The Highland Council
Comhairle na Gàidhealtachd

The Highland Council Pension Fund

Annual Report and Annual Accounts
Aithris Chunntasan

2016 - 2017

Pensions Regulator Scheme Number: 10051259

Approved at
Pensions Committee
31/08/17

HIGHLAND COUNCIL PENSION FUND

ANNUAL REPORT AND ANNUAL ACCOUNTS 2016/17

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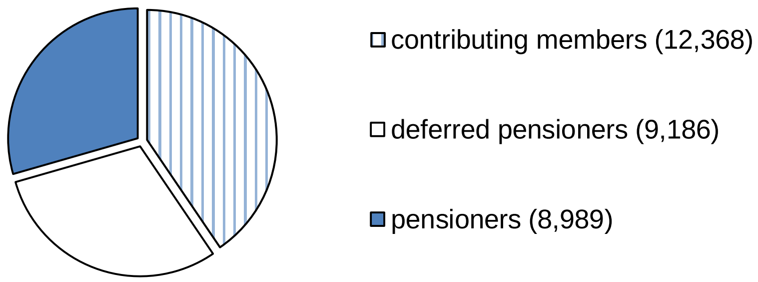
Background

Under the Local Government Pension Scheme (LGPS), The Highland Council is designated as an “Administering Authority” and is required to operate and maintain a pension fund - the Highland Council Pension Fund (HCPF) (“the Fund”). The Fund is established to provide retirement and death benefits to employees and dependants within the scheme.

The closing net assets of the Fund at 31 March 2017 are £1,765m (31 March 2016 £1,469m)**.**

The fund provides benefits for those employees of The Highland Council, Comhairle Nan Eilean Siar and 28 other scheduled and admitted bodies that are active members of the Fund.

Current Scheme Membership



Governance

The main legislation directing the governance requirements for the Fund is The Local Government Pension Scheme (Governance) (Scotland) Regulations 2015. The main impact of these regulations was the creation of The Scheme Advisory Board and Pension Boards.

The Scheme Advisory Board is a Scottish-wide Board which provides advice to the Scottish Ministers on the desirability of changes to the LGPS. It also provides guidance to the scheme mangers or pension boards on the effective and efficient administration and management of the LGPS and the pension fund.

Each scheme has its own Pension Board to ensure the regulations and legislation relating to the governance and administration of the LGPS are complied with.

For HCPF specifically, governance is undertaken by the Pensions Committee and Pensions Board which meet simultaneously to consider the same agenda and to whom Fund business has been delegated by The Highland Council. This includes the appointment and monitoring of investment managers, which is further delegated to the Pensions Investment Sub Committee.

More information on the governance process can be found in the Governance Section on Page 24.

Business Model and Risk

HCPF is managed and administered from The Highland Council Headquarters in Inverness.

Many of the Fund's activities are managed in-house and are accountable to the Pensions Committee and Board, Fund employers, and scheme members. The in-house support teams aim to provide a quality service to meet the needs of the Fund's stakeholders.

Pension Fund support functions cover the following areas:

- Membership and Benefits Administration
- Investment Management
- Funding and Accounting

Membership and Benefits Administration

For the benefit of all HCPF stakeholders the website below includes a broad range of information relating to the Fund.

http://www.highlandpensionfund.org

The Administration Strategy is one of the key documents available at the above website. It is reviewed regularly in consultation with employers.

a) General

2016/17 saw the Pension Administration team continue to play a central role in supporting The Highland Council and scheme members during both The Highland Council's Voluntary Severance (VS) and Employee Early Release schemes. The team has never before had to be relied upon to accommodate such a volume of work relating to VS and it is notable that the team performed exceptionally well.

The VS Scheme required over 200 calculations and payments to be provided to employees leaving under the scheme in 2016/17. Alongside dealing with retirements under VS, the volume of normal retirements continued at a similar rate to 2015/16 with 810 benefits coming into payment in 2016/17 compared to 606 in 2015/16. In addition, requests for estimates increased by 75% to 1,277 in 2016/17 compared to 730 in 2015/16.

The need to pay and provide guidance to employees granted VS was the main priority of 2016/17. In order to achieve this, the more regular tasks were reviewed and re-prioritised to ensure appropriate focus was placed on dealing with the VS activities. Further information on this prioritisation exercise is in section c) below.

b) Communication

The VS scheme required the Pension Administration team to produce meaningful estimates of benefits for around 820 eligible scheme members. With assistance from The Highland Council's Human Resources and Digital Services, the Pension Administration team were able to provide secure information to members online. This ensured an exceptionally high volume of enquiries could be handled whilst minimising the impact on additional staffing costs in the team.

This technology was also used to provide online Annual Benefits statements for the first time. This new initiative provided 17,562 members with online access to their personal pension data and saved the Pension Fund around £0.010m in printing and postage costs.

The Highland Council Pension Fund website received a number of new enhancements this year and now features a news page enabling the pension team to upload articles of interest immediately for scheme members to view.

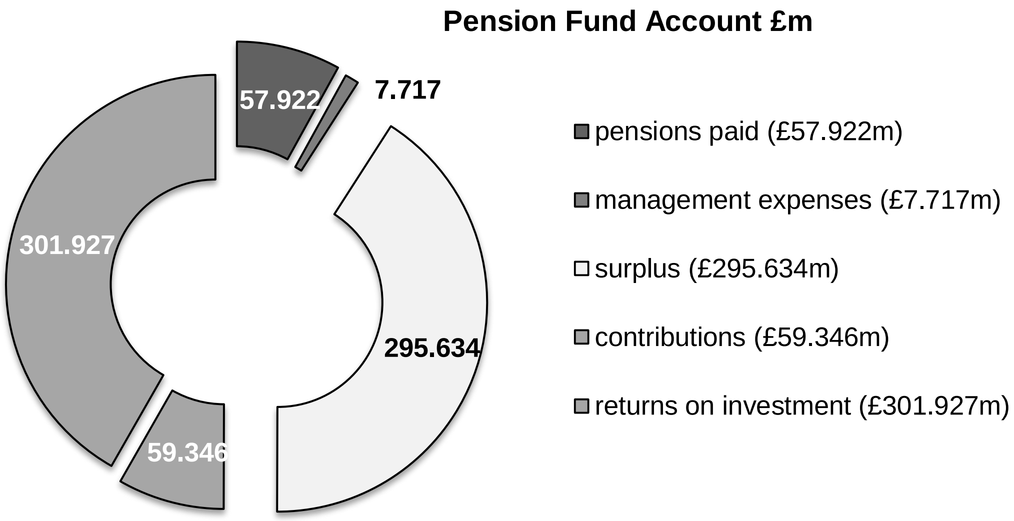
c) Performance

During 2016/17, the Pension Administration team has continued to take advantage of the electronic workflow function on the Pensions system and more key processes have been transferred to help provide the best possible service to members. Analysis of the workflow data shows that performance during the year was generally consistent with the previous year apart from activities, as mentioned earlier, where focus was re-prioritised on VS.

In particular, issuing notices to early leavers with several years to retirement age was given a lower priority than providing this information to leavers with an imminent retirement date. Although the overall indicator is down from the previous year, where payment of benefits was imminent, the necessary documentation was issued within the target date.

The key performance indicators (KPI) on page 18 reflect the exceptional nature of the past year and show the increased volume of benefits estimates, 1,277 in 2016/17 compared to 730 in 2015/16. Despite increased volumes, 94% of benefits estimates were issued within 10 days and levels of service were maintained at a similar level to 2015/16 (98%).

Delays in receiving new actuarial guidance from the Government Actuaries department in respect of transfers resulted in a stockpiling situation across all funds in Scotland contributed to the reduction in this KPI (transfers in from outwith Fund) compared to previous years.



Investment Management

The Fund income comes from member contributions, employer contributions and interest and returns on Fund investments. Fund expenditure relates to paying of member benefits and the administration costs of looking after the Fund. Thus far the Fund has been in surplus, i.e. the income is more than the expenditure and these surpluses are invested to generate further income for the Fund.

Investment Management of the Fund's assets is undertaken by external Fund managers and overseen by the Pensions Accounting Team with the support of AON Hewitt, the Fund's Investment Adviser.

The investment activity of the Fund is set out in The Statement of Investment Principles (SIP) which is reviewed regularly and agreed by the Pension Committee and Board and performance of the Fund Managers is reviewed by the Investment Sub Committee.

http://www.highlandpensionfund.org/media/2633/statement-of-investment-principles.pdf

Some of the main considerations in the SIP are:

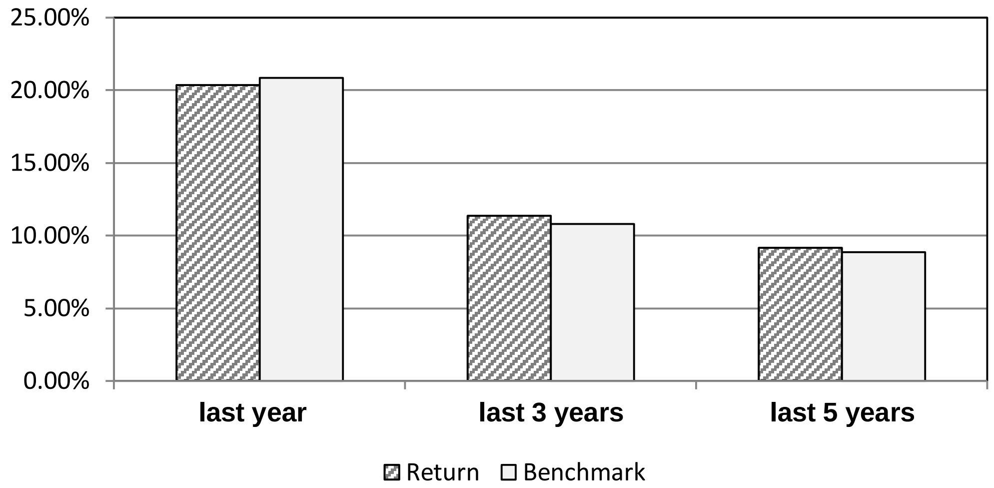
- the types of investment to be held
- the balance between different types of investment
- risk, including the ways in which risks are to be measured and managed
- the expected return on investments

Against a backdrop of continued uncertainty in the global economy, and volatility in the financial markets, the Fund returned 20.4%, slightly below the benchmark for the year of 20.9%.

Including the recent quarter results, the total Fund has outperformed its benchmark across two of the most recent four calendar quarters and across eight of the most recent twelve months. As a result, the total Fund fell marginally below benchmark over the rolling one year period, albeit with a double-digit gain in the fourth quarter. Apart from this, the Fund continues to deliver outperformance over every longer performance horizon.

During June 2016, there was the UK referendum on membership of the European Union (EU). The result of the UK's referendum on membership of the EU may affect the pension fund's risk profile by introducing potentially significant new uncertainties and instability in financial markets as the UK negotiates its exit from the EU. These uncertainties could have a material direct or indirect effect on the fund, its financial condition and operations although the extent is not quantifiable at this time. Also, since the 31 March 2017, the lack of an overall majority for the conservative party in the June 2017 election has resulted in a fall in Sterling and continuing uncertainty over Brexit negotiations.

The following graph shows the Fund return against the benchmark for the last year, the last 3 years and the last 5 years. Further information on the benchmarks used for the Fund is in the SIP.



The main drag on performance in 2016/17 was in private equity which is benchmarked against the MSCI All Countries World Index, an Index that has performed particularly well. Investment decisions for the Fund are considered over the longer term. Short term performance is reviewed closely, but, alone, it is unlikely to lead to investment changes. In 2016/17 the total Fund investments increased in value to £1,756m from £1,455m at the end of 2015/16.

A review of Investment performance is provided on page 20 of this report.

Funding and Accounting

Funding and accounting matters are undertaken internally by the Pensions Accounting team with the assistance of the Fund Actuary, Hymans Robertson.

Every three years the actuary carries out a valuation of the Fund. The main purpose of the valuation is to review the financial position of the Fund and determine the rate at which the employing bodies participating in the Fund should contribute in the future to ensure that the existing assets and future contributions will be sufficient to meet future benefit payments from the Fund. The last valuation was in 2014 and there have been no significant changes in the Fund position since then (which would trigger an interim review). There is work ongoing on the current valuation as at 31 March 2017 which is scheduled to be completed by the end of the financial year 2017/18.

The triennial valuation as at 31 March 2014 covers the financial years 2015/16 to 2017/18 and was concluded during early 2015. The results of this valuation are that the funding level shows a slight decrease since the 2011 valuation (96.2% compared to 96.8%) and an increase in the deficit from £33m to £52m. This is due to a number of factors but primarily because of the decrease in real gilt yields.

Alongside the completion of the Actuarial Valuation, the Funding Strategy Statement, which explains the setting of the employer contribution rates, was updated and approved at Pensions Committee in February 2017. The strategy can be viewed at

http://www.highlandpensionfund.org/media/2294/funding-strategy-statement.pdf

Risk

Awareness of risk and risk mitigation is a key aspect of the Fund's strategic and operational activities. Whilst it is not possible to eliminate risk entirely, the Fund has taken steps to evaluate risk and put mitigating controls in place to minimise its adverse effects.

A risk register is maintained and reported to the Pensions Committee.

http://www.highland.gov.uk/meetings/meeting/3804/pensions_committee_and_board

The five highest identified risks are:

1. Ongoing risk of members and officers being unaware of changes to LGPS governance, administration and investment matters.
2. Inefficiencies with the portfolio can result in unintended risks.
3. If the investment strategy is inconsistent with funding plans it can lead to setting inaccurate employer contribution rates.
4. Volatility in markets created by events such as Brexit could adversely impact returns leading to increasing deficits and additional costs.
5. Following the voluntary redundancy exercise, early release scheme and ongoing organisational restructure, there are risks associated with staff leaving which might lead to loss of knowledge and impact on service delivery.

These risks and mitigating controls in place to manage the risks have been reported to the Pensions Committee.

Looking Ahead

The ongoing volatility and uncertainty in the global economy and investment markets, and, linked to that, the continuing regime of public sector austerity over the medium and quite possibly longer term may have significant financial implications for the Fund and Fund employers.

The anticipated level of future returns on the equity markets both in the UK and globally is a particular concern and options are being considered to reduce the potential impact of this on the Fund.

In Conclusion

Our thanks and appreciation is extended to all Councillors and Officers for their continued input to the strong governance and management arrangements of the Fund.

Steve Barron Chief Executive	Derek Yule B.Com. FCPFA. IRRV (Hons) Director of Finance	Chairman Pensions Committee

31 August 2017

About the Fund

The Fund is part of the national Local Government Pension Scheme (LGPS) and is a contributory defined benefit pension scheme. The LGPS was set up by the UK Government to provide retirement and death benefits for local government employees, and those employed in similar or related bodies, across the whole of the UK.

The Fund is constituted under legislation governing the Local Government Superannuation Scheme. The primary Act of governance is the Superannuation Act 1972. Detailed regulations for the Scheme are contained in the Local Government Pension Scheme (Scotland) Regulations 1998, the Local Government Pension Scheme (Management & Investment of Funds) Regulations 2010, the Local Government Pension Scheme (Scotland) Regulations 2014, the Local Government Pension Scheme (Transitional Provisions and Saving) (Scotland) Regulations 2015 and the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015.

The Administering Authority (The Highland Council) runs The Highland Council Pension Fund, to make sure the Fund achieves the following objectives:

- Receives the proper amount of contributions from employees and employers, and any transfer payments;

  The Fund is built up by contributions from both employees and employers, together with interest and dividends from investments, out of which defined pensions and other benefits are paid.

