Fund is exposed to price risk. This arises from investments held by the fund for which the future price is uncertain. All securities represent a risk of loss of capital. The maximum risk resulting from financial instruments is determined by the fair value of the financial instruments. The Fund's investment managers aim to mitigate this price risk through diversification and the selection of securities and other financial instruments.

All assets with the exception of cash, other investment balances, debtors and creditors are exposed to price risk. The value of the assets exposed to price movements along with what the value would have been if prices had been 10 per cent higher or 10 per cent lower is shown below.

Assets exposed to price risk	Value £000	+ 10% £000	-10% £000
At 31 March 2016	821,994	904,193	739,795
At 31 March 2015	808,023	888,825	727,221

Interest Rate Risk

The Fund invests in financial assets for the primary purpose of obtaining a return on investments. Fixed interest securities and cash are subject to interest rate risks, which represent the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Investment Committee recognises that interest rates can vary and can affect both income to the Fund and the value of the net assets available to pay benefits.

Elements of the pooled investment vehicles (e.g. Fixed Interest Securities and Cash) are exposed to interest rate risk. The value of the assets exposed to interest rate movements along with sensitivity analysis is shown below.

<u>Assets exposed to interest rate risk</u>	Value £000	+ 1% £000	-1% £000
At 31 March 2016	107,507	108,582	106,432
At 31 March 2015	114,357	115,501	113,213

Currency Risk

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than pounds sterling.

Overseas equities, overseas index linked securities, cash in foreign currencies, and some elements of the pooled investment vehicles are exposed to currency risk. The table below shows the value of these assets at the balance sheet date and what the value would have been if currencies had been 10 per cent higher or 10 per cent lower.

<u>Assets exposed to currency risk</u>	Value £000	+ 10% £000	-10% £000
At 31 March 2016	642,709	706,980	578,438
At 31 March 2015	611,786	672,965	550,607

(b) Credit Risk

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the Fund's financial assets and liabilities.

In essence the Fund's entire investment portfolio is exposed to some form of credit risk. However, the selection of high quality fund managers, counterparties, brokers and financial institutions minimises credit risk that may occur.

(c) Liquidity Risk

Liquidity risk represents the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund therefore takes steps to ensure that the Fund has adequate cash resources to meet its commitments.

The Fund has immediate access to its cash holdings and majority of its assets are liquid assets. The only assets in the Fund which cannot be liquidated within a month are the private equity assets which amounted to £48.8 million at 31 March 2016 (£45.8 million at 31 March 2015).

17. Contractual Commitments

As at 31 March 2016, the Fund had a commitment to invest a further £14.8 million into the Adams Street private equity funds of funds. It is anticipated that these commitments will be spread over the next 10 years and will be largely offset by cash distributions from the investments made since 2007.

18. Stock Lending

The Fund does not participate in stock lending.

19. Funding Arrangements

The Scheme Regulations require that a full actuarial valuation is carried out every third year. The purpose of this is to establish that the Fund is able to meet its liabilities to past and present contributors and to review employer contribution rates.

The last such valuation for the Fund was carried out by Barnett Waddingham, as at 31 March 2013 in accordance with the Funding Strategy Statement of the Fund and Regulation 36 of the Local Government Pension Scheme (Administration) Regulations 2008. The results were published in the triennial valuation report which is available on the Council's website at the link below. The next valuation will take place as at 31 March 2016.

<https://www.rbkc.gov.uk/council/how-council-manages-money/council-spending-and-finances/pension-fund-2014-15>

The funding policy is set out in the Funding Strategy Statement. The key elements of the funding policy are:

- Set levels of employer contribution that will build up a Fund of assets that will be sufficient to meet all future benefit payments from the Fund, and to
- Build up the required assets in such a way that employer contribution rates are kept as low and stable as possible.

To reach the funding level of 100 per cent over a period of 7 years, the common contribution rate is 17.8 per cent of pensionable pay to be paid by each employing body participating in the Fund. In addition, each employing body has to pay an individual adjustment to reflect its own particular circumstances and funding position within the Fund. Details of each employer's contribution rate are contained in the *Statement to the Rates and Adjustment Certificate* in the triennial valuation report.

The actuarial valuation, done using the projected unit method, is based on financial and statistical assumptions, the main ones being:

Financial assumptions	March 2013
RPI Increases	3.5%
CPI Increases	2.7%
Salary Increases	4.5%
Pension Increases	2.7%
Discount Rate	5.9%

Other assumptions:

- Commutation – An allowance is included for future retirements to elect to take 50 per cent of the maximum additional tax-free cash up to HMRC limits.
- 50/50 Scheme Allowance – It is assumed that 5 per cent of active members will opt to pay 50 per cent of contributions for 50 per cent of benefits under the new scheme.
- Mortality Projection – Long term rate of improvement of 1.5 per cent per annum.

The actuary's smoothed market value of the scheme's assets at 31 March 2013 was £630 million and the actuary assessed the present value of the funded obligation at £663 million indicating a net liability of £33 million, resulting in a funding level of 95 per cent.

