

**SOUTHWARK COUNCIL  
STATEMENT OF ACCOUNTS 2016/17**

**LONDON BOROUGH OF SOUTHWARK PENSION FUND  
STATEMENT OF ACCOUNTS**

**FUND ACCOUNT**

	Note	2016-17		2015-16	
		£000	£000	£000	£000
<b>Dealings with members, employers and others directly involved in the fund</b>					
Contributions	6	(52,212)		(55,479)	
Transfers in from other pension funds	7	(3,577)		(5,702)	
<b>Sub total</b>			<b>(55,789)</b>		<b>(61,181)</b>
Benefits	8	57,367		56,850	
Payments to and on account of leavers	9	2,902		4,905	
<b>Sub total</b>			<b>60,269</b>		<b>61,755</b>
<b>Net reduction/(addition) from dealing with members of the fund</b>			<b>4,480</b>		<b>574</b>
<b>Management expenses</b>	10		<b>5,096</b>		<b>4,549</b>
<b>Returns on investments</b>					
Investment income	11	(14,324)		(12,717)	
Taxes on income	11	175		155	
Profit and losses on disposal of investments and changes in market value of investments	12	(234,037)		(1,212)	
<b>Net return on investments</b>			<b>(248,186)</b>		<b>(13,774)</b>
<b>Net (increase)/decrease in the net assets available for benefits during the year</b>			<b>(238,610)</b>		<b>(8,651)</b>
Opening net assets of the scheme			(1,256,382)		(1,247,731)
<b>Net assets of the scheme available to fund benefits at 31 March</b>			<b>(1,494,992)</b>		<b>(1,256,382)</b>

**NET ASSETS STATEMENT**

	Note	31/03/2017 £000	31/03/2016* £000
Investment assets	12	1,487,842	1,246,582
Current assets	13	13,612	14,936
Current liabilities	13	(6,462)	(5,136)
<b>Net assets of the scheme available to fund benefits at 31 March</b>		<b>1,494,992</b>	<b>1,256,382</b>

*\*The fund's accounting policies for accrued dividend entitlements have been reviewed for the 2016-17 statement of accounts and have resulted in a change of classification from treatment as a current asset to an investment asset. To reflect this change the 2015-16 net asset statement has been restated. The value of accrued dividend entitlements as at the 31 March 2016 is £1,143k.*

The fund's financial statements do not take account of liabilities to pay pensions and other benefits after the period end. The estimated actuarial present value of promised retirement benefits is disclosed at Note 19.

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**NOTES TO THE PENSION FUND STATEMENTS**

**1. INTRODUCTION**

The Pension Fund is part of the Local Government Pension Scheme (LGPS) and is administered by Southwark Council (the council).

The following description of the fund is a summary only. For more detail, reference should be made to the Pension Fund Annual Report 2016-17 and the underlying statutory powers underpinning the scheme, namely the Public Service Pension Act 2013 and the LGPS Regulations.

a) General

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

- The Local Government Pension Scheme Regulations 2013 (as amended)
- The Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 (as amended)
- The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (as amended).

It is a contributory defined benefit scheme that provides pensions and other benefits for former employees of the council and other admitted organisations.

The overall investment strategy is the responsibility of the council. This responsibility is delegated to the strategic director of finance and governance, taking account of the advice of the Pensions Advisory Panel. In line with the provisions of the Public Services Pensions Act 2013, the council has set up a Local Pension Board to assist the council in its role as scheme manager of the Pension Fund. The Board meets on a quarterly basis and has its own terms of reference. Board members are independent of the Pensions Advisory Panel.

b) Membership

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

Organisations participating in the Fund include:

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

A list of participating organisations and their contributions for the financial year 2016-17 is included within the Pension Fund Annual Report 2016-17. This is available from the council website on the following link.  
[https://www.2.southwark.gov.uk/downloads/download/2717/pension\\_fund\\_annual\\_report](https://www.2.southwark.gov.uk/downloads/download/2717/pension_fund_annual_report)

	31/03/2017	31/03/2016
Number of contributors to the Fund	6,914	7,117
Number of contributors and dependants receiving allowances	7,483	7,212
Number of contributors who have deferred their pensions	7,895	7,858

c) Funding

Benefits are funded by contributions and investment earnings. Contributions are made by active members of the fund in accordance with the LGPS Regulations 2013 and range from 5.5% to 12.5% of pensionable pay for the financial year ending 31 March 2017. Employee contributions are matched by employers' contributions, which are set in accordance with the triennial actuarial funding valuations, the last being at 31 March 2016. Currently, employer rates range from 10.7% to 17.8% of pensionable pay, plus additional deficit payments where appropriate.