  Employees' contributions to the Fund are fixed by statute and contributions payable by employers are fixed every three years following a report by an independent actuary who determines the level of contribution necessary to ensure that the Fund will be able to meet future benefits. A common contribution rate for the Fund of 20.2% of payroll contributions was set by the Actuary for the period 1 April 2015 to 31 March 2018 in the Triennial Actuarial Valuation report 2014.

- Invests the contributions appropriately, with the aim that the Fund's assets grow over time with investment income and capital growth.

  The Fund's assets are managed by appointed Investment Fund Managers. Once the cost of current benefits is met all surplus cash income is invested to meet future liabilities to employees within the Fund and deferred pension benefits.

- Uses the assets to pay Fund benefits to the members (as and when they retire, for the rest of their lives) and to their dependants (as and when members die), as defined in the LGPS Regulations (pre 1 April 2014 pensions benefits payable were based on final pensionable pay and length of pensionable service. Post 1 April the scheme became a career average scheme whereby members accrue benefits based on their pensionable pay in that year at an accrual rate of 1/49th which is updated annually in line with the Consumer Price Index). Assets are also used to pay transfer values and administration costs.

Funding Strategy Statement

A Funding Strategy Statement, which summaries the Fund's approach to funding liabilities, has been prepared and describes the strategy of The Highland Council acting in its capacity as Administering Authority for the funding of the Highland Council Pension Fund and is available at

http://www.highlandpensionfund.org/media/2294/funding-strategy-statement.pdf

Employees' benefits are guaranteed by the LGPS Regulations, and do not change with market values or employer contributions. Investment returns will help pay for some of the benefits, but with no guarantee as to the level of funding. Employees' contributions are fixed in the Regulations, at a level which covers only part of the cost of the benefits.

Therefore, employers need to pay the balance of the cost of delivering the benefits to members and their dependants.

The Funding Strategy Statement focuses on how employer liabilities are measured, the pace at which these liabilities are funded, and how employers or pools of employers pay for their own liabilities. This statement sets out how the Administering Authority has balanced the conflicting aims of:

- affordability of employer contributions,
- transparency of processes,
- stability of employers' contributions, and
- prudence in the funding basis.

There is also a regulatory requirement for the Fund to have a Funding Strategy Statement.

The Funding Strategy Statement provides details of the key elements of the funding strategy, the regulatory framework, responsibilities of key parties, links to the SIP, key risks (financial, demographic, regulatory and governance), calculation of employer contributions and actuarial assumptions.

Statement of Investment Principles

A Statement of Investment Principles (SIP) details the policy governing the Fund's investments. A summary of the SIP is set out on the following page.

The detailed version of the SIP expanding on the paragraphs below was approved by Committee and Board in February 2017.

http://www.highlandpensionfund.org/media/2633/statement-of-investment-principles.pdf

The Highland Council has delegated authority to the Pensions Committee to take decisions on behalf of the Pension Fund. The Pensions Board was set up to comply with the LGPS (Governance) (Scotland) 2015 Regulations and is responsible for assisting the Committee in securing compliance with pension governance and administration legislation and regulations and requirements of the Pensions Regulator.

The Investment Sub Committee is responsible for overseeing the management of the investments of the Fund and scrutinises the performance of the Fund's seven investment managers.

The Highland Council Pension Fund qualifies as an HMRC 'exempt approved scheme'.

Statement of Investment Principles – Summary

Background

The Highland Council is the administering authority of the Highland Council Pension Fund. Elected members recognise that they have fiduciary duties and responsibilities towards beneficiaries, employers and local taxpayers that are similar to those of Trustees in the private sector.

Advisors

Independent Investment Managers, Investment Consultants, Actuaries and Performance Measurement Consultants are employed to give ongoing expert advice and assistance in the managing of the Fund.

Funding Policy

The Fund is a defined benefit pension scheme which provides members with pensions and lump sums related to their final salaries. The fundamental objective is to meet these benefits on retirement, or the dependant's benefits on death before or after retirement.

The funding policy is directed to ensuring that in normal market conditions, all accrued benefits are fully covered by the actuarial value of the Fund's assets and that the appropriate level of contributions is agreed by the administering authority to meet the cost of future benefits accruing.

A Funding Strategy Statement for the Pension Fund has been prepared in accordance with Regulation 75A (1) of the Local Government Pension Scheme (Scotland) Regulations 1998 as amended by the Local Government Pension Scheme (Scotland) Amendment Regulations 2005. The Statement describes the strategy of The Highland Council in acting in its capacity as Administering Authority for the funding of the Highland Council Pension Fund. The Statement can be viewed at:

http://www.highlandpensionfund.org/media/2294/funding-strategy-statement.pdf

Investment Policy

The Fund's Investment Policy will be directed to ensuring that in normal market conditions, all accrued benefits are fully covered by the actuarial value of the Fund's assets and that an appropriate level of contributions is agreed by the administering authority to meet the cost of future employees' benefits accruing.

The long term investment objective of the Fund is to achieve a real rate return of 3-4% per annum on average. The Fund has agreed a strategic benchmark for each Manager. In broadly defining the assets to be held and setting the asset allocation this benchmark provides an efficient balance between risk and return in light of the liability profile, and funding level of the Fund.

The strategic benchmark is expected to produce a return over the long term in excess of the investment return assumed in the Actuarial Valuation. The Fund's assets are managed 78% on an active basis and these are expected to outperform their respective benchmarks over the long term. The remainder is managed on an index tracking (passive) basis.

Asset Mix of Investments

The overall investment portfolio for the Fund is weighted to the equity market, both UK and Overseas. However, the portfolio also has invested in Index-Linked Gilts, Property, UK Bonds, Overseas Bonds, Private Equity, Property Debt and Cash. This diverse range of investments over 7 different Managers (6 active and 1 passive) is employed to minimise the effect of risk and enhance overall performance of the Fund for its Members.

Each Manager, with the exception of the index tracking Manager, has full discretion in asset mix and stock selection, subject to the investment principles.

Strategic Asset Allocation

The Fund's strategic asset allocation targets are as follows.

Portfolio	Target	Actual	Comment
UK Equities	23.0%*	23.8%	18.2% Baillie Gifford (active) 4.8% L&G (passive)
Global Equities	38.0%	43.0%	14.8% Baillie Gifford (active) 12.0% Pyrford (active) 11.2% L&G (passive)
Private Equity	5.0%*	4.8%	Partners Group (active)
Property Debt	4.0%*	2.1%	Standard Life Investments (SLI) (active)
Property	10.0%	9.6%	Schroders (active)
Bonds	20.0%	16.7%	15.0% Fidelity (active) 5.0% L&G (passive)
	100%	100%	

* When private equity is fully funded.

Monitoring

The Fund's officers and, when required, advisers meet with each of its Investment Managers on a rotational basis and monitor performance quarterly relative to performance targets.

Adoption of the strategic benchmark and the performance monitoring constrains the Investment Managers from deviating significantly from the intended approach. It also permits flexibility to manage the Fund in such a way as to enhance returns.

Risk

The Fund pursues a policy of lowering risk through diversification of both investments and investment managers. A management agreement is in place for each Investment Manager, which sets out the relevant benchmark performance target, asset allocation ranges, and any restrictions, as determined by the Fund.

Realisation of Investments

The majority of the investments held by the Fund are quoted on major stock markets and may be realised quickly if required. Property investment is via pooled funds which are relatively illiquid (target asset allocation 10%). There are also private equity (target asset allocation 5%) and property debt investments (target asset allocation 4%) which are also very illiquid.

Underwriting

Managers are permitted to underwrite and sub-underwrite stock issues on the basis that the subject stock is already held in the portfolio or that the Manager wishes to acquire a long term holding.

Social, Environmental and Ethical Considerations (ESG)

The Fund recognises that ESG considerations are among the factors which Investment Managers will take into account, where relevant, when selecting investments for purchase, retention or sale. However, the over-riding consideration for Pension Committee members is their fiduciary duty to the scheme employers and scheme members.

Whilst recognising its over-riding fiduciary duties the Fund will continue to encourage its managers to engage on issues with companies in which it holds investment as the Fund believes that ESG issues will have a significant effect on the performance of investment portfolios through time. The key areas of ESG will be Employee Care, Human Rights, Sustainability and the Environment.

Engagement in this context is to involve the Investment Managers in:

- Meeting and corresponding with Companies on relevant issues.
- Working with the representatives of other shareholders, where appropriate.
- Voting against adverse proposals at Company AGM/EGMs.
- Reporting regularly on actions taken in this regard.

The managers are instructed to summarise their engagement activity in their quarterly Investment Reports.

Corporate Governance

The Fund ensures that the votes attached to its holdings in all UK quoted companies are exercised whenever practical. The Fund's votes are exercised by its Investment Managers in accordance with their own policies and practices and taking account of the Combined Code on Corporate Governance.

Custody

The Fund has a Global Custodian who ensures the safekeeping of all assets separate from each Investment Manager and other officials.

The Global Custodian also provides all the reporting data to the Council for performance monitoring and independent reconciliation purposes for each Investment Manager.

Stock Lending

During 2015, after evaluation of the risks and arrangements being put in place to ensure there would be adequate collateral to support stock lending arrangements, it was decided that The Fund would undertake stock lending. The Fund now has a stock-lending agreement with Northern Trust. Adequate collateral is held which consists of acceptable securities and government debt and as at 31 March 2017 the Fund held collateral (via the custodian) of 108.6% of stock lent.

The amount of lendable securities is limited to a maximum of 25% of the value of the Fund. This arrangement will be regularly reviewed to take account of changing market circumstances.

Compliance

Investment Managers and the Custodian will provide an annual statement to The Highland Council confirming that they have adhered to the investment principles contained in this document so far as is reasonably practicable.

Adhering to guidance given by Scottish Ministers, The Fund is compliant with the six revised principles on investment decision making for occupational pension schemes, as set out in guidance published by the Chartered Institute of Public Finance and Accountancy in December 2009 called 'Investment Decision Making and Disclosure in the Local Government Pension Scheme: A Guide to the Application of the Myners Principles'.

HIGHLAND COUNCIL PENSION FUND

ANNUAL REPORT AND ANNUAL ACCOUNTS 2016/17

Members & Advisors

All councillors on the Pensions Committee have been appointed by The Highland Council. The membership of the Pensions Committee, Pensions Board and Investment Sub Committee as at 31 March 2017 is outlined below.

Pensions Committee

Cllr D Fallows (Chairman)
Cllr I Cockburn
Cllr A Christie
Cllr H Carmichael
Cllr N Donald
Cllr M Green
Cllr R Laird
Cllr B Lobban
Cllr A MacKinnon
Cllr K MacLeod
Cllr B Thompson

Investment Sub Committee

Cllr A MacKinnon (Chairman)
Cllr H Carmichael
Cllr R Laird
Cllr B Lobban
Cllr K MacLeod
Cllr B Thompson

Non-Voting Members

Cllr A Campbell
(Comhairle nan Eilean Siar)
Mr E Macniven
(Trade Union representative)

Pensions Board

Cllr C Caddick, Highland Council (Chair)
Cllr A Campbell, Comhairle nan Eilean Siar
Ms L Leonard, representative for the other Employers
Mr D Macdonald, Unison
Ms L MacKay, Unison
Cllr T MacLennan, Highland Council
Mr E Macniven, GMB
Mr A Wemyss, Unite

Fund Custodian

Northern Trust

Fund Bankers

Clydesdale Bank

Investment Advisers

AON Hewitt

AVC Provider

Prudential Assurance

Fund Actuary

Hymans Robertson

Fund Investment Managers

Baillie Gifford
Fidelity International
Legal & General Investment Management
Partners Group
Pyrford International
Schroder Property Investment Management
Standard Life Investments

Admitted & Scheduled Bodies with Active Members

Administering Authority

The Highland Council (also Scheduled Body)

Scheduled Bodies

(specified in legislation as participating in the HCPF)

The Highland Council
Comhairle Nan Eilean Siar
Highland and Western Isles Valuation Joint Board
Scottish Fire & Rescue
Highlands of Scotland Tourist Board
Western Isles Tourist Board
HITRANS
Inverness College
Lews Castle College
Scottish Police Authority
Scottish Police Service Authority
The North Highland College

Admitted Bodies

(have applied and been accepted to participate in an LGPS fund under the terms of an ‘Admission Agreement ‘)

Bord Na Gaidhlig
An Comunn Gaidhealach
Cromarty Firth Port Authority
Eden Court Theatre
Forth & Oban Limited
Hebridean Housing Partnership
Highland Blindcraft
Highland & Islands Enterprise (HIE)
Highlife Highland
Inverness Harbour Trust
Morrison FM
NHS Highland
Skills Development Scotland
Stornoway Port Authority
University of the Highlands & Islands
Vacman Limited
Sight Action
WIPRO Holdings (UK) (new 1/3/17)

Administration Strategy and Performance

The Fund's Administration Strategy can be found on the Fund's website at

http://www.highlandpensionfund.org/media/2310/administration-policy.pdf

The strategy sets outs the roles and responsibilities of both the Administering Authority and scheme employer. The strategy also sets out a number of key processes and tasks to be benchmarked against expected results. Service level standards for the administering authority performance are based on industry standard Performance Indicators and are detailed in the following tables. The management commentary on page 4 provides further contextual information on these targets.

Administering Authority Performance

Task	Target	Number from 1/4/16 to 31/3/17	% completed within target	Number from 1/4/15 to 31/3/16	Previous Year %
New Entrants (includes re-employments)	Issue Statutory Notice within 14 days of receipt of a new start notice.	1,812	89%	1,435	99%
Early Leavers	The standard issue date is 10 days from receipt of leavers forms and 15 days for deferred benefit entitlement.*	913	57%	889	93%
Retirements including deferred benefits coming into payment	The standard issue date is 10 days of receipt of leaver option forms.	810	100%	606	98%
Deaths in Service	Contact next of kin within 5 days of notification being received.	21	100%	22	95%
Transfers in from out with Fund	The standard is to issue statutory notice within 10 days of receipt of payment.**	64	89%	37	100%
Transfers of pension rights out with Fund	Case to be finalised & payment made within 10 days of receipt of election payment.	28	96%	47	98%
Estimate of benefits	Issue within 10 days of request.	1,277	94%	730	98%

Scheme Employer Performance - Target performance 90%

Standard	Number from 1/4/16 to 31/3/17	% on target	Number from 1/4/15 to 31/3/16	Previous year %
New Start Notification – within 30 days of joining (or 10 days from first deduction if later).	1,812	93%	1,435	93%
Retirement information – to allow benefits to be paid on time.	474	86%	392	85%
Early leaver notification – within 30 days of leaving (or 10 days after last deduction if later).	913	94%	889	93%
Death in Service notification – within 7 days of death.	21	91%	22	100%
Year End Queries issued to employers, responses – within 14 days.	12	100%	23	100%

As outlined in the management commentary on page 5, 2016/17 was an unprecedented year whereby workloads were significantly increased due to VS.

Despite this increased workload, overall performance was maintained at similar levels to the previous year apart from two key performance indicators. The reason for the change in these performance indicators is as follows:

* Early Leavers – it was necessary to reprioritise tasks due to the increased volume of work attributable to VS. Although the overall indicator is down from the previous year, where payment of benefits was imminent, the necessary documentation was issued within the target date.

** Delays in receiving new actuarial guidance from the Government Actuaries department in respect of transfers resulted in a stockpiling situation across all funds in Scotland and impacted this indicator.

Investment Performance Report

Economic and Market Background

The UK economy proved to be resilient after the Brexit vote and economic conditions improved across many regions. Donald Trump's win in the US presidential election further boosted optimism in the US economy towards the end of the year. A pick-up in inflation across many regions from summer 2016 spurred a rotation from bond markets into equity markets, although bond markets rallied once more in Q1 2017.