The next actuarial valuation of the Fund will be as at 31st March 2016 and will be published in 2017.

20. Actuarial Present Value of Promised Retirement Benefits

The table below shows the total net liability of the Fund as at 31 March 2016. The figures have been prepared by the Fund's actuary, only for the purposes of providing the information required by IAS26. In particular, they are not relevant for calculations undertaken for funding purposes or for other statutory purposes under UK pensions legislation.

In calculating the required numbers the actuary adopted methods and assumptions that are consistent with IAS19. In conducting the 2016 actuarial valuation referred to in paragraph 19, the Actuary will take into account the investment policy when determining the assumptions to be used.

	31 March 2016 £'000	31 March 2015 £'000
Present value of promised retirement benefits*	1,027,282	1,066,149
Fair value of scheme assets (bid value)	(841,015)	(825,896)
Net Liability	186,267	240,253

*Present value of promised retirement benefits comprises £991,170,000 in respect of vested obligation and £36,112,000 in respect of non-vested obligations.

The assumptions applied by the actuary are set out below:

Financial Assumptions

	31 March 2016	31 March 2015
RPI Increases	3.3%	3.2%
CPI Increases	2.4%	2.4%
Salary Increases	4.2%	4.2%
Pension Increases	2.4%	2.4%
Discount Rate	3.7%	3.3%

Demographic Assumptions

The post mortality tables adopted are the S1PA tables with a multiplier of 105 per cent for males and 95 per cent for females. These base tables are then projected using the CMI 2012 Model allowing for a long term rate of improvement of 1.5 per cent per annum.

Life expectancy from age 65		31 March 2016	31 March 2015
Retiring today	Males	22.5	22.4
	Females	25.8	25.7
Retiring in 20 years	Males	24.8	24.6
	Females	28.1	28.0

Other Assumptions

- Members will exchange half of their commutable pension for cash at retirement;
- Members will retire at one retirement age for all tranches of benefit, which will be the pension weighted average tranche retirement age; and
- 5 per cent of active members will take up the option under the new LGPS to pay 50 per cent of contributions for 50 per cent of benefits.

21. Current Assets

	31 March 2016 £'000	31 March 2015 £'000
Debtors:		
Contributions due - employers	346	100
Contributions due - employees	130	42
Sundry debtors	2,465	-
Cash balances	7,476	9,388
Total	10,417	9,530

	31 March 2016 £'000	31 March 2015 £'000
Analysis of debtors		
Central government bodies	131	-
Other local authorities	26	-
Royal Borough of Kensington and Chelsea	2,506	-
Other entities and individuals	278	142
Total	2,941	142

22. Current Liabilities

	31 March 2016 £'000	31 March 2015 £'000
Creditors:		
Sundry creditors	1,700	793
Benefits payable	70	421
Cash overdrawn	500	-
	2,270	1,214
	31 March 2016 £'000	31 March 2015 £'000
Analysis of creditors		
Central government bodies	313	-
Other local authorities	129	-
Royal Borough of Kensington and Chelsea	403	280
Other entities and individuals	925	934
Total	1,770	1,214

23. Additional Voluntary Contributions

The Council has made arrangements for current members to make additional payments through its payroll into a variety of funds operated by Prudential Assurance according to individuals' preferences. These funds are invested in equities, bonds, property and cash. The *Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 as amended* do not permit Additional Voluntary Contributions (AVCs) to be paid into the Fund, so they are not included in these accounts.

During 2015-16, AVC contributions of £481,000 were paid to the provider (2014-15 £516,000).

	Market Value 31 March 2016 £'000	Market Value 31 March 2015 £'000
<i>Prudential</i>	2,919	2,853*
Total	2,919	2,853

*The valuation as at March 2015 has been amended to reconcile to the opening figures of 2016 valuation provided by the AVC provider.

24. Related Party Transactions

The Fund is administered by the Royal Borough of Kensington and Chelsea. The Council incurred costs of £0.242 million in the financial year 2015-16 (2014-15 £0.302 million) in relation to the administration of the Fund and was reimbursed by the Fund for the expenses.

In year, and in total, the Council contributed £14.043 million to the Fund compared to £14.196 million in 2014-15. In addition £15,000 was owed by a Council maintained school in respect of March 2016 contributions.

As at 31 March 2016 the Council owed the Pension Fund a net amount of £2.103 million.

The Council has a significant relationship with one admitted body, the Kensington and Chelsea Tenant Management Organisation (TMO). The Fund received £1.187 million in employer contributions, deficit and early retirement costs from the TMO.

Key management personnel

The Code exempts local authorities from the key management personnel disclosure requirements of IAS24, on the basis that the disclosure requirements for officer remuneration and members' allowances detailed in section 3.4 of the Code satisfy the key management personnel disclosure requirements of IAS24. This applies in equal measure to the accounts of the RBKC Pension Fund.

The disclosure required by the legislation can be found in the main account of the Royal Borough of Kensington and Chelsea.

25. Agency Services

The Fund pays discretionary awards to the former employees of the Royal Borough of Kensington and Chelsea. The amounts are not included within the Fund Account but are provided as a service and fully reclaimed from the council. The gross sum paid out is disclosed below.