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d) Benefits

Prior to 1 April 2014, pension benefits under the LGPS were based on final pensionable pay and length of pensionable service, summarized in the following table:

	<b>Service Pre 1 April 2008</b>	<b>Service post 31 March 2008</b>
Pension	Each year worked is worth 1/80 x final pensionable salary	Each year worked is worth 1/60 x final pensionable salary
Lump sum	Automatic lump sum of 3 x pension. In addition, part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up.	No automatic lump sum. Part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up.

From 1 April 2014, the scheme became a career average scheme, whereby members accrue benefits based on their pensionable pay in that year at an accrual rate of 1/49<sup>th</sup>. Accrued pension is uprated annually in line with Consumer Prices Index.

**2. BASIS OF PREPARATION**

The Statement of Accounts summarises the fund's transactions for the 2016-17 financial year and its position at year-end as at 31 March 2017. The 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 Financial 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.

**3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Fund Account – Revenue Recognition

a) *Contributions 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.

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 financial asset.

b) *Transfers to and from other schemes*

Transfer values represent the amounts received and paid during the year for members who have either joined or left the fund during the financial year and are calculated in accordance with the Local Government Scheme Regulations. Individual transfers in or out are accounted for when received or 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 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*

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, transaction costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

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 a current investment asset.

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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 a current investment asset. Property related income consists primarily of rental income. Rental income from operating leases on properties owned by the fund is recognised on a straight-line basis over the term of the lease. Any lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease. Contingent rents based on the future amount of a factor that changes other than with the passage of time, such as turnover rents, are only recognised when contractually due.

Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits and or losses during the year.

d) *Fund account – 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

e) *Fund account – 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 as it arises.

f) *Management Expenses*

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

*Administrative expenses*

All administrative expenses are accounted for on an accruals basis. All staff costs of pensions administration are charged direct to the fund. Management, accommodation and other overheads are apportioned to the fund in accordance with council policy.

*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 direct to the fund. Management, accommodation and other overheads are apportioned to the fund in accordance with council policy.

*Investment management expenses*

All investment management expenses are accounted for on an accruals basis. Fees for the fund managers and custodian are agreed in the respective mandates governing their appointments and are based broadly on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.

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Net Asset 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 assets are recognised by the fund. The values of investments as shown in the net assets statement have been determined as follows:

- Equity investments, unit trusts and unitised insurance policies at their market bid price on 31 March each year.
- Foreign currency transactions have been brought into the accounts at the exchange rate that was in force when the transaction took place.
- End of year balances on foreign currency transactions have been translated at the exchange rate on 31 March each year.
- Investment assets have been valued and included in the accounts at bid price except for derivative contracts which are valued on the basis of unrealised gains and losses.
- Property unit trusts have been included at net asset price.

*h) Freehold and leasehold property*

Property assets have been included in the accounts at fair value as at 31 March each year. The valuation of direct property managed by TH Real Estate is carried out annually by an independent valuer.

*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. The future value of forward currency contracts is based on market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year-end with an equal and opposite contract.

*j) Cash and cash equivalents*

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

*k) Financial liabilities*

The fund recognises financial liabilities at fair value as at the reporting date. A financial liability is recognised in the net assets statement on the date the fund becomes party to the liability. From this date any gains or losses arising from changes in the fair value of the liability are recognised by the fund.

*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 IAS 26, the fund has opted to disclose the actuarial present value of promised retirement benefits by way of a note in the net assets statement.

*m) Additional voluntary contributions*

The fund provides an additional voluntary contributions (AVC) scheme for its members, the assets of which are invested separately from those of the pension fund. AVCs are not included in the accounts but are disclosed as a note (Note 6).

#### **4. CRITICAL JUDGEMENTS IN APPLYING ACCOUNTING POLICIES**

Pension Fund Liability

The pension fund liability is calculated every three years by the appointed actuary, with annual updates in the intervening years. The methodology used is in line with accepted guidelines and in accordance with IAS 19. Assumptions underpinning the valuations are agreed with the actuary and are summarised in Note 19. This estimate is subject to significant variances based on changes to underlying assumptions.