Global equities rebounded following a poor start to 2016, with the MSCI AC World Index returning 17.0% over the 12 months in local currency terms. Sterling depreciated sharply on the back of the EU referendum result and renewed monetary policy. Consequently, the MSCI AC World index returned 32.2% in sterling terms. The US dollar appreciated on a trade-weighted basis.

The US Federal Reserve (Fed) raised the target federal funds rate by 0.25% from 0.50% to 0.75% in December. In March 2017, a further hike of 0.25% to 1.00% was announced. In contrast, accommodative monetary policy continued in other major countries.

UK gilt yields fell up until summer 2016, with an acceleration following the Brexit result and subsequent monetary policy actions undertaken by the Bank of England. From August, however, there was a turnaround in yields as inflation expectations increased. This upward yield move reversed somewhat in early 2017 as the reflation trade lost momentum with UK yields trending lower than other markets.

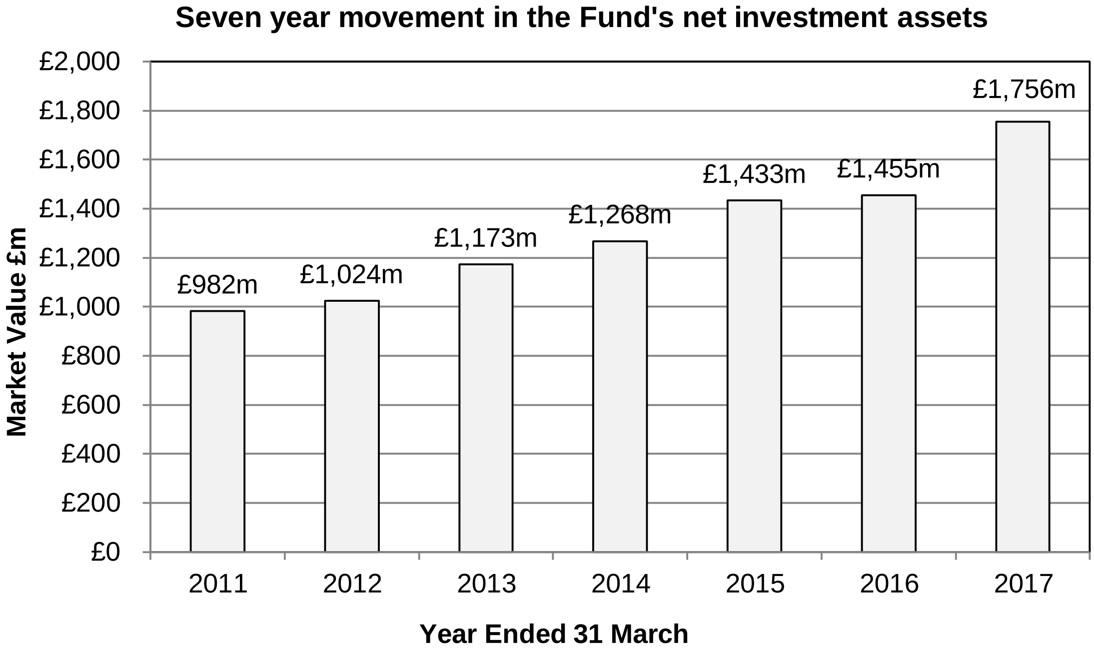
UK investment grade credit spreads narrowed by 0.34% to end the first quarter of 2017 at 1.28% following better than expected economic data and the Bank of England's extension to corporate bonds in its asset purchasing programme.

UK property returns remained positive over the year despite concerns over the impact of Brexit on the commercial real estate market.

Pension Fund Investment Performance

In the year to 31 March 2017, the Highland Council Pension Fund achieved a return on investments of 20.4% against its customised benchmark of 20.9%: underperformance of 0.5% against the benchmark. Although the general economy and market conditions remain challenging, the overall level of performance of the Fund in the year was positive.

The market value of the Fund's net investment assets as at 31 March 2017 was £1,756m (£1,455m at 31 March 2016). The seven year movement in the market value of the Fund's net investment assets is on the following page.



Across the longer term, the main contributors to the positive performance have been global equities, as a result of overall equity market performance (benchmark return) and strong manager stock selection and market out-performance (excess return) and property debt.

Details of the Fund's investments, analysed by investment category are shown in the financial statements (Note 13).

Actuarial Position

Employer contributions are assessed every three years by an independent actuary and expressed as a percentage of pensionable pay. The Common Rate of Contribution payable by each authority under Regulation 32 of the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008 is 20.2% of pensionable pay on the basis of the last actuarial valuation as at 31 March 2014, applying to financial years 2015/16 – 2017/18.

The "Projected Unit Method" was used for employers open to new staff and the "Attained Age Method" was used for employers that are closed to new staff. Individual employers' rates will vary from the common contribution rate depending on the demographic and actuarial factors particular to each employer. Full details of the contribution rates payable can be found in the 2014 actuarial valuation report and the funding strategy statement on the Pension Fund website.

http://www.highlandpensionfund.org/media/2295/valuation-report-march-2014.pdf

Demographic assumptions are used to estimate future consequences for the Fund. They take account of expected future trends (for instance future improvements in life expectancy) as well as the past experience in the Fund.

As at the 2014 actuarial valuation, the Fund was assessed as 96.2% funded (2011 valuation: 96.8%). This corresponded to a deficit of £52m at that time (2011 valuation: deficit of £33m). The 2014 funding level decreased marginally due to future investment returns achieved by the Fund being less than were assessed previously. In particular the real gilt yield has increased the value placed on the Fund's liabilities. More information on the recent actuarial valuation can be found in the Actuary's statement (page 82).

For the purposes of the contribution rates set for financial year 2016/17, the following assumptions from the triennial Valuation completed in 2014 were used.

Financial assumptions

Financial assumptions are used to estimate the amount of benefits and contributions payable and to place a current value on these benefits and contributions. The key financial assumptions are:

Financial Assumptions	March 2011		March 2014	
	Nominal p.a.	Real (RPI) p.a.	Nominal p.a.	Real (RPI) p.a.
Discount Rate	6.4%	3.4%	5.3%	2.6%
Salary Increase (excludes promotional increases)	5.0%	2.0%	4.5%	1.8%
Price Inflation/Pension Increases	3.0%	-	2.7%	-

The actuarial projection of the Market Value of the Fund's assets as at 31 March 2014 was £1,279m (2011 Valuation £991m). The aim is to achieve 100% solvency over a period of 20 years and to provide stability in employer contribution rates by spreading any increases in rates.

Mortality assumptions

The key mortality assumptions are that all members will follow the mortality experience based on the latest industry standard and using information from longevity experts.

Future life expectancy based on the Actuary's Fund-specific mortality review was:

Mortality assumption at age 65	Male	Female
Current pensioners	22.5	24.1
Future pensioners (assumed current age 45)	24.7	26.8

Commutation assumption

Half the members will commute their commutable pension for cash at retirement. Active members will retire one year later than they are first able to do so without reduction.

How to Contact Us

Website: http://www.highlandpensionfund.org/highland-pension-fund/about-us/contact-details/

Enquiries regarding Pension Fund Investments:

Corporate Budgeting, Taxation and Treasury
The Highland Council
Council Buildings
Glenurquhart Road
Inverness
IV3 5NX
Tel: 01463 702432
E-mail: treasury.team@highland.gov.uk

Enquiries regarding Pensions Contributions & Benefits:

Pensions Section
The Highland Council
Council Buildings
Glenurquhart Road
Inverness
IV3 5NX
Tel: 01463 702441
E-mail: pensions.section@highland.gov.uk
Website: www.highlandpensionfund.org

Annual Governance Statement

Scope of responsibility

The Highland Council acts as Administering Authority for the Highland Council Pension Fund. The Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded, properly accounted for, and used economically, efficiently and effectively. The Council has a statutory duty to make arrangements to secure best value under the Local Government in Scotland Act 2003.

In discharging this overall responsibility, the Council is responsible for putting in place proper arrangements for the governance of its affairs and facilitating the effective exercise of its functions. This includes arrangements for the management of risk.

The Council has approved and adopted a Local Code of Corporate Governance, which is consistent with the principles of the CIPFA/SOLACE framework 'Delivering Good Governance in Local Government'. The Code is available on our website. The authority's financial and management arrangements conform with the governance requirements of the CIPFA Statement on the role of the Chief Financial Officer in local government.

The Local Code of Corporate Governance evidences the Council's commitment to achieving good governance and demonstrates how it complies with the governance standards recommended by CIPFA. The document is regularly reviewed and updated.

The purpose of the governance framework

The governance framework comprises the systems and processes, and cultures and values, by which the Council is directed and controlled, and the activities used to engage with and lead the community. It enables the Council to monitor the achievement of its strategic objectives and to consider whether those objectives have led to the delivery of appropriate, cost effective services.

The system of internal control is a significant part of that framework and is designed to manage risk to an acceptable level, and provide reasonable, but not absolute, assurance that policies, aims and objectives can be delivered. The system of internal control is based on an ongoing process designed to identify and prioritise the risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The governance framework has been in place for the year ended 31 March 2017 and up to the date of approval of the Annual Accounts.

The governance framework

The Local Code is based upon the following six principles:

1. Focusing on the purpose of the Authority and on outcomes for the community and creating and implementing a vision for the local area.
2. Members and officers working together to achieve a common purpose with clearly defined functions and roles.
3. Promoting values for the Authority and demonstrating the values of good governance through upholding high standards of conduct and behaviour.
4. Taking informed and transparent decisions which are subject to effective scrutiny

and managing risk.
5. Developing the capacity and capability of members and officers to be effective.
6. Engaging with local people and other stakeholders to ensure robust public accountability.

The Pension Fund has a separate Governance Policy Statement which is one of a number of key documents it must hold and this was updated to reflect the changes in governance arrangements as a result of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015. This Statement was approved by the Pensions Committee in September 2016.

Review of effectiveness

The Highland Council has put in place appropriate management and reporting arrangements to enable it to satisfy itself that its approach to corporate governance is adequate and effective in practice. The Depute Chief Executive/Director of Corporate Development has been given responsibility for:

- overseeing the implementation of the Local Code of Corporate Governance and monitoring its operation.
- reviewing the operation of the Local Code of Corporate Governance in practice.
- reporting annually to the Council on compliance with the Local Code and any changes required to maintain it and ensure its effectiveness.

In fulfilling these duties, the Depute Chief Executive/Director of Corporate Development has taken into account the results of reviews of internal control that have been carried out by Internal Audit.

The Council's corporate governance arrangements are subject to annual review by Internal Audit and the work undertaken in respect of the Local Code during this year has not identified any control weaknesses in these arrangements.

The Internal Audit Service operates in accordance with the Public Sector Internal Audit Standards (the Standards). Section 2450 of the Standards states that "the annual Internal Audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control". In addition, the annual report must incorporate:

- the opinion;
- the summary of work that supports that opinion; and
- a statement on conformance with the Standards and the results of the quality assurance and improvement programme.

The Corporate Audit Manager's responsibilities in this regard will be discharged through the presentation of the Internal Audit Annual Report 2016/17 to the Audit and Scrutiny Committee on 26 June 2017.

A review of the adequacy and effectiveness of the systems of internal control for the financial year 2016/17 has not identified any control issues.

The seven Fund Managers and the Global Custodian each provide an annual assurance report (AAF 01/06/ ISAE 3402) which sets out the control procedures in place during the year, and includes an assessment, by an independent accountant, of the effectiveness of the systems of internal controls in operation throughout the period examined. These reports were obtained and reviewed, and it was confirmed that the appropriate assurances were provided by the independent accountants.

The 2016/17 Internal Audit plan comprised of the following two audits:

- Matters arising from the Statement of Internal control for the financial year 2015/16. This report had the audit opinion of "Substantial Assurance" and contained 2 medium grade recommendations, both of which have been implemented as agreed.
- A review of Pensions Contributions which looked at transactions relating to 2015/16. Again this report had the opinion of "Substantial Assurance" with 3 recommendations comprising of 2 medium and 1 low priority grades. All management agreed actions have been satisfactorily implemented.

Audit recommendations are action tracked to ensure that the management agreed actions have been satisfactorily implemented. As detailed above, a total of 5 audit recommendations were made during the year and have all been actioned as agreed.

From August 2016 the intercompany reconciliation has been completed regularly with a monthly reconciliation being completed from January 2017.

On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's internal control systems for the year to 31 March 2017.

We have been advised on the implications of the result of the review of the effectiveness of the governance framework by the Audit and Scrutiny Committee and that the arrangements continue to be regarded as fit for purpose in accordance with the governance framework. Internal Audit commits to monitoring implementation of any future recommendations as part of the next annual review.

Steve Barron Chief Executive	Chairman Pensions Committee

31 August 2017

On behalf of the members and senior officers of the Highland Council.

Governance Compliance Statement

The Regulations that govern the management of LGPS funds in Scotland require that a Governance Compliance Statement is published. The Governance Compliance Statement sets out the extent to which governance arrangements comply with best practice. The following arrangements were in place for financial year 2016/17.

Principle	Fully Compliant	Comments
Structure		
The management of the administration of benefits and strategic management of Fund assets clearly rests with the main committee established by the appointing Council.	Yes	The Highland Council as administering authority has delegated all pension scheme matters to the Pensions Committee. Meeting at the same time as the Committee, the Pensions Board assists the Committee in complying with Pensions Regulator requirements. In addition a small Investment Sub Committee has been established to enhance the Council's management and investment of the assets of the Pension Fund in accordance with the respective objectives and strategies of the Fund.
That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.	Yes	The Pensions Committee has members representing other employers and two voting members representing scheme members. The Pensions Board has 4 trade union members and 4 employer representatives. The Investment Sub Committee has two non-voting members representing other employers.
That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	Yes	The Pensions Committee and the Pensions Board meet concurrently. The minutes of the Investment Sub Committee are presented to the Pensions Committee and Board and there is significant commonality in the membership of the two committees.
That where a secondary committee or panel has been established, at least one seat of the main committee is allocated for a member from the secondary committee or panel.	Yes	The minutes of the Investment Sub Committee are presented to the Pensions Committee and Board and there is significant commonality in the membership of the two committees.

Principle	Fully Compliant	Comments
Representation		
That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include: • Employing authorities (including non-scheme employers, e.g. admitted bodies). • Scheme members (including deferred and pensioner scheme members). • Where appropriate, independent professional observers. • Expert advisors (on an ad-hoc basis).	Yes	As stated above there are employer and employee representatives on both Pension Fund Committees and the Pension Board. The Fund's investment advisers regularly attend the Pension Investment Sub-Committee and the Fund's actuaries attend the Pension Committee and Board when appropriate. In addition, Fund Managers attend the Investment Sub Committee on a rotational basis.
That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.	Yes	All Pensions Committee and Board members are provided with training, as well as access to papers in advance of Committee meetings and have the opportunity to contribute to the decision making process. There is a Pensions Board which is a bipartite body (set up 1 April 2015) with an equal number of representatives from local government employers and relevant trade unions. There must be a minimum of 4 from each side.
Selection and Role of Lay Members		
That committee or panel members are made fully aware of the status, role and function that they are required to perform on either a main or secondary committee.	Yes	A comprehensive training programme including induction is in place. Training for Pension Committee, Pensions Board and Investment Sub Committee members includes presentations from investment managers, Custodian, actuary and investment advisors. Attendance at meetings and training is monitored and reported.
That at the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.	Yes	The declaration of Member's interests is a standard item on the agenda of the Pension Fund Committee, Pension Board and Investment Sub Committee.