	2015-16	2014-15
	£'000	£'000
Payments on behalf of Royal Borough of Kensington and Chelsea	264	-
Total	264	-

Independent auditor's report to the members of the Royal Borough of Kensington and Chelsea on the pension fund financial statements published with the Pension Fund Annual Report and Accounts

We have examined the pension fund financial statements for the year ended 31 March 2016 on pages 22 to 42.

Respective responsibilities of the Town Clerk and the auditor

As explained more fully in the Statement of the Town Clerk's Responsibilities, the Town Clerk is responsible for the preparation of the pension fund financial statements in accordance with applicable law and the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

Our responsibility is to report to you our opinion on the consistency of the pension fund financial statements included in the Pension Fund Annual Report and Accounts with the pension fund financial statements included in the annual published statement of accounts of the Royal Borough of Kensington and Chelsea, and their compliance with applicable law and the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

In addition, we read the information given in the Pension Fund Annual Report and Accounts to identify material inconsistencies with the pension fund financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Our report on the administering authority's annual published statement of accounts describes the basis of our opinion on those financial statements.

Opinion

In our opinion, the pension fund financial statements are consistent with the pension fund financial statements included in the annual published statement of accounts of the Royal Borough of Kensington and Chelsea for the year ended 31 March 2016 and comply with applicable law and the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

Matters on which we are required to report by exception

The Code of Audit Practice requires us to report to you if:

- the information given in the Pension Fund Annual Report and Accounts for the financial year for which the financial statements are prepared is not consistent with the financial statements; or
- any matters relating to the pension fund have been reported in the public interest under section 24 of the Local Audit and Accountability Act 2014 in the course of, or at the conclusion of, the audit.

We have nothing to report in respect of these matters.

Andrew Sayers, for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants
15 Canada Square, London, E14 5GL
30 September 2016

5. CONTACTS

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Email: pensions@rbkc.gov.uk

Surrey County Council

Pension Services
Surrey County Council
Room 243 County Hall
Penrhyn Road
Kingston upon Thames
Surrey, KT1 2DN
Email: myhelpdeskpensions@surreycc.gov.uk
Telephone: 020 8213 2802

National Local Government Pension Scheme information website

www.lgps.org.uk

The Pensions Advisory Service (TPAS)

11 Belgrave Road
London SW1V 1RB
Telephone: 0845 601 2923
Email: www.pensionsadvisoryservice.org.uk/online-enquiry

The Office of the Pensions Ombudsman

11 Belgrave Road
London, SW1V 1RB
Telephone: 020 7630 2200
Email: enquiries@pensions-ombudsman.org.uk

6. GLOSSARY

Active member: Current employee who is contributing to a pension scheme.

Actuary: An independent professional who advises the Council on the financial position of the Fund. Every three years the actuary values the assets and liabilities of the Fund and determines the funding level and the employers' contribution rates.

Additional Voluntary Contributions (AVC): An option available to active scheme members to secure additional pension benefits by making regular contributions to separately held investment funds managed by the Fund's AVC provider.

Admitted Body: An organisation, whose staff can become members of the Fund by virtue of an admission agreement made between the Council and the organisation. It enables contractors who take on the Council's services with employees transferring, to offer those staff continued membership of the Fund.

Asset Allocation: The apportionment of a fund's assets between different types of investments (or asset classes). The long-term strategic asset allocation of a Fund will reflect the Fund's investment objectives.

Benchmark: A measure against which the investment policy or performance of an investment manager can be compared.

Deferred members: Scheme members who have left employment or ceased to be an active member of the scheme whilst remaining in employment, but retain an entitlement to a pension from the scheme.

Defined Benefit Scheme: A type of pension scheme, where the pension that will ultimately be paid to the employee is fixed in advance, and not impacted by investment returns. It is the responsibility of the sponsoring organisation to ensure that sufficient assets are set aside to meet the pension promised.

Employer Contribution Rates: The percentage of the salary of employees that employers pay as a contribution towards the employees' pension.

Equities: Ordinary shares in UK and overseas companies traded on a stock exchange. Shareholders have an interest in the profits of the company and are entitled to vote at shareholders' meetings.

Index: A calculation of the average price of shares, bonds, or other assets in a specified market to provide an indication of the average performance and general trends in the market.

Pooled Investment Vehicles: Funds which manage the investments of more than one investor on a collective basis. Each investor is allocated units which are revalued at regular intervals. Income from these investments is normally returned to the pooled fund and increases the value of the units.

Private Equity: Investments in companies not quoted on public stock exchanges. Commonly these are start up businesses (also known as venture capital) or buyouts of companies with a view to restructuring and selling on.

Return: The total gain from holding an investment over a given period, including income and increase or decrease in market value.

Scheduled Body: An organisation that has the right to become a member the Local Government Pension Scheme under the scheme regulations. Such an organisation does not need to be admitted, as it's right to membership is automatic.

Unrealised Gains/Losses: The increase or decrease in the market value of investments held by the fund since the date of their purchase.