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Property Unit Trust Valuation

Fund investment assets in property funds were reclassified as level 3 from level 2 within the fair valuation hierarchy. This change was the result of additional information becoming available as to the nature of the funds and following consideration of recently published guidance on the classification of investment assets. The funds are valued infrequently on a monthly basis based upon an assessment of the net asset value. Furthermore the funds have, differing but significant, impediments to the redemption of assets, including significant time period delays to redemption, redemption only at manager discretion or only in certain circumstances. Key sensitivities and judgements therefore are present in the potential market movements between valuation and redemption dates.

**5. ASSUMPTIONS MADE ABOUT THE FUTURE AND OTHER MAJOR SOURCES OF ESTIMATION UNCERTAINTY**

The Statements contain estimated figures that are based on assumptions made by the council about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, as balances cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of retirement benefits (Note 19)	This applies to the estimation of the net liability to pay pensions, which depends upon 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.  The council's actuaries are engaged to provide the Fund with expert advice about the assumptions to be applied.	A 1.0% change in the discount rate is estimated to change the present value of pension liability by £215m
Freehold and leasehold property, pooled property funds (Note 12)	Valuation techniques are used to determine the carrying amount of pooled property funds and directly held freehold and leasehold property. Where possible these valuation techniques are based on observable data, but where this is not possible management uses the best available data. Changes in the valuation assumptions used, together with significant changes in rental growth, vacancy levels or the discount rate could affect the fair value of property.	The effect of variations in the factors supporting the valuation would be an increase or decrease in the value of directly held property of £10m, on a fair value of £240m.

**6. CONTRIBUTIONS RECEIVABLE**

Contributions represent the total amount receivable from employees and employers of the scheme.

	2016-17			2015-16		
	Employees £000	Employers £000	Total £000	Employees £000	Employers £000	Total £000
Southwark Council	(10,906)	(37,315)	(48,221)	(11,295)	(39,881)	(51,176)
Admitted bodies	(298)	(873)	(1,171)	(346)	(1,145)	(1,491)
Scheduled bodies	(905)	(1,915)	(2,820)	(900)	(1,912)	(2,812)
<b>Total Contributions</b>	<b>(12,109)</b>	<b>(40,103)</b>	<b>(52,212)</b>	<b>(12,541)</b>	<b>(42,938)</b>	<b>(55,479)</b>

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Contributions receivable from employers are shown below:

	<b>2016-17 £000</b>	<b>2015-16 £000</b>
Normal	(23,075)	(23,919)
Early retirement strain	(3,840)	(4,795)
Deficit funding	(13,188)	(14,224)
<b>Total contributions from employers</b>	<b>(40,103)</b>	<b>(42,938)</b>
Contributions from employees	(12,109)	(12,541)
<b>Total Contributions</b>	<b>(52,212)</b>	<b>(55,479)</b>

During 2016-17 employees made Additional Voluntary Contributions (AVCs) of £179k (£468k in 2015-16). The value of the AVCs at 31 March 2017 was £2.6 million (£2.7 million at 31 March 2016).

**7. TRANSFERS IN FROM OTHER PENSION FUNDS**

Transfers in from other pension funds were as follows:

	<b>2016-17 £000</b>	<b>2015-16 £000</b>
Individual transfers	(3,577)	(5,702)
<b>Total transfers in from other pension funds</b>	<b>(3,577)</b>	<b>(5,702)</b>

**8. BENEFITS PAYABLE**

The table below shows the types of benefit payable by category:

	<b>2016-17 £000</b>	<b>2015-16 £000</b>
Pensions	44,118	43,630
Commutation of pensions and lump sum retirement benefits	11,960	11,923
Lump sums – death benefits	1,289	1,297
<b>Total benefits payable</b>	<b>57,367</b>	<b>56,850</b>

The table below shows the total benefits payable grouped by entities:

	<b>2016-17 £000</b>	<b>2015-16 £000</b>
Southwark Council	55,182	54,929
Admitted bodies	1,431	1,582
Scheduled bodies	754	339
<b>Total benefits payable</b>	<b>57,367</b>	<b>56,850</b>

**9. PAYMENTS TO AND ON ACCOUNT OF LEAVERS**

	<b>2016-17 £000</b>	<b>2015-16 £000</b>
Refund of contributions	94	90
State Scheme Premiums	40	114
Individual transfers out to other schemes	2,768	4,701
<b>Total payments</b>	<b>2,902</b>	<b>4,905</b>