Principle	Fully Compliant	Comments
Voting		
The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees.	Yes	The policy on voting rights is clearly stated in the remits of the Pension Fund Committee, Board and Investment Sub Committee.
Training /Facility Time /Expenses		
That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision making process.	Yes	There is a training, knowledge and skills policy in place which was approved by Pensions Committee in September 2016 which incorporates the CIPFA Local Pensions Boards Technical Knowledge and Skills framework, including the self-assessment matrix. This Policy also highlights the assessment and training resources provided by the Pensions Regulator and sets out a training programme for 2016/17. The training policy recognises the importance of ensuring that it has the necessary resources to discharge its pension's administration responsibilities and that all staff and members charged with financial administration, governance and decision-making with regard to the pension scheme are fully equipped with the knowledge and skills to discharge the duties and responsibilities allocated to them.
That where such a policy exists it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	Yes	All members are treated equally under the training policy regardless of whether or not they have voting rights.
That the administering authority considers the adoption of annual training plans for committee members and maintains a log of all such training.	Yes	Members receive training each year and this is monitored and reported.
Meeting Frequency		
That an administering authority's main committee or committees meet at least quarterly.	No	The Pensions Committee and Board meet twice a year with the option to hold special meetings as necessary.

Principle	Fully Compliant	Comments
That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committees sits.	Yes	The Investment Sub Committee meets at least four times a year with the option to hold special meetings as necessary. The Investment Sub-Committee meetings will be timed so minutes can be presented to the Pensions Committee and Board.
That an administering authority who does not include lay members in their formal governance arrangements must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	N/A	There is a Scheme Members' representative on the Pensions Committee. The Pensions Board has an equal number of representatives from local government employers and relevant trade unions.
Access		
That subject to any rules in the council's constitution, all members of main and secondary committees or panels have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	Yes	All Members of the Pension Fund committees, Board and Investment Sub Committee have full access to agendas, reports and minutes. Voting rights are restricted to Highland Council Elected Members.
Scope		
That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Yes	The Pension Committee has an overview of investment, funding and member benefit matters. The Pensions Board assists the Committee with securing compliance with pension legislation and regulations.
Publicity		
That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express interest in wanting to be part of those arrangements.	Yes	The Highland Council publishes governance documents and communicates regularly with employers and scheme members. http://www.highlandpensionfund.org/highland-pension-fund/about-us/forms-and-publications/

Steve Barron
Chief Executive

Chairman
Pensions Committee

31 August 2017

On behalf of the members and senior officers of the Highland Council.

Statement of Responsibilities

The Authority's Responsibilities

The Highland Council, as the administering authority for the Highland Council Pension Fund, is required to:

- make arrangements for the proper administration of its financial affairs and to secure that the proper officer of the authority has responsibility for the administration of those affairs (section 95 of the Local Government (Scotland) Act 1973). In this authority that officer is the Director of Finance.
- manage its affairs, to secure economic, efficient and effective use of resources and safeguard its assets.
- Ensure that Annual Accounts are prepared in accordance with legislation (The Local Authority Accounts (Scotland) Regulations 2014), and so far as is compatible with that legislation in accordance with proper accounting practices (section 12 of the Local Government in Scotland Act 2003).
- Approve the Annual Accounts for signature.

Chairman
Pensions Committee

31 August 2017

The Director of Finance's Responsibilities

The Director of Finance is responsible for the preparation of the Pension Fund'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 Accounting Code).

In preparing this statement of accounts, the Director of Finance has:

- selected suitable accounting policies and applied them consistently
- made judgements and estimates that were reasonable and prudent
- complied with legislation
- complied with the local authority Accounting Code (in so far as it is compatible with legislation)

The Director of Finance has also:

- kept adequate accounting records which are up to date
- taken reasonable steps for the prevention and detection of fraud and other irregularities.

I, the Director of Finance of Highland Council as Chief Finance Officer certify that the financial statements give a true and fair view of the financial transactions of the Fund for the year ended 31 March 2017.

Derek Yule
B.Com. FCPFA.
IRRV (Hons)
Director of Finance

31 August 2017

Independent Auditor's Report

Independent auditor's report to the members of the Highland Council as administering authority for the Highland Council Pension Fund and the Accounts Commission

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 120 of the Code of Audit Practice approved by the Accounts Commission, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Report on the audit of the financial statements

Opinion on financial statements

We certify that we have audited the financial statements in the annual accounts of the Highland Council Pension Fund for the year ended 31 March 2017 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Pension Fund Account, Net Assets Statement and Accounting Policies and Notes to Accounts. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the 2016/17 Code).

In our opinion the accompanying financial statements:

- give a true and fair view in accordance with applicable law and the 2016/17 Code of the financial transactions of the fund during the year ended 31 March 2017 and of the amount and disposition at that date of its assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2016/17 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Basis of opinion

We conducted our audit in accordance with applicable law and International Standards on Auditing in the UK and Ireland (ISAs (UK&I)). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are fully independent of the fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standards for Auditors, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of the Director of Finance for the financial statements

As explained more fully in the Statement of Responsibilities, the Director of Finance is responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Director of Finance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibilities for the audit of the financial statements

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable legal requirements and ISAs (UK&I) as required by the Code of Audit Practice approved by the Accounts Commission. Those standards require us to comply with the Financial Reporting Council's Ethical Standards for Auditors. An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the circumstances of the fund and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance; and the overall presentation of the financial statements.

Our objectives are to achieve reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK&I) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Other information in the annual accounts

The Director of Finance is responsible for the other information in the annual accounts. The other information comprises the information other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except on matters prescribed by the Accounts Commission to the extent explicitly stated later in this report.

In connection with our audit of the financial statements in accordance with ISAs (UK&I), our responsibility is to read all the financial and non-financial information in the annual accounts to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Report on other requirements

Opinions on other prescribed matters

We are required by the Accounts Commission to express an opinion on the following matters.

In our opinion, based on the work undertaken in the course of the audit

- the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with statutory guidance issued under the Local Government in Scotland Act 2003;
- the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements

and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016); and

- the information given in the Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations 2014.

Matters on which we are required to report by exception

We are required by the Accounts Commission to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Joanne Brown CPFA, (for and on behalf of Grant Thornton UK LLP)
110 Queen Street
Glasgow
G1 3BX
31 August 2017

Pension Fund Account

This statement shows a summary of the income and expenditure that the Pension Fund has generated and incurred in delivering the Local Government Pension Scheme. Included is the income generated from employer and employees' contributions and investment income, as well as the cost of providing benefits and administration of the Fund.

restated 2015/16 £000		Notes	**2016/17 £000**
	Dealings with members, employers and others directly involved in the scheme		
55,232	Contributions receivable	8	57,296
1,709	Individual Transfers in from other pension funds		2,050
56,941			59,346
(51,594)	Benefits payable	9	(56,922)
(3,095)	Payments to and on account of leavers	10	(1,000)
(54,689)			(57,922)
2,252	**Net additions/(reductions) from dealings with members**		**1,424**
(7,024)	Management expenses	11	**(7,717)**
(4,772)	**Net additions/(withdrawals) including fund management expenses**		**(6,293)**
	Returns on Investments		
28,375	Investment income	12	31,144
(214)	Taxes on income from equities		(260)
(2,914)	Profit and losses on disposal of investments and changes in values of investments	13.1	271,043
25,247	**Net Return on Investments**		**301,927**
20,475	**Net increase in the net assets available for benefits during the year**		**295,634**
1,448,794	Opening net assets as at the start of the year		1,469,269
1,469,269	**Closing net assets as at the end of the year**		**1,764,903**

Net Assets Statement as at 31 March 2017

The Net Assets Statement sets out the value, as at the Statement date, of all assets and liabilities of the Fund.

As at 31/03/16 £000		Notes	**As at 31/03/17 £000**
1,430,093	Investment assets	13.1	1,703,807
21,227	Cash deposits	13.1	37,479
4,080	Investment income due	13.1	3,764
927	Amounts receivable for sales	13.1	10,612
(1,282)	Amounts payable for purchases	13.1	(135)
1,455,045	**Total net investment assets**	13.1	**1,755,527**
	Long term assets		
1,013	**Long term debtors**	23	**792**
	Current assets		
6,815	Short term debtors		8,753
10,200	Bank accounts		3,045
17,015		22	**11,798**
	Less current liabilities		
(3,804)	Sundry creditors	24	(3,214)
13,211	**Net current assets**		**8,584**
1,469,269	**Closing net assets as at the end of the year available to fund benefits at the period end**[1]		**1,764,903**

Derek Yule
B.Com. FCPFA IRRV (Hons).
Director of Finance
31 August 2017

[1] 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 at Note 17.

Accounting Policies and Notes to Accounts

1. Description of Fund

The Highland Council is the administering authority of the Highland Council Pension Fund ("the Fund") and is the reporting entity for the Fund.

General

The Fund is part of the national Local Government Pension Scheme (LGPS) and is a contributory defined benefit pension scheme. The LGPS was set up by the UK Government to provide retirement and death benefits for local government employees, and those employed in similar or related bodies, across the whole of the UK.

The Fund is constituted under legislation governing the Local Government Superannuation Scheme. The primary Act of governance is the Superannuation Act 1972. Detailed regulations for the Scheme are contained in the Local Government Pension Scheme (Scotland) Regulations 1998, the Local Government Pension Scheme (Management & Investment of Funds) Regulations 2010, the Local Government Pension Scheme (Scotland) Regulations 2014, the Local Government Pension Scheme (Transitional Provisions and Saving) (Scotland) Regulations 2015 and the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015.

The Administering Authority (The Highland Council) runs The Highland Council Pension Fund, to make sure the Fund achieves the following objectives:

- Receives the proper amount of contributions from employees and employers, and any transfer payments;

  The Fund is built up by contributions from both employees and employers, together with interest and dividends from investments, out of which defined pensions and other benefits are paid.

  Employees' contributions to the Fund are fixed by statute and contributions payable by employers are fixed every three years following a report by an independent actuary who determines the level of contribution necessary to ensure that the Fund will be able to meet future benefits. A common contribution rate for the Fund of 20.2% of payroll contributions was set by the Actuary for the period 1 April 2015 to 31 March 2018 in the Triennial Actuarial Valuation report 2014.

- Invests the contributions appropriately, with the aim that the Fund's assets grow over time with investment income and capital growth.

  The Fund's assets are managed by appointed Investment Fund Managers. Once the cost of current benefits is met all surplus cash income is invested to meet future liabilities to employees within the Fund and deferred pension benefits.

- Uses the assets to pay Fund benefits to the members (as and when they retire, for the rest of their lives) and to their dependants (as and when members die), as defined in the LGPS Regulations (pre 1 April 2014 pensions benefits payable were based on final pensionable pay and length of pensionable service. Post 1

April the scheme became a career average scheme whereby members accrue benefits based on their pensionable pay in that year at an accrual rate of 1/49th which is updated annually in line with the Consumer Price Index). Assets are also used to pay transfer values and administration costs.

2. Basis of Preparation

The Pension Fund Accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 which is based upon International Reporting Standards (IFRS) as amended for the UK public sector.

The accounts summarise the transactions of the Fund and report on the net assets available to pay pension benefits. The accounts do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present value of the promised retirement benefits, valued on an International Accounting Standard (IAS) 19 basis is disclosed at Note 16 of these accounts.

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 Fund actuary in the payroll period to which they relate.

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

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

b. Transfer to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the Local Government Pension Scheme Regulations 2013.

Individual transfers in/out are accounted for when received/paid, which is normally when the member liability is accepted or discharged.

Transfers in from members wishing to use the proceeds of their additional voluntary contributions (see paragraph m) to purchase scheme benefits are accounted for on a receipts basis and are included in Transfers in.

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

c. Investment income

i) Interest income
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. Income includes the amortisation of any discount or premium, transactions costs (where material) or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

ii) Dividend income
Dividend income is recognised on the date the shares are quoted ex-dividend. Any amount not received by the end of the reporting period is disclosed in the net assets statement as investment income due.

iii) Distributions from pooled funds
Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the net assets statement as investment income due.

iv) Property-related income
The Fund does not invest directly in property. All property investments are on a 'fund of funds' basis.

v) Movement in the net market value of investments
Changes in the net market value of investments are recognised as income and comprise all realised and unrealised profits/losses during the year.

vi) Income from stock lending is recognised when the deal has been agreed to lend stock and any amount not received by the end of the reporting period is disclosed in the net assets statement as investment income due.

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. Any amounts due but unpaid are disclosed in the net assets statement as current liabilities (sundry creditors).

e. Taxation

The Fund is a registered public service scheme under section 1(1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. 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 at year end.

f. Management expenses

The Code does not require any breakdown of pension fund administrative expenses. However, in the interests of greater transparency, the Fund discloses its pension Fund management expenses in accordance with the CIPFA guidance 'Accounting for Local Government Pension Scheme Management Costs' (2016).

- Administrative expenses

All administrative expenses are accounted for on an accruals basis. All staff costs of the pension administration team are charged to the Fund. Associated management, accommodation and other overheads are apportioned to this activity and charged as expenses to the Fund.

- Oversight and governance costs

All oversight and governance expenses are accounted for on an accruals basis. All staff costs associated with governance and oversight are charged to the Fund. Associated management, accommodation and other overheads are apportioned to this activity and charged as expenses to the Fund.

- Investment management expenses

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

Fees of the external Investment Managers and Custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.

In advance of preparing the year end accounts a request was made to all Investment Managers and Advisors for their fee invoice to the end of March 2017 or an estimated fee for accrual purposes.

A proportion of the Council's costs representing management time spent by officers on investment management are also charged to the Fund.

For private equity fees and property debt fees, the relevant Fund Managers provided information on fees to the end of March 2017 or a basis for estimating these fees.

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. A financial asset is recognised in the net assets statement on the date the Fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in the fair value of the asset are recognised in the Fund account.

The values of investments as shown in the net assets statement have been determined at fair value in accordance with the requirements of the Code and IFRS13 (see Note 12.1). For the purposes of disclosing levels of fair value hierarchy, the Fund has adopted the classification guidelines recommended in Practical Guidance on Investment Disclosures (PRAG/Investment Association 2016).

h. Foreign currency transactions

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

i. Derivatives

The Fund uses derivative financial instruments to manage its exposure to specific risks arising from its investment activities. The Fund does not hold derivatives for speculative purposes (see Note 13.7).

j. Cash and cash equivalents

Cash comprises cash in hand and demand deposits and includes amounts held by the Fund's external managers. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal risk of changes in value.

k. Financial liabilities

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

l. Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits is assessed on a triennial basis by the scheme actuary in accordance with the requirements of IAS 19 and relevant actuarial standards.

As permitted under the Code, the Fund has opted to disclose the actuarial present value of the promised retirement benefits by way of a note to the Net Assets Statement (Note 17).

m. Additional voluntary contributions

The Highland Council Pension Fund provides an additional voluntary contributions (AVC) scheme for its members, the assets of which are invested separately from those of the Fund. The Fund has appointed Prudential as its AVC provider. AVCs are paid to the AVC provider by employers and are specifically for providing additional benefits for individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and the movements in the year.

AVCs are not included in the accounts in accordance with Regulation 4(1)(b) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 but are disclosed as a note only (Note 18).

n. Contingent assets and contingent liabilities

A contingent liability arises when an event has taken place prior to the year-end giving rise to a possible financial obligation whose existence will only be confirmed or otherwise by the occurrence of future events. Contingent liabilities can also arise in circumstances where a provision would be made, except that it is not possible at the balance sheet date to measure the value of the financial obligation reliably.

A contingent asset arises where an event has taken place giving rise to a possible asset whose existence will only be confirmed or otherwise by the occurrence of future events.

Contingent assets and liabilities are not recognised in the net assets statement but are disclosed by way of narrative in the notes.

o. Prior year adjustments

Changes in accounting policies are only made when required by proper accounting practices or the change provides more reliable or relevant information about the effect of transactions, other events and conditions on the Fund's financial position or financial performance. Where a change is made, it is applied retrospectively by adjusting opening balances and comparative amounts for the prior period as if the new policy had always been applied.

Changes in accounting estimates are accounted for prospectively, i.e. in the current and future years affected by the change and do not give rise to a prior period adjustment.

Material errors discovered in prior period figures are corrected retrospectively by amending opening balances and comparative amounts for the prior period.

4. Accounting Standards Issued but Not Yet Adopted

Amendments to the following accounting standards will be adopted within the 2017/18 Code of Practice on Local Authority Accounting effective from 1 April 2017. There is therefore no impact on the 2016/17 financial statements.

- Amendment to the reporting of pension fund scheme transaction costs
- Amendment to the reporting of investment concentration

Changes arising from the adoption of these standards are not expected to have any impact on the General Fund balance.

5. Critical Judgements in Applying Accounting Policies

Unquoted private equity investments

It is important to recognise the highly subjective nature of determining the fair value of private equity investments. They are inherently based on forward-looking estimates and judgements involving many factors. Unquoted private equities are valued by the investment managers using guidelines set out by the British Venture Capital Association. The value of unquoted private equities at 31 March 2017 was £83.8m (£63.7m as at 31 March 2016).

Unquoted property debt investment

The unquoted holdings in property debt (commercial real estate loans) have been included at fair value. The value of unquoted property debt is £35.6m.

Pension fund liability

The net pension fund liability is recalculated every three years by the appointed actuary, with annual updates in the intervening year. The methodology used is in line with accepted guidelines.

The estimate is subject to significant variances based on changes to the underlying assumptions which are agreed with the actuary and have been summarised in Note 17.

These actuarial revaluations are used to set future contribution rates and underpin the Fund's most significant investment management policies, for example in terms of the balance struck between longer term investment growth and short term yield/return.

6. Assumptions Made About the Future and Other Major Sources of Estimation Uncertainty

The Statement of Accounts contains estimated figures that are based on assumptions made about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because outcomes cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

The items in the Financial Statements at 31 March 2017 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of promised retirement benefits	Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension Fund assets. A firm of consulting actuaries is engaged to provide the Fund with expert advice about the assumptions to be applied.	The effects on the net pension liability of changes in individual assumptions can be measured. • 0.5% p.a. increase in the pension increase rate would result in an increase of approximately 7% to liabilities (£172m). • 0.5% p.a. increase in salary increase rate would result in an increase of approximately 4% to liabilities (£87m). • 0.5% p.a. decrease in the discount rate assumption would result in an increase of approximately 11% to liabilities (£267m). • 1 year increase in member life expectancy would result in an increase in the liabilities of 3-5%.
Private equity	Private equity investments are valued at fair value in accordance with International Private Equity and Venture Capital Valuation guidelines (2012). These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total private equity investments in the financial statements are £83.7m. There is a risk that this investment may be under or overstated in the accounts. For example a potential market movement of 25.0% up or down could result in an increase of £104.7m or decrease of £62.8m.
Property Debt	Investment is valued by the Fund Manager using critical accounting estimates and judgements from the fund's financial statement. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total property debt investments in the financial statements are £35.6m. There is a risk that this investment may be under or overstated in the accounts. For example a potential market movement of 8.0% up or down could result in an increase of £38.5m or decrease of £32.8m.

7. Events after the Reporting Date

The unaudited statement of accounts was issued on 16 June 2017. Events taking place after this date are not reflected in the accounts or notes. There have been no events since 31 March 2017 and up to the date these accounts were authorised that require any adjustment to these accounts.

8. Contributions Receivable

By category	2015/16	**2016/17**
	£000	**£000**
Employees' pension contributions	12,608	12,508
Employers' pension contributions	42,624	44,788
Total contributions	**55,232**	**57,296**

As a result of the 2014 valuation, the future service contribution rate excluding deficit contributions has increased to 18.8% primarily due to the decrease in the real gilt yields which has increased both the employer future service rate and the past service adjustment. The outcome of the 2014 valuation meant revised contributions for 2015/16, 2016/17 and 2017/18.

Analysis of Contributions by Authority

	2016/17			
	Highland Council	**Scheduled Bodies**	**Admitted Bodies**	**Totals**
	£000	£000	£000	£000
Normal contribution	21,437	9,166	8,506	39,109
Deficit funding	113	218	487	818
	21,550	9,384	8,993	39,927
Strain on Fund	3,558	668	635	4,861
Employer's contributions	25,108	10,052	9,628	44,788
Members' pension contributions	6,794	3,000	2,714	12,508
Total contributions	**31,902**	**13,052**	**12,342**	**57,296**

	2015/16			
	Highland Council	Scheduled Bodies	Admitted Bodies	Totals
	£000	£000	£000	£000
Normal contribution	21,280	8,846	8,029	38,155
Deficit funding	0	93	637	730
	21,280	8,939	8,666	38,885
Strain on Fund	3,454	211	74	3,739
Employer's contributions	24,734	9,150	8,740	42,624
Members' pension contributions	6,888	2,932	2,788	12,608
Total contributions	**31,622**	**12,082**	**11,528**	**55,232**

Number of Contributors and Pensioners

2016/17	**Contributors**	**Pensioners**	**Deferred Pensioners**
Highland Council	7,080	6,599	5,956
Scheduled Bodies	2,886	1,900	2,089
Admitted Bodies	2,402	687	944
Total	**12,368**	**9,186**	**8,989**
2015/16			
Highland Council	7,011	6,105	5,677
Scheduled Bodies	2,931	1,775	1,901
Admitted Bodies	2,376	582	796
Total	**12,318**	**8,462**	**8,374**

9. Benefits Payable

By category	2015/16	**2016/17**
	£000	**£000**
Pensions	(37,358)	(40,840)
Lump sum retirement benefits	(12,146)	(14,036)
Lump sum death benefits	(2,090)	(2,046)
	(51,594)	**(56,922)**

By authority	2015/16	**2016/17**
	£000	**£000**
Highland Council	(36,404)	(39,286)
Scheduled Bodies	(10,244)	(11,572)
Admitted Bodies	(4,946)	(6,064)
	(51,594)	**(56,922)**

10. Payments to and on Account of Leavers

	2015/16	**2016/17**
	£000	**£000**
Refunds to members leaving service	(137)	(126)
Payments for members joining state scheme	(108)	(52)
Individual transfers	(2,850)	(822)
	(3,095)	**(1,000)**

At the year-end there are no potential liabilities (no potential liabilities 2015/16) in respect of individuals transferring out of the Fund upon whom the Fund is awaiting final decisions.

11. Management Expenses

	restated 2015/16 £000	**2016/17 £000**
Administrative costs	(932)	(1,054)
Investment Management expenses	(5,781)	(6,402)
Oversight and Governance costs	(311)	(261)
	(7,024)	**(7,717)**

Administrative Costs

Administrative costs	(168)	(250)
Employee costs	(756)	(795)
Other administration	(8)	(9)
	(932)	**(1,054)**

Investment Management Expenses	2015/16 £000	**2016/17** **£000**
External management fees invoiced	(2,975)	(3,330)
External management fees deducted from capital*	(1,025)	(1,274)
Performance fees	(355)	(1,003)
Custodian fees	(68)	(85)
Investment expenses**	(996)	(314)
Transaction costs	(362)	(396)
	(5,781)	**(6,402)**
Oversight and Governance costs		
Actuarial fees	(25)	(30)
External Audit fees (external audit only)	(49)	(29)
Internal Audit fees	(20)	(1)
Investment advisor fees	(53)	(37)
Tax advisor fees	-	-
Legal fees	(21)	(1)
Performance management	(21)	(22)
Employee costs	(103)	(106)
Sundry costs	(19)	(35)
	(311)	**(261)**
Total Management Expenses	**(7,024)**	**(7,717)**

* Adjustment made to external management fees deducted from capital (2015/16) in order to be consistent with approach in 2016/17 (see Note 25 for details).

** Fee rebates have been included in investment income rather than investment expenses in 2016/17 and adjustment has been made to 2015/16 accounts to follow a consistent approach (Note 12).

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions or in the proceeds of investment sales.

12. Analysis of Investment Income

	restated 2015/16 £000	**2016/17 £000**
Income from equities	18,037	20,108
Income from pooled investments (unit trusts and other managed funds)	3,490	3,550
Pooled property investments*	5,340	5,519
Interest on cash deposits	725	174
Private equity income	318	1,091
Stock lending and other income**	465	702
	28,375	**31,144**

* Pooled property investments are shown separately in the accounts for 2016/17 to follow best practice.

** Fee rebates have been included in investment income rather than investment expenses in 2016/17 and adjustment has been made to 2015/16 accounts to follow a consistent approach (see Note 25).

13. Investment Assets

13.1. Reconciliation of Movements in Investments and Derivatives

2016/17 **Classifications**	**Market value 1 Apr 16**	**Purchases at cost derivative payments**	**Sales proceeds derivative receipts**	**Change in market value**	**Market value 31 Mar 17**
	£000	**£000**	**£000**	**£000**	**£000**
Investment assets					
Equities	652,195	93,671	(97,284)	167,548	816,130
Pooled investments					
Unitised ins policies (equities)	249,726	487,121	(496,494)	61,692	302,045
Unitised ins policies (bonds)	68,771	88,481	(84,109)	9,384	82,527
Unit trusts (equities)	10,943	180	-	1,924	13,047
Unit trusts (bonds)	190,404	7,565	(3,462)	16,099	210,606
Unit trusts (property)	159,545	17,888	(17,410)	(695)	159,328
Venture capital and partnerships					
Private equity	63,685	16,303	(10,694)	14,466	83,760
Property debt	34,950	(124)	(929)	1,752	35,649
Currency forwards	(126)	2,271	(332)	(1,098)	715
Investment liabilities					
Currency forwards	-	-	-	-	-
	1,430,093	713,356	(710,714)	271,072	1,703,807
Other investment balances					
Cash deposits	21,227	-	-	(29)	37,479
Investment income due	4,080	-	-	-	3,764
Amounts receivable for sales	927	-	-	-	10,612
Amounts payable for purchases	(1,282)	-	-	-	(135)
Total net investment assets	1,455,045			271,043	1,755,527

2015/16 (restated)* **Classifications**	**Market value 1 Apr 15**	**Purchases at cost derivative payments**	**Sales proceeds derivative receipts**	**Change in market value**	**Market value 31 Mar 16**
	£000	**£000**	**£000**	**£000**	**£000**
Investment assets					
Equities	656,160	85,495	(70,146)	(19,314)	652,195
Pooled investments					
Unitised ins policies (equities)	279,095	3,448	(24,781)	(8,036)	249,726
Unitised ins policies (bonds)	94,139	-	(27,167)	1,799	68,771
Unit trusts (equities)	11,071	204	-	(332)*	10,943
Unit trusts (bonds)	189,337	71,184**	(67,475)	(2,642)*	190,404
Unit trusts (property)	140,550	9,572**	(1,456)	10,879**	159,545
Venture capital and partnerships					
Private equity	37,219	18,148	(7,001)	15,319	63,685
Property debt	-	35,503	(381)	(172)	34,950
Currency forwards	-	-	-	-	-
Investment liabilities					
Currency Forwards	(792)	1,307	(75)	(566)	(126)
	1,406,779	224,861	(198,482)	(3,065)	1,430,093
Other investment balances					
Cash deposits	26,004	-	-	151	21,227
Investment income due	3,192	-	-	-	4,080
Amounts receivable for sales	171	-	-	-	927
Amounts payable for purchases	(3,045)	-	-	-	(1,282)
Total net investment assets	1,433,101			(2,914)**	1,455,045

* The 2015/16 figures were updated using separate categories for unit trust equities and unit trust (bonds/fixed income).

** See Note 25 for details of prior year adjustment to profits and losses on disposal of investment and changes in values of investments.

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

13.2. Analysis of Investments

2015/16 (restated)		Portfolio Distribution UK & overseas	2016/17	
UK	Overseas		**UK**	**Overseas**
£000	£000	**Investment assets**	**£000**	**£000**
276,572	375,623	Equities	327,403	488,727
		Pooled investments		
198,267	51,459	Unitised insurance policies (equities)*	90,722	211,323
68,771	-	Unitised insurance policies (bonds)	82,527	-
10,943	-	Unit trust (equities)	13,047	-
123,741	66,663	Unit trust (bonds)	137,334	73,272
154,509	5,036	Unit trust (property)	155,715	3,613
		Venture capital and partnerships		
-	63,685	Private equity	-	83,760
34,950	-	Property debt	35,649	-
19,096	2,131	Cash deposits	37,326	153
1,924	2,156	Investment income due	1,974	1,790
84	843	Amounts receivable for sales	856	9,756
-	-	Currency forwards	-	715
		Investment liabilities		
-	(126)	Currency forwards	-	-
-	(1,282)	Amounts payable for purchases	-	(135)
888,857	**566,188**	**Net total**	**882,553**	**872,974**
	1,455,045			**1,755,527**

* During June to September 2016, changes were made to the unitised insurance policy investments whereby the allocation to UK equities was reduced and the global equities allocation was increased.

2015/16 (restated)		Portfolio Distribution (Quoted / Unquoted)	**2016/17**	
Quoted	Unquoted		**Quoted**	**Unquoted**
£000	£000	**Investment assets**	**£000**	**£000**
652,195	-	Equities	816,130	-
		Pooled investments		
249,726	-	Unitised insurance policies (equities)	302,045	-
68,771	-	Unitised insurance policies (bonds)	82,527	-
10,943	-	Unit trust (equities)	13,047	-
190,404	-	Unit trust (bonds)	210,606	-
	159,545	Unit trust (property)	-	159,328
		Venture capital and partnerships		
-	63,685	Private equity	-	83,760
-	34,950	Property debt	-	35,649
-	21,227	Cash deposits	-	37,479
4,080	-	Investment income due	3,764	-
-	927	Amounts receivable for sales	-	10,612
-	-	Currency forwards	-	715
		Investment liabilities		
-	(126)	Currency forwards	-	-
-	(1,282)	Amounts payable for purchases	-	(135)
1,176,119	**278,926**	**Net total**	**1,428,119**	**327,408**
	1,455,045			**1,755,527**

13.3. Investments Analysed by Fund Manager

The Market Value of the assets which were under the management of fund managers and the proportion managed by each manager are below.

2015/16			**2016/17**	
Market Value £000	% of Fund	**Manager Analysis**	**Market Value £000**	**% of Fund**
497,610	34.2	Baillie Gifford (UK and global equity)	636,553	36.3
186,128	12.8	Pyrford (global equity)	235,470	13.4
190,891	13.1	Fidelity (bonds and gilts)	210,606	12.0
318,500	21.9	Legal and General (unitised insurance - equity and bonds)	384,572	21.9
163,004	11.2	Schroders (property fund)	167,620	9.5
63,728	4.4	Partners Group (private equity)	83,839	4.8
35,184	2.4	Standard Life Investments	36,867	2.1
1,455,045	**100.0**	**Combined Fund**	**1,755,527**	**100.0**

13.4. Top 10 Equity Holdings by Market Value

Holding at 31 March 2017	**Market Value £000**	**% of Total Equity Investments**	**Classification**
Prudential	23,106	2.04	Insurance
British American Tobacco	19,641	1.74	Tobacco
Royal Dutch Shell 'B'	15,443	1.36	Oil and gas
Ashtead	13,361	1.18	Industrial goods and services
Amazon	13,133	1.16	Consumer discretionary
St James's Place	11,965	1.06	Insurance
Legal & General	11,375	1.01	Insurance
Bunzl	11,008	0.97	Support Services
SAP SE	10,219	0.90	Software
Royal Caribbean Cruises	10,136	0.90	Travel and leisure
Total	**139,387**	**12.32**	

13.5. Holdings Exceeding 5% by Total Net Assets

The Fund holds the following investments that exceed 5% of the net assets available for benefits.