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**10. MANAGEMENT EXPENSES**

	<b>2016-17</b>	<b>2015-16*</b>
	<b>£000</b>	<b>£000</b>
Administrative costs	1,579	1,430
Investment and management expenses	3,103	2,742
Oversight and governance costs	414	377
<b>Total management expenses</b>	<b>5,096</b>	<b>4,549</b>

*\*Restated to account for recent changes to the Code of Practice regarding the classification of management expenses.*

During 2016-17, the fee for external audit services for the pension fund was £21k (£21k in 2015-16)

The table below shows the total investment and management expenses

	<b>2016-17</b>	<b>2015-16</b>
	<b>£000</b>	<b>£000</b>
Management Fees	2,342	2,308
Performance Fees	-	-
Property Management Expenses	694	355
Custody Fees	67	79
<b>Total Investment expenses</b>	<b>3,103</b>	<b>2,742</b>

The pension fund incurred expenses of £1.0m in relation to services provided by the council during 2016-17 (£0.8m during 2015-16).

**11. INVESTMENT INCOME**

	<b>2016-17</b>	<b>2015-16</b>
	<b>£000</b>	<b>£000</b>
Dividends from equities	(3,404)	(2,601)
Income from pooled investment vehicles	(2,034)	(1,813)
Net rent from properties	(8,819)	(8,207)
Interest on cash deposits	(10)	(75)
Other income	(57)	(21)
<b>Total investment income before taxes</b>	<b>(14,324)</b>	<b>(12,717)</b>
Taxes on income	175	155
<b>Total investment income after taxes</b>	<b>(14,149)</b>	<b>(12,562)</b>



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**12. INVESTMENT ASSETS**

	31/03/2017 £000	31/03/2016 £000
<b>Bonds</b>		
Quoted Overseas	11,702	5,793
<b>Equity</b>		
Quoted UK	11,353	12,651
Quoted Overseas	130,931	104,033
<b>Pooled Funds</b>		
Fixed Income Overseas	121,111	117,561
Index Linked Gilts	144,332	119,853
Multi Asset	122,264	118,474
<b>Unitised Insurance Policy</b>	696,217	555,780
<b>Property</b>		
Direct Property	160,200	167,000
Property Unit Trust	80,057	43,989
<b>Derivatives</b>		
Forward currency contracts	(19)	55
<b>Cash Deposits</b>	8,100	100
<b>London Collective Investment Vehicle (CIV)</b>	150	150
<b>Other Investment Balances</b>	1,445	1,143
<b>Investment Assets</b>	<b>1,487,842</b>	<b>1,246,582</b>

Note 12 is restated from 2015-16 to account for the change in accounting policy for accrued dividend entitlement to be reclassified as other investment balances as part of investment assets, rather than a current asset. The value of accrued dividend entitlements as at the 31 March 2016 is £1,143k.

The change in market value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on the sale of investments during the year. The table below shows the movement in investment assets and the change in market value for the year:

	Value at 31/03/2016 £000	Purchase £000	Sales £000	Change in market value £000	Cash movement £000	Value at 31/03/2017 £000
Bonds	5,793	40,221	(35,633)	1,321	-	11,702
Equity	116,684	48,550	(47,183)	24,233	-	142,284
Pooled Funds	355,888	76,074	(116,961)	72,705	-	387,706
Unitised Insurance Policy	555,780	288,120	(287,123)	139,440	-	696,217
Property	210,989	40,123	(6,913)	(3,942)	-	240,257
Derivatives	55	1,535	(1,889)	280	-	(19)
Cash Deposits	100	-	-	-	8,000	8,100
London Collective Investment Vehicle (CIV)	150	-	-	-	-	150
Other Investment balances	1,143	-	-	-	302	1,445
<b>Investment Assets</b>	<b>1,246,582</b>	<b>494,623</b>	<b>(495,702)</b>	<b>234,037</b>	<b>8,302</b>	<b>1,487,842</b>

	Value at 31/03/2015 £000	Purchase £000	Sales £000	Change in market value £000	Cash movement £000	Value at 31/03/2016 £000
Bonds	8,150	22,335	(24,855)	163	-	5,793
Equity	107,586	53,546	(52,158)	7,710	-	116,684
Pooled Funds	127,159	267,863	(36,164)	(2,970)	-	355,888
Unitised Insurance Policy	817,835	1,972	(249,970)	(14,057)	-	555,780
Property	174,117	34,023	(7,302)	10,151	-	210,989
Derivatives	0	521	(681)	215	-	55
Cash Deposits	4,428	-	-	-	(4,328)	100
London Collective Investment Vehicle (CIV)	0	-	-	-	150	150
Other Investment balances	314	-	-	-	829	1,143
<b>Investment Assets</b>	<b>1,239,589</b>	<b>380,260</b>	<b>(371,130)</b>	<b>1,212</b>	<b>(3,349)</b>	<b>1,246,582</b>