Fund Manager & Category	Market Value at 31 March 2016	% of total net assets	Market Value at 31 March 2017	% of total net assets
	£000	%	£000	%
Fidelity (Institutional UK Aggregated Bond)	95,190	6.5	105,477	6.0
Legal & General (UK Equity Index)	198,544	13.5	90,722	5.1
Total net assets available for benefits	1,469,269		1,764,903	

13.6. Stock Lending

The fund's investment strategy sets parameters for the Fund's stock- lending programme.

At the year-end, the value of quoted equities on loan was £92.613m (31 March 2016 £0m). These equities continue to be recognised in the fund's financial statements.

Counterparty risk is managed through holding collateral at the Fund's custodian bank. At the year end, the Fund held collateral (via the custodian) at fair value of £100.612m (31 March 2016 £0m) representing 108.6% of stock lent. Collateral consists of acceptable securities and government debt.

Stock Lending commissions are remitted to the Fund via the custodian. During the period the stock is on loan, the voting rights of the loaned stock pass to the borrower.

The income from stock lending in 2016/17 was £0.153m which is included in investment income in the Pension Fund account and is part of the "Stock lending and other income" in Note 12 Analysis of Investment Income (£0.702m).

There are no liabilities associated with the loaned assets.

13.7. Analysis of Derivatives

Objectives and policies for holding derivatives

Most of the holding in derivatives is to hedge liabilities or hedge exposures to reduce risk in the Fund. Derivatives maybe used to gain exposure to an asset more efficiently than holding the underlying asset.

The use of derivatives is managed in line with the investment management agreements in place between the Fund and the various investment managers. The only derivatives that the Fund uses are forward foreign currency.

Forward foreign currency

To maintain appropriate diversification and to take advantage of overseas investment returns, a significant proportion of the Fund's quoted equity portfolio is in overseas stock. The Investment Managers Pyrford International and Baillie Gifford hold short term currency forwards for the Fund. The use of these forward foreign currency contracts is in line with the investment management agreement between the Fund and these Fund Managers.

This currency hedging is in place to reduce the extent to which the Fund is exposed to certain currency movements. These investments are used to ensure that cash can remain invested short term in equities. The sale of currency forwards, traded over the counter (OTC), is undertaken in order to hedge foreign currency exposure risk back to the portfolio's base currency of GBP.

Settlement	Currency bought	Local value	Currency sold	Local value	Asset value	Liability value
		000		000	£000	£000
Up to six months	GBP	8,642	CAD	(14,244)	116	0
Up to six months	GBP	18,439	AUD	(30,099)	202	0
Up to six months	GBP	25,254	CHF	(30,957)	372	0
Up to one month	CHF	356	GBP	(286)	2	0
Up to one month	EUR	1,008	GBP	(864)	3	0
Up to one month	JPY	131,121	GBP	(942)	1	0
Up to one month	SEK	2,079	GBP	(187)	1	0
Up to one month	USD	8,168	GBP	(6,549)	17	0
Up to one month	ZAR	5,652	GBP	(338)	1	0
Net forward currency contracts at 31 March 2017					**715**	0
Prior year comparative						
Net forward currency contracts at 31 March 2016					**0**	**(126)**

14.1. Fair Value – Basis of Valuation

The basis of the valuation of each class of investment asset is set out below. There has been no change in the valuation techniques used during the year. All assets have been valued using fair value techniques which represent the highest and best price available at the reporting date.

Description of Asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivities affecting the valuations provided
Market quoted investments	Level 1	Published bid market price ruling on the final day of the accounting period	Not required	Not required
Quoted bonds	Level 1	Fixed interest securities are valued at a market value based on current yields	Not required	Not required
Exchange traded pooled investments (includes unitised insurance policies (equities and bonds))	Level 1	Closing bid value on published exchanges	Not required	Not required
Pooled investments – overseas unit trusts and property funds	Level 2	Closing bid price where bid and offer prices are published. Closing single price where single price published.	Net Asset Value (NAV) based pricing set on a forward pricing basis	Not required
Pooled investments – property funds which are not listed	Level 3	Financial statements or other market indicators or information are used to calculate valuation.	The following is used: Estimated rental growth Covenant strength for existing tenancies Discount rate Estimated rental growth Land/building valuation survey	Significant changes in rental growth, vacancy levels or the discount rate could affect valuations as could more general changes to market prices.

Description of Asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivities affecting the valuations provided
Unquoted equity	Level 3	Comparable valuation of similar companies in accordance with International Private Equity and Venture Capital Valuation Guidelines (2012)	Earnings Before Interest, Taxes, Depreciation and Amortisation (EBITDA) multiple Revenue multiple Discount for lack of marketability Control premium	Valuations could be affected by material events occurring between the date of the financial statements and the Fund's own reporting date, by changes to expected cashflows, and any differences between audited and unaudited accounts.
Unquoted commercial real estate debt	Level 3	Valued by the Fund Manager using critical accounting estimates and judgements from the fund's financial statement.	Observable and unobservable input are critical accounting estimates and judgements from the fund's financial statement.	Valuations could be affected by material events occurring between the date of the financial statements provided and the pension fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts

14.2. Sensitivity of assets valued at level 3

Having consulted the Fund's independent investment advisors (Aon Hewitt), it was determined that the valuation methods described above for Level 3 investments are likely to be accurate to within the following ranges, and has set out below the consequent potential impact on the closing value of investments held at 31 March 2017.

Asset type	Value as at 31 Mar 2017	Assessed valuation range	Value on increase	Value on decrease
	£000	%	£000	£000
Pooled investment vehicles				
Units trust (property)	159,328	12.5%	179,244	139,412
Venture capital and partnerships				
Private equity	83,760	25%	104,700	62,820
Property debt	35,649	8%	38,501	32,797

14.3. Fair Value Hierarchy

Asset and liability valuations have been classified into three levels, according to the quality and reliability of information used to determine fair values. Transfers between levels are recognised in the year in which they occur.

Level 1
Assets and liabilities at Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level

1 comprise quoted equities, quoted fixed securities, quoted index linked securities and unit trusts.

Level 2
Assets and liabilities at Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active; or where valuation techniques are used to determine fair value.

Level 3
Assets and liabilities 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.

The following table provides an analysis of the financial assets and liabilities of the Fund grouped into Levels 1 to 3 based on the level at which the fair value is observable.

Values at 31 March 2017	**Quoted market price**	**Using observable input**	**With significant unobservable inputs**	
	Level 1	**Level 2**	**Level 3**	**Total**
Financial assets	**£000**	**£000**	**£000**	**£000**
Equities	816,130	-	-	816,130
Pooled investments				
Unitised insurance policies (equities)	302,045	-	-	302,045
Unitised insurance policies (bonds)	82,527	-	-	82,527
Unit trust (equities)	-	13,047	-	13,047
Unit trust (bonds)	210,606	-	-	210,606
Unit trust (property)		-	159,328	159,328
Venture capital and partnerships				
Private equity	-	-	83,760	83,760
Property debt	-	-	35,649	35,649
Cash deposits	37,479	-	-	37,479
Investment income due	3,764	-	-	3,764
Amounts receivable for sales	10,612	-	-	10,612
Currency forwards	715	-	-	715
Investment liabilities				
Currency forwards	-	-	-	-
Amounts payable for purchases	(135)	-	-	(135)
Net total	**1,463,743**	**13,047**	**278,737**	**1,755,527**

Values at 31 March 2016 (restated)	**Quoted market price**	**Using observable input**	**With significant unobservable inputs**	
	Level 1	**Level 2**	**Level 3**	**Total**
Financial assets	**£000**	**£000**	**£000**	**£000**
Equities	652,195	-	-	652,195
Pooled investments				
Unitised insurance policies (equities)	249,726	-	-	249,726
Unitised insurance policies (bonds)	68,771	-	-	68,771
Unit trust (equities)	-	10,943	-	10,943
Unit trust (bonds)	190,404	-	-	190,404
Unit trust (property)		-	159,545	159,545
Venture capital and partnerships				
Private equity	-	-	63,685	63,685
Property debt	-	-	34,950	34,950
Cash deposits	21,227	-	-	21,227
Investment income due	4,080	-	-	4,080
Amounts receivable for sales	927	-	-	927
Currency forwards		-	-	
Investment liabilities				
Currency forwards	(126)	-	-	(126)
Amounts payable for purchases	(1,282)	-	-	(1,282)
Net total	**1,185,922**	**10,943**	**258,180**	**1,455,045**

14.4. Reconciliation of Fair value Measurements within Level 3

Asset type	March value 1 Apr 2016	Transfers into Level 3	Transfer out of Level 3	Purchases during the year and derivative payments	Sales during the year and derivative receipts	Unrealised gains/ (losses)	Realised gain/(losses)	Market value 31 March 2017
	£000	£000	£000	£000	£000	£000	£000	£000
Pooled investment vehicles								
Units trust (property)	159,545	-	-	17,888	(17,410)	(4,644)	3,949	159,328
Venture capital and partnerships								
Private equity	63,685	-	-	16,303	(10,694)	6,632	7,834	83,760
Property debt	34,950	-	-	(124)	(929)	1,628	124	35,649

15. Financial Instruments

15.1. Classification of Financial Instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the carrying amount of financial assets and liabilities by category and net assets statement heading. No financial instruments were reclassified during the accounting period.

31 March 2017		**Loans & receivables**	**Financial liabilities at cost**	**Total**
		£000	**£000**	**£000**
Financial assets				
Equities	816,130	-	-	816,130
Pooled investments				
Unitised ins policies (equities)	302,045	-	-	302,045
Unitised ins policies (bonds)	82,527	-	-	82,527
Unit trust equity	13,047	-	-	13,047
Unit trusts (bonds)	210,606	-	-	210,606
Unit trusts (property)	159,328	-	-	159,328
Venture capital and partnerships				
Private equity	83,760	-	-	83,760
Property debt	35,649	-	-	35,649
Derivative contracts	715	-	-	715
Amounts receivable for sales	10,612	-	-	10,612
Cash deposits	-	37,479	-	37,479
Investment income due	-	3,764	-	3,764
Long term debtors		792		792
Short term debtors	-	8,753	-	8,753
Bank	-	3,045	-	3,045
	1,714,419	**53,833**	**-**	**1,768,252**
Financial liabilities				
Amounts payable for purchases	(135)	-	-	(135)
Creditors		-	(3,214)	(3,214)
Closing net assets	**1,714,284**	**53,833**	**(3,214)**	**1,764,903**

31 March 2016	**Fair value through profit & loss**	**Loans & receivables**	**Financial liabilities at cost**	**Total**
Financial assets	**£000**	**£000**	**£000**	**£000**
Equities	652,195	-	-	652,195
Pooled investments				
Unitised ins policies (equities)	249,726	-	-	249,726
Unitised ins policies (bonds)	68,771	-	-	68,771
Unit trust equity	10,943	-	-	10,943
Unit trusts (bonds)	190,404	-	-	190,404
Unit trusts (property)	159,545	-	-	159,545
Private equity	63,685	-	-	63,685
Property debt	34,950	-	-	34,950
Cash deposits	-	21,227	-	21,227
Investment income due	4,080	-	-	4,080
Amounts receivable for sales	927	-	-	927
Long term debtors		1,013		1,013
Short term debtors	-	6,815	-	6,815
Bank	-	10,200	-	10,200
	1,435,226	**39,255**	**-**	**1,474,481**
Financial liabilities				
Derivative contracts – currency forwards	(126)	-	-	(126)
Amounts payable for purchases	(1,282)	-	-	(1,282)
Creditors		-	(3,804)	(3,804)
Closing net assets	**1,433,818**	**39,255**	**(3,804)**	**1,469,269**

15.2. Net Gains and Losses on Financial Instruments

	2015/16	**2016/17**
	£000	**£000**
Financial assets		
Fair value through profit and loss	(1,544)	272,170
Loans and receivables	(3,133)	(29)
Financial liabilities	-	-
Financial liabilities	1,763	(1,098)
Total	**(2,914)**	**271,043**

16. The Nature and Extent of Risks 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 (i.e. promised benefit payable to members). Therefore 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. The Fund manages these investment risks as part of its overall Pension Fund risk management programme.

The Pensions Committee is responsible for the Fund's risk management strategy. There is a risk register in place which follows the CIPFA guidance on "Managing risk in the LGPS". This is regularly reviewed and significant risks are reported to the Pensions Committee.

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 Fund is exposed to market risk from its investment activities, particularly through its equity holdings. 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.

In general, excessive volatility in market risk is managed through the diversification of the portfolio in terms of geographical and industry sectors and individual securities. To mitigate market risk, the Fund and its investment advisors undertake appropriate monitoring of market conditions and benchmark analysis.

The Fund manages these risks by ensuring that specific risk exposure is limited by applying risk-weighted maximum exposures to individual investments.

Equity futures contracts and exchange traded option contracts on individual securities may also be used to manage market risk on equity investments. It is possible for over-the-counter equity derivative contracts to be used in exceptional circumstances to manage specific aspects of market risk.

Other price risk

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

The Fund is exposed to share and derivative price risk. This arises from investments held by the Fund for which the future price is uncertain. All securities investments present a risk of loss of capital. Except for shares sold short, the maximum risk resulting from financial instruments is determined by the fair value of the financial instruments. Possible losses from shares sold short are unlimited.

The Fund's investment managers mitigate this price risk through diversification and the selection of securities and other financial instruments.

Other price risk – sensitivity analysis

Following analysis of historical data and expected investment return movement during the financial year, in consultation with the Fund's investment advisors, the Fund has determined that the following movements in market price risk are reasonably possible for the 2016/17 reporting period.

Asset type	Potential market movement (+/)
UK equities	19.0%
Global equities (excluding UK)	20.0%
UK fixed income unit trusts	11.0%
Corporate bonds (medium term)	9.0%
Overseas corporate bonds	9.0%
UK fixed gilts (medium term)	11.0%
UK index linked gilts (medium term)	9.0%
Property	12.5%
Private Equity	25.0%
Property Debt	8.0%
Cash	0.0%

The potential price changes disclosed above are broadly consistent with a one-standard deviation movement in the value of the assets. The sensitivities are consistent with the assumptions contained in the investment advisors' most recent review. The Fund's investment advisors suggest that the approach to modelling market price risk should take account of the diversification of assets in the Fund. This approach is different to that outlined in the CIPFA recommended code of practice, where the sum of all potential changes in asset class values are taken to determine the impact on the total value of the Fund. Consequently the total Fund volatility takes into account the expected interactions between the different asset classes shown, based on the underlying volatilities and correlations of the assets, in line with mean variance portfolio theory.

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

Asset type	**Value as at 31 Mar 2017**	**Percentage change**	**Value on increase**	**Value on decrease**
	£000	**%**	**£000**	**£000**
Cash deposits	37,479	0.0	37,479	37,479
Investment portfolio assets:				
UK equities	431,172	19.0	513,095	349,249
Global equities (excluding UK)	700,050	20.0	840,060	560,040
UK fixed income unit trusts	31,857	11.0	35,362	28,353
UK Corporate bonds (medium term)	105,477	9.0	114,970	95,984
Overseas Corporate bonds (medium term)	73,272	9.0	79,866	66,677
UK fixed gilts (medium term)	49,567	11.0	55,020	44,115
UK index linked gilts (medium term)	32,960	9.0	35,926	29,994
Unit trusts property	159,328	12.5	179,244	139,412
Private equity	83,760	25.0	104,700	62,820
Property debt	35,649	8.0	38,501	32,797
Net currency forwards	715	0.0	715	715
Investment income due	3,764	0.0	3,764	3,764
Amounts receivable for sales	10,612	0.0	10,612	10,612
Amounts payable for purchases	(135)	0.0	(135)	(135)
Net investment assets	**1,755,527**		**2,049,179**	**1,461,876**

Asset type	Value as at 31 Mar 2016	Percentage change	Value on increase	Value on decrease
	£000	%	£000	£000
Cash deposits	21,227	0.0	21,227	21,227
Investment portfolio assets:				
UK equities	276,572	19.0	329,121	224,023
Global equities (excluding UK)	375,623	20.0	450,748	300,498
UK fixed income unit trusts	289,220	9.0	315,250	263,190
UK Corporate bonds (medium term)	95,190	9.0	103,757	86,623
Overseas Corporate bonds (medium term)	66,663	9.0	72,663	60,663
UK fixed gilts (medium term)	41,265	11.0	45,804	36,726
UK index linked gilts (medium term)	27,506	9.0	29,981	25,030
Unit trusts property	159,545	12.5	179,488	139,602
Private equity	63,685	25.0	79,606	47,764
Property debt	34,950	8.0	37,746	32,154
Net currency forwards	(126)	0.0	(126)	(126)
Investment income due	4,080	0.0	4,080	4,080
Amounts receivable for sales	927	0.0	927	927
Amounts payable for purchases	(1,282)	0.0	(1,282)	(1,282)
Net investment assets	**1,455,045**		**1,668,990**	**1,241,099**

Interest rate risk
The Fund invests in financial assets for the primary purpose of obtaining a return on investments. These investments 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 Fund's interest rate risk is routinely monitored by the Fund and its investment advisors in accordance with the Fund's risk management strategy, including monitoring the exposure to interest rates and assessment of actual interest rates against the relevant benchmarks.

The Fund's direct exposure to interest rate movements as at 31 March 2017 and 31 March 2016 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value.

Asset type	31 March 2016	31 March 2017
	£000	£000
Cash and cash equivalents	21,227	37,479
Bank accounts	10,200	3,045
Legal & General fixed interest gilts	41,265	49,567
Legal & General index linked gilts	27,506	32,960
Fidelity unit trust bonds	190,404	210,606
Total	**290,602**	**333,657**

Interest rate risk sensitivity analysis

The Fund 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.

The Fund's investment advisors suggest that a 100 basis point (BPS) movement in interest rates is appropriate for carrying out the interest rate sensitivity analysis.

The analysis that follows assumes that all other variables, in particular exchange rates, remain constant, and shows the effect in the year on the net assets available to pay benefits of a +/- 100 BPS (1%) change in interest rates:

Asset type	Carrying amount as at 31 March 2017	Change in year in the net assets available to pay benefits	
		+1%	-1%
	£000	£000	£000
Cash and cash equivalents	37,479	375	(375)
Bank accounts	3,045	30	(30)
Legal & General fixed interest gilts	49,567	496	(496)
Legal & General index linked gilts	32,960	330	(330)
Fidelity unit trust bonds	210,606	2,106	(2,106)
Total	**333,657**	**3,337**	**(3,337)**

Asset type	Carrying amount as at 31 March 2016	Change in year in the net assets available to pay benefits	
		+1%	-1%
	£000	£000	£000
Cash deposits	21,227	212	(212)
Bank accounts	10,200	102	(102)
Legal & General fixed interest gilts	41,265	413	(413)
Legal & General index linked gilts	27,506	275	(275)
Fidelity unit trust bonds	190,404	1,904	(1,904)
Total	**290,602**	**2,906**	**(2,906)**

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 the base currency of the Fund (£ Sterling).

The Fund's currency rate is routinely monitored by the Council and its investment advisors in accordance with the Fund's risk management strategy, including monitoring the range of exposure to currency fluctuations.

The following table summarises the Fund's currency exposure as at 31 March 2017 and as at the previous period end.

Currency exposure – asset type	Asset value as at 31 March 2016	Asset value as at 31 March 2017
	£000	£000
Overseas quoted securities	375,623	488,727
Overseas unitised insurance policies	51,459	211,323
Overseas property fund	5,036	3,613
Overseas unquoted private equity	63,685	83,685
Total overseas assets	**495,803**	**787,348**

Currency risk - sensitivity analysis

A 13% fluctuation in the currency is considered reasonable based on the Fund advisor's analysis of long-term historical movements in the month-end exchange rates over a rolling 36-month period. This analysis assumes that all other variables, in particular interest rates, remain constant. A 13% strengthening/weakening of the pound against the various currencies in which the Fund holds investments would increase/decrease the net assets available to pay benefits as follows:

Currency exposure - asset type	Asset value 31 March 2017	Change to net assets available to pay benefits	
		+13%	-13%
	£000	£000	£000
Overseas quoted securities			
Australian dollar (AUD)	20,581	23,256	17,905
Brazilian real (BRL)	1,953	2,207	1,699
Irish investments in British pound sterling (GBP)	5,971	6,747	5,195
Canadian dollar (CAD)	10,922	12,342	9,502
Danish krone (DKK)	4,770	5,390	4,150
Euro (EUR)	43,802	49,496	38,108
Hong Kong dollar (HKD)	23,000	25,990	20,010
Japanese yen (JPY)	26,645	30,109	23,181
Malaysian ringgit (MYR)	9,156	10,346	7,966
New Israeli shekel (ILS)	2,033	2,298	1,769
New Taiwan dollar (TWD)	11,120	12,565	9,674
Norwegian krone (NOK)	5,008	5,659	4,357
Singapore dollar (SGD)	11,772	13,302	10,242
South African rand (ZAR)	9,771	11,041	8,500
Swedish krona (SEK)	13,565	15,328	11,801
Swiss franc (CHF)	33,001	37,292	28,711
United States dollar (USD)	255,657	288,892	222,422
Total	488,727	552,260	425,192
Overseas unitised insurance policies (quoted in GBP no other values available)	211,323	238,795	183,851
Overseas property fund (EUR)	3,613	4,083	3,143
Overseas unquoted private equity (EUR)	83,685	94,564	72,806
Total change in assets available	**787,348**	**889,702**	**684,992**

Currency exposure - asset type	**Asset value 31 March 2016**	**Change to net assets available to pay benefits**	
		+13%	**-13%**
	£000	**£000**	**£000**
Overseas quoted securities			
Australian dollar (AUD)	17,644	19,938	15,350
Brazilian real (BRL)	1,343	1,518	1,168
Irish investments in British pound sterling (GBP)	4,151	4,691	3,611
Canadian dollar (CAD)	9,891	11,177	8,605
Danish krone (DKK)	4,063	4,591	3,535
Euro (EUR)	31,364	35,441	27,287
Hong Kong dollar (HKD)	18,038	20,383	15,693
Japanese yen (JPY)	21,746	24,573	18,919
Malaysian ringgit (MYR)	9,646	10,900	8,392
New Israeli shekel (ILS)	1,860	2,102	1,618
New Taiwan dollar (TWD)	10,038	11,343	8,733
Norwegian krone (NOK)	4,113	4,648	3,578
Singapore dollar (SGD)	8,846	9,996	7,696
South African rand (ZAR)	7,257	8,200	6,314
South Korean won (KRW)	725	819	631
Swedish krona (SEK)	10,493	11,857	9,129
Swiss franc (CHF)	24,582	27,777	21,386
United States dollar (USD)	189,823	214,500	165,147
Total	375,623	424,454	326,792
Overseas unitised insurance policies (quoted in GBP no other values available)	51,459	58,149	44,769
Overseas property fund (EUR)	5,036	5,690	4,381
Overseas unquoted private equity (EUR)	63,685	71,964	55,406
Total change in assets available	**495,803**	**560,257**	**431,348**

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 value of investments generally reflects an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the Fund's financial assets and liabilities.

In essence the Fund's entire investment portfolio is exposed to some form of credit risk, with the exception of the derivatives positions, where the risk equates to the net market value of a positive derivative position. However the selection of high quality counterparties, brokers and financial institutions minimises credit risk that may occur through the failure to settle a transaction in a timely manner.

Contractual credit risk is represented by the net payment or receipt that remains outstanding and the cost of replacing the derivative position in the event of a counterparty default. The residual risk is minimal due to the various insurance policies held by the exchanges to cover defaulting counterparties.

None of the investment managers of the Pension Fund have a mandate to specifically manage cash and so cash is generally held by the Custodian and invested in Money Market Funds (Sterling and Euro Funds). The Northern Trust Money Market Funds are triple A rated. In addition, the Fund's surplus cash from scheme members' contributions is managed as part of The Highland Council's treasury management function. Prior to transfer to the Fund's investment managers, cash surpluses, are deposited with the Pension Fund's bank (Clydesdale), Svenska Handelsbanken and the Royal Bank of Scotland thus minimising credit risk. The Fund had the following cash holdings at the year end.

	Moody's credit rating	**£000**
Northern Trust Global Investment – liquidity funds	AAA	37,412
Northern Trust Cash deposits	A1	67
		37,479

The following cash balances are held and managed in accordance with the Highland Council Treasury Strategy Statement.

	£000
Clydesdale accounts	2,045
Svenska Handelsbanken	1,000
	3,045

Liquidity Risk

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

Following the triennial valuation at 31 March 2014 the Fund's Actuary was asked to assess the projected cash flows of the Fund assuming a variety of possible maturity profiles. This study concluded that, provided the investment income yield remains at current levels, then the time when assets need to be sold to meet benefit payments still looks a long way off. The Actuary stated that there is no need to review investment strategy in the short term in any significant way although the cash flow position should continue to be monitored.

Refinancing Risk

The key risk is that the Fund will be bound to replenish a significant proportion of its Pension Fund financial instruments at a time of unfavourable interest rates. The Fund does not have any financial instruments that have a refinancing risk as part of its treasury management and investment strategies.

17. Actuarial Present Value of Promised Retirement Benefits

CIPFA's Code of Practice on Local Authority Accounting 2016/17 requires administering authorities of LGPS Funds that prepare Pension Fund accounts to disclose what IAS 26 refers to as the actuarial present value of promised retirement benefits.

The actuarial present value of promised retirement benefits is to be calculated similarly to the defined benefit obligation under IAS19. There are three options for its disclosure in Pension Fund accounts:

- showing the figure in the Net Assets Statement, in which case it requires the statement to disclose the resulting surplus or deficit;
- as a note to the accounts; or
- by reference to this information in an accompanying actuarial report.

If an actuarial valuation has not been prepared as at the date of the financial statements as is the case, IAS 26 requires the most recent valuation to be used as a base and the date of the valuation disclosed. The valuation should be carried out using assumptions in line with IAS 19 and not the Pension Fund's funding assumptions.

Assumptions underpinning the valuations are agreed with the actuary and are summarised in the Actuarial Position (page 82). This estimate is subject to significant variances based on changes to the underlying assumptions.

The actuarial present value of promised retirement benefits is as follows:

	31 March 2017 £m	31 March 2016 £m	31 March 2015 £m
Present Value of Promised Retirement Benefits*	2,471	1,883	1,988
Net Assets per Annual Accounts	1,764	1,469	1,448

* Liabilities have been projected using a roll forward approximation from the latest formal funding valuation as at 31 March 2014.

The Actuary estimates that the liability at 31 March 2017 comprises of £1,506m in respect of employee members, £345m in respect of deferred pensioners and £620m in respect of pensioners. The approximation involved in the roll forward model means that the split of scheme liabilities between the three classes of member may not be reliable. However, the Actuary is satisfied the aggregate liability is a reasonable estimate of the actuarial present value of benefit promises. The Actuary has not made any allowance for unfunded benefits.

Assumptions

The assumptions used are those adopted for the Administering Authority's IAS 19 report as required by the Code of Practice. These are given below. The Actuary estimates that the impact of the change of assumptions to 31 March 2017 is to increase the actuarial present value by £493m. There is no impact from any change in the demographic and longevity assumptions because they are identical to the previous period.

Financial Assumptions

The financial assumptions used for the purposes of the actuarial calculations are calculated on an IAS 19 basis and therefore differ from the results of the 2014 triennial funding valuation (see Actuarial Statement page 82) because IAS 19 stipulates a discount rate rather than a rate which reflects market values. The Financial Assumptions are as follows:

Assumptions as at	31 March 2017	31 March 2016	31 March 2015
	%p.a.	%p.a.	%p.a.
Inflation/Pensions Increase Rate	2.4%	2.2%	2.4%
Salary Increase Rate	4.4%	4.2%	4.3%
Discount Rate	2.6%	3.5%	3.2%

Discount rate

IAS 19 states that the discount rate used to place a value on the liabilities should be "determined by reference to market yields at the end of the reporting period on high quality corporate bonds". It further states that "the currency and term of the corporate bonds shall be consistent with the currency and estimated term of the post-employment benefit obligations". To that end the Actuary previously recommended a single discount rate for all LGPS employers broadly equivalent to the yield available on a basket of AA rated bonds with a duration similar to that of a "typical" LGPS employer.

The Actuary's approach to setting the discount rate as at 31 March 2017 follows the same principles to those adopted at 31 March 2016.

Separate discount rates are then set (and corresponding RPI/CPI inflation assumptions – see below) for individual employers, dependent on their own weighted average duration. Each employer is allocated to a duration category, as defined below:

Weighted average duration	Discount rate category
Less than 17 years	Short
Between 17 and 23 years	Medium
More than 23 years	Long

Retail price inflation assumption

This assumption is typically derived from yields available on fixed interest and index linked government bonds, and should be consistent with the derivation of the discount rate.

For consistency with the assessment described in paragraph above, the Actuary's recommended RPI inflation assumption for each discount rate category defined above has been identified at appropriate durations from the Bank of England implied inflation curve as at 31 March 2017.

Pension increase assumption

The pension increase assumption is set in line with the Actuary's default Consumer Prices Index (CPI) assumption. As a market in CPI linked bonds does not exist, the Actuary estimates the long term gap between RPI and CPI in order to derive a CPI assumption for accounting purposes. The default assumed RPI-CPI gap will be 1.0% p.a. (unchanged from the 2016 accounting exercise).

Salary increase assumption

The long term assumption for salary increases is RPI plus 1% p.a. This translates to CPI plus 1.8% p.a.

Longevity assumptions

The life expectancy assumptions are included in the Actuary's statement on page 82.

18. Additional Voluntary Contributions (AVCs)

The AVC facility is provided by the Prudential Assurance Company Limited and is a money purchase arrangement where members have the choice to invest in a range of low, medium and high risk investment funds. In accordance with regulation 5 (2) (c) of the Pension Scheme (Management and Investment of Funds) Regulations 1998 (S1 1998 No. 1831), these figures do not form part of the accounts of the Pension Fund and are stated for information only.

The value of Prudential AVCs at 31 March 2017 was £9.291m (£10.415 in 2015/16) and AVC contributions of £1.065m (£1.284m 2015/16) were paid directly to Prudential during the year.

19. Agency Services

Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998 (Section 31) allows employers to pay additional pensions on a voluntary basis.

As is typical within the Local Government Pension Schemes (LGPS), arrangements exist whereby additional teachers' pensions and employee pensions are paid with the payment of funded pensions. In order that such are not regarded as "unauthorised payments" by HMRC these pension payments are met by the administering authority and recharged to the body or service which granted the benefits.

As "unfunded payments" are discretionary benefits, they are not relevant to the sums disclosed in the Fund accounts. As such Highland Council Pension Fund provides payment and billing services to employers on a no charge agency agreement basis.

20. Related Parties

The Highland Council Pension Fund is administered by the Highland Council. As a result there is a strong relationship between the Council and the Fund. The Council is also the largest employer in the Fund.

The Pension Fund operates its own separate bank accounts. The Council's Treasury Management team manage surplus cash balances prior to transmission of funds to the Fund Managers for investment.

The Pension Fund does not directly employ any staff. Therefore no remuneration report is included within the Annual Report and Annual Accounts. All staff are employed by the Highland Council and their costs reimbursed by the Pension Fund. The Councillors, who are members of the Pension Fund Sub-Committee and Pension Board are also remunerated by the Highland Council. Details of Councillor and Senior Employee remuneration can be found in the accounts of the Highland Council on the Council's website.

http://www.highland.gov.uk/downloads/download/539/annual_accounts

At 31 March 2017, there is one member of the Pensions Committee (Cllr Norrie Donald) and one member of the Pensions Board (Mr Ewen Macniven (Trade Union representative) in receipt of a pension. Each member of the Fund is required to declare their interests at each meeting.

The following Senior Officer of the Highland Council held a key position in the financial management of the Pension Fund during the financial year to 31 March 2017.

Name	**Resp**	**Pension Contributions in year to**		**Accrued Pension Benefits as at 31/03/17**		**Difference in Accrued Pension benefits compared to March 2016**
		31/03/16	**31/03/17**			
Derek Yule	Director of Finance	£20,198	£20,951	Pension	£55,022	£2,794
				Lump Sum	£118,421	£1,170

Pension receipts and payments are transacted using the Highland Council financial systems and the Fund's banking arrangements. Throughout the year, the Fund maintains a cash balance for this purpose which is listed as Bank accounts in the net assets statement.

Contributions of £31.902m were paid by the Highland Council to the Fund during 2016/17 as set out in Note 8 (£31.622m - 2015/16) and central administration costs of £1.180m (£1.064m - 2015/16) were recharged to the Fund.

As at 31 March 2017, the Pension Fund had a net intercompany debtor of £4.151m representing sums due from the Highland Council. These balances in the main cover contributions payable by the Highland Council to the Pension Fund which were paid over in April 2017.

21. Contingent Assets, Liabilities and Contractual Commitments

Contingent assets

During 2006/07, the Highland Council Pension Fund joined a group litigation to recover tax credits on overseas dividends and foreign income dividends. The estimated claim, gross of fees is £1.7m. As at 31 March 2017, these claims are still active although many of the tax authorities are resisting claims thus delaying the recovery process.

During 2009/10, KPMG were contracted to submit "EU Fokus Bank" claims for recovery of withholding tax with an estimated value of £1.3m gross of fees. An additional revised contract was agreed in April 2012 with KPMG to continue with the claim. There have been no further repayments in 2016/17.

Contingent liabilities

As at 31 March 2017 there is a contingent liability of £0.554m (£0.522m - 2015/16) for frozen refunds representing 2,465 (2,377 - 2015/16) frozen refund records.

Contractual commitment

As at 31 March 2017 the Highland Council had contractual commitments in respect of private equity and commercial real estate debt portfolios.

	Commitment	**Undrawn commitments**
Partners Group 2011	£42.455m (€50.000m)	£9.544m (€11.240m)
Partners Group 2014	£67.928m (€80.000m)	£26.526m (€30.923m)
Standard Life Investments	£55.000m	£19.497m

22. Current Assets

2015/16 £000	**Debtors**	**2016/17 £000**
1,027	Contributions due - employees	1,019
3,588	Contributions due - employers	3,215
834	Strain on fund costs	1,207
191	Transfer values receivable	-
1,175	Short term debtors	3,297
-	Prepayments	15
10,200	Bank accounts	3,045
17,015	**Total current assets**	**11,798**

Analysis of Debtors

2015/16 £000	Debtors	2016/17 £000
182	Central government bodies	187
4,506	Local authorities	5,796
413	NHS bodies	378
1,714	Other entities and individuals	2,392
6,815		**8,753**

23. Long Term Debtors

2015/16 £000	Debtors	2016/17 £000
59	Central government bodies	21
931	Local authorities	764
4	NHS bodies	7
19	Other entities and individuals	-
1,013		**792**

24. Current Liabilities

2015/16 £000	Creditors	2016/17 £000
(2,493)	Sundry creditors	(1,927)
(76)	Transfer values payable (leavers)	(74)
(1,235)	Benefits payable	(1,213)
(3,804)		**(3,214)**

Analysis of creditors

2015/16 £000	Creditors	2016/17 £000
(533)	Central government bodies	(471)
(1,140)	Local authorities	(3)
-	NHS bodies	(41)
(2,131)	Other entities and individuals	(2,699)
(3,804)		**(3,214)**

25. Prior year adjustment

Investment income and expenses

Where fee rebates were received in 2016/17, these are included as income rather than a negative expense. Also, this is the third year that management fees have been reported and revised CIPFA guidance (Local Government Pension Scheme Management Expenses (2016) requires that only direct fees should be disclosed. In order to follow a consistent approach and provide a performance comparator for 2015/16, the results have been restated.

The fee rebate change has the effect of increasing investment income by £0.465m (Note 12) and increasing investment management expenses (Note 11) by £0.465m. The changes are reported in the Fund account but there is no change to the net increase in the Fund for the year ended 31 March 2016.

The change in reporting management fees has the effect of increasing the profits and losses on disposal of investments and changes in values of investments by £1.348m and decreasing the investment management expenses (Note 11) by £1.348m

In order to follow a consistent approach and provide a performance comparator for 2015/16, the results have been restated.

	£000	£000	£000
Fund account 2015/16	Per 2015/16 audited accounts	Changes made	Fund account as restated
Investment income	27,910	465	28,375
Profits and losses on disposal of investments and changes in values of investments	(1,566)	(1,348)	(2,914)

The inclusion of a comparator for 2015/16 performance fees also required changing the management expenses (oversight and governance costs).

	£000	£000	£000
Fund account 2015/16	Per 2015/16 audited accounts	Changes made	Fund account as restated
Administrative Costs	(932)	-	(932)
Oversight and Governance Costs	(311)	-	(311)
<u>Investment management expenses</u>			
Fee rebate adjustment	-	(465)	-
Management fee adjustment	-	1,348	-
Total investment management expenses	(6,664)		(5,781)
Management Expenses	**(7,907)**	**883**	**(7,024)**

Training, Knowledge and Skills - Policy Statement

The Highland Council Pension Committee approved a Training Policy for 2016/17 on 22 September 2016 which set out the following requirements:

- the CIPFA Code of Practice on Public Sector Pensions Finance Knowledge and Skills, and CIPFA's supporting Framework and guidance documentation (formally adopted by the Pensions Committee in November 2013).
- the Public Service Pensions Act 2013 the Pensions Regulator has outlined the legal requirements for individual Pension Board members to have the correct level of knowledge and understanding to undertake their role.

This Policy set out the planned training for 2016/17 and recorded training attended during 2015/16.

The Pensions Committee has delegated responsibility for implementation to the Director of Finance, and requires that there is annual reporting on the Pension Fund's training policy and its implementation. The table below summarises how training needs were fulfilled during the year 2016/17.

CIPFA framework core competency	Training specifics	Training event	Attendees
Pensions accounting & audit standards	CIPFA Pensions Network presentation by Audit Scotland; pensions accounting update CIPFA	14/09/16: CIPFA Pensions Network Workshops	Council officer
	Update on Pension Fund accounting requirements. Case study of Pension Fund accounts	14/02/17: CIPFA LGPS Accounting training	Council officer
Investment performance & risk management	Investment update from Baillie Gifford	14/09/16: CIPFA Pensions Network Workshops	Council officer
	Investing to meet long term liabilities presentation	05/10/16: Training seminar provided by Baillie Gifford	Council officer Members
Financial markets & products knowledge	Presentations on infrastructure investment by Lothian Pension Fund	29/09/16: CIPFA Investment Governance Group (IGG) training for Members	Council officer
	Session on volatility, investment diversification.	05/10/16: Training seminar provided by Baillie Gifford	Council officer Members
	Presentation on infrastructure by KPMG.	12/12/16:IGG training for Members and Officers	Members (2) Union rep (1) Council officers

CIPFA framework core competency	Training specifics	Training event	Attendees
Actuarial methods, standards and practices	CIPFA Pensions Network presentation by Hymans Robertson	14/09/16: CIPFA Pensions Network Workshops	Council officer
	Aon Hewitt training on Actuarial Valuation	22/09/16: Aon Hewitt session following Pensions Committee/Board meeting	Members Council officers
Pensions legislative & governance context	Pension Governance structures	14/09/16: CIPFA Pensions Network Workshops	Council officer
	Pensions Admin legislative context.	12/12/16: IGG training for Members and Officers	Members (2) Union rep (1) Council officers

The specific training events set out above are supplemented by additional knowledge and skills acquired through other ‘on the job’ activities including participation in working groups, attendance at meetings, general reading and research e.g. agenda reports and presentations, investment manager reports and briefings, magazines and other periodicals, online reading etc.

Actuary's Statement as at 31 March 2017

HYMANS ROBERTSON LLP

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The funding policy is set out in the Administering Authority's Funding Strategy Statement (FSS), dated March 2015. In summary, the key funding principles are as follows:

- to ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable where appropriate;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return;
- to reflect the different characteristics of different employers in determining contribution rates; and
- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

The FSS sets out how the Administering Authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable. For employers whose covenant was considered by the Administering Authority to be sufficiently strong, contributions have been stabilised below the theoretical rate required to return their portion of the Fund to full funding over 20 years if the valuation assumptions are borne out. Asset-liability modelling has been carried out which demonstrates that if these contribution rates are paid and future contribution changes are constrained as set out in the FSS, there is still around a 75% chance that the Fund will return to full funding over 20 years.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 32 of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008 was as at 31 March 2014. This valuation revealed that the Fund's assets, which at 31 March 2014 were valued at £1,279 million, were sufficient to meet 96% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2014 valuation was £52 million. Individual employers' contributions for the period 1 April 2015 to 31 March 2018 were set in accordance with the Fund's funding policy as set out in its FSS.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the valuation report dated 24 March 2015.

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth to retirement or expected earlier date of leaving pensionable membership.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market value. The key financial assumptions adopted for the 2014 valuation were as follows:

Financial assumptions	31 March 2014	
	% p.a. Nominal	% p.a. Real(CPI)
Discount rate	5.3%	2.6%
Pay increases	4.5%	1.8%
Price inflation/Pension increases	2.7%	-

The key demographic assumption was the allowance made for longevity. The life expectancy assumptions are based on the Fund's VitaCurves with improvements in line with the CMI 2012 model, assuming the current rate of improvements has reached a peak and will converge to a long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	22.5 years	24.1 years
Future Pensioners (currently aged 45)	24.7 years	26.8 years

Copies of the 2014 valuation report and Funding Strategy Statement are available on request from The Highland Council, the Administering Authority to the Fund.

Experience over the period since April 2014

The Fund's experience has been worse than expected since the last formal valuation (excluding the effect of any membership movements). Real bond yields have fallen sharply which places a significantly higher value on liabilities. The effect of this will have been partially offset by stronger than expected asset returns. The overall impact on the funding position at 31 March 2017 is that funding levels have likely worsened and deficits increased since the last formal valuation. This excludes the impact of possible changes to funding assumptions for the 2017 formal valuation, and membership experience which will be measured as part of that valuation: these items may improve or worsen the funding position.

The next actuarial valuation will be carried out as at 31 March 2017. The Funding Strategy Statement will also be reviewed at that time.

Robert Bilton FFA
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
20 Waterloo Street, Glasgow, G2 6DB
28 April 2017

Glossary

Actuarial assumptions/basis	The combined set of assumptions made by the actuary, regarding the future, to calculate the value of **liabilities**. The main assumptions will relate to the **discount rate**, salary growth, pension increases and longevity. More prudent assumptions will give a higher liability value, whereas more optimistic assumptions will give a lower value.
Administering Authority	The council with statutory responsibility for running the Fund, in effect the Fund's "trustees".
Admission Bodies	Employers which voluntarily participate in the Fund, so that their employees and ex-employees are **members**. There will be an Admission Agreement setting out the employer's obligations. For more details (see 2.5).
Common contribution rate	The Fund-wide **future service rate** plus **past service adjustment**. It should be noted that this will differ from the actual contributions payable by individual **employers**.
Covenant	The assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term.
Deficit	The shortfall between the assets value and the **liabilities** value. This relates to assets and liabilities built up to date, and ignores the future build-up of pension (which in effect is assumed to be met by future contributions).
Deficit repair/recovery period	The target length of time over which the current **deficit** is intended to be paid off. A shorter period will give rise to a higher annual **past service adjustment** (deficit repair contribution), and vice versa.
Discount rate	The annual rate at which future assumed cashflows (in and out of the Fund) are discounted to the present day. This is necessary to provide a **liabilities** value which is consistent with the present day value of the assets, to calculate the **deficit**. A lower discount rate gives a higher liabilities value, and vice versa. It is similarly used in the calculation of the **future service rate** and the **common contribution rate**.
Employer	An individual participating body in the Fund, which employs (or used to employ) **members** of the Fund. Normally the assets and **liabilities** values for each employer are individually tracked, together with its **future service rate** at each **valuation**.

Funding level	The ratio of assets value to **liabilities** value: for further details (see 2.2).
Future service rate	The actuarially calculated cost of each year's build-up of pension by the current active **members**, excluding members' contributions but including Fund administrative expenses. This is calculated using a chosen set of **actuarial assumptions**.
Gilt	A UK Government bond, ie a promise by the Government to pay interest and capital as per the terms of that particular gilt, in return for an initial payment of capital by the purchaser. Gilts can be "fixed interest", where the interest payments are level throughout the gilt's term, or "index-linked" where the interest payments vary each year in line with a specified index (usually RPI). Gilts can be bought as assets by the Fund, but their main use in funding is as an objective measure of solvency.
Guarantee / guarantor	A formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's **covenant** to be as strong as its guarantor's.
Letting employer	An employer which outsources or transfers a part of its services and workforce to another employer (usually a contractor). The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer. A letting employer will usually be a local authority.
Liabilities	The actuarially calculated present value of all pension entitlements of all **members** of the Fund, built up to date. This is compared with the present market value of Fund assets to derive the **deficit**. It is calculated on a chosen set of **actuarial assumptions**.
LGPS	The Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 101 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.
Maturity	A general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is

	shorter. This has implications for investment strategy and, consequently, funding strategy.
Members	The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).
Past service adjustment	The part of the employer's annual contribution which relates to past service **deficit** repair.
Pooling	Employers may be grouped together for the purpose of calculating contribution rates, so that their combined membership and asset shares are used to calculate a single contribution rate applicable to all employers in the pool. A pool may still require each individual employer to ultimately pay for its own share of **deficit**, or (if formally agreed) it may allow **deficits** to be passed from one employer to another. For further details of the Fund's current pooling policy (see 3.4).
Profile	The profile of an employer's membership or liability reflects various measurements of that employer's **members**, ie current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc. A membership (or liability) profile might be measured for its **maturity** also.
Rates and Adjustments Certificate	A formal document required by the LGPS Regulations, which must be updated at least every three years at the conclusion of the formal **valuation**. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three year period until the next valuation is completed.
Scheduled Bodies	Types of employer explicitly defined in the LGPS Regulations, whose employers must be offered membership of their local LGPS Fund. These include Councils, colleges, universities, academies, police and fire authorities etc, other than employees who have entitlement to a different public sector pension scheme (e.g. teachers, police and fire officers, university lecturers).
Solvency	In a funding context, this usually refers to a 100% **funding level**, ie where the assets value equals the **liabilities** value.
Stabilisation	Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly

required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund. Different methods may involve: probability-based modelling of future market movements; longer deficit recovery periods; higher discount rates; or some combination of these.

Theoretical contribution rate The employer's contribution rate, including both **future service rate** and **past service adjustment**, which would be calculated on the standard **actuarial basis**, before any allowance for **stabilisation** or other agreed adjustment.

Valuation An actuarial investigation to calculate the liabilities, future service contribution rate and common contribution rate for a Fund, and usually individual employers too. This is normally carried out in full every three years (last done as at 31 March 2014), but can be approximately updated at other times. The assets value is based on market values at the valuation date, and the liabilities value and contribution rates are based on long term bond market yields at that date also.