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The Pension Fund does not hold derivatives as a main asset class, but they are used by Newton Investment Management, our active equity fund manager, to hedge the currency risk of holding global equities. The currency forward contracts are traded over the counter.

The valuation of direct property managed by TH Real Estate is carried out by Knight Frank LLP. The valuer is RICS qualified and the valuation took place on 31 March 2017. All properties have been valued at market value.

The Investment Strategy Statement can be accessed on the council's website via the following link [http://www.2.southwark.gov.uk/downloads/download/4759/southwark\\_pension\\_fund\\_administration\\_strategy](http://www.2.southwark.gov.uk/downloads/download/4759/southwark_pension_fund_administration_strategy) Alternatively a copy can be obtained on request from the Strategic Director of Finance and Governance, Southwark Council, Finance and Governance, PO Box 64529, London SE1P 5LX.

The following investments represent more than 5% of investment assets.

Name of Investment	Fund Manager	31/03/2017	% of investment assets	31/03/2016	% of investment assets
		£000	%	£000	
North America Equity	Legal & General	206,559	14%	152,946	12%
US Equity Fund	Blackrock	134,526	9%	115,968	9%
Diversified Growth Fund	Blackrock	122,264	8%	118,475	10%
Absolute Return Bond Fund	Blackrock	121,111	8%	117,561	9%
+5 Year Index Linked Gilt Fund	Legal & General	77,043	5%	63,053	5%

The market value of assets (excluding cash and accruals) managed by the investment managers at the balance sheet date 31 March 2017 has been set out in the table below.

Investment Manager	31/03/2017		31/03/2016	
	£000	%	£000	%
BlackRock	670,335	45%	595,839	48%
Legal & General Investment Managers	413,588	28%	315,953	25%
TH Real Estate (formerly Henderson Global Investors)	200,608	13%	204,027	16%
Newton Investment Management	153,966	10%	129,463	11%
M&G Real Estate	20,006	1%	-	-
Invesco Real Estate	14,897	1%	-	-
Brockton Capital LLP	7,934	-	5,148	-
Frogmore Real Estate Partners	4,913	-	3,551	-
London CIV	150	-	150	-
<b>Total</b>	<b>1,486,397</b>		<b>1,254,131</b>	

### 13. CURRENT ASSETS AND LIABILITIES

The current assets of the fund are analysed as follows:

	2016-17	2015-16*
	£000	£000
Contribution due from employers	3,578	3,124
Other current assets	3,467	1,774
Cash at managers	5,835	8,210
Cash and bank	732	1,828
<b>Total</b>	<b>13,612</b>	<b>14,936</b>

*Restated to account for the change in accounting policy for accrued dividend entitlement to be reclassified as an investment asset, rather than other current assets. The value of accrued dividend entitlements as at the 31 March 2016 is £1,143k.*

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The current liabilities of the fund are analysed as follows:

	<b>2016-17 £000</b>	<b>2015-16 £000</b>
Support services	(1,759)	(33)
Benefits	(111)	(323)
Professional fees	(563)	(473)
Investment	(2,131)	(1,915)
Taxes	(1,361)	(1,131)
Other	(537)	(1,261)
<b>Total</b>	<b>(6,462)</b>	<b>(5,136)</b>

#### **14. RELATED PARTY TRANSACTIONS**

The Pension Fund is required to disclose details of its financial relationship with related third parties. This has been defined as where the related party has, or is perceived to have, real influence over any transaction between the parties.

Through its administration of the Fund, the council has a related party interest with the Pension Fund, and the costs charged by the council are disclosed in Note 28.

Management of the Pension Fund is the responsibility of the council's strategic director of finance and governance. No officers' remuneration is paid directly by the Fund; costs are instead recovered as part of the costs disclosed in Note 10. The strategic director of finance and governance remuneration is disclosed in Note 25 of the council's Statement of Accounts.

The Pension Advisory Panel (PAP) offers advice to the strategic director of finance and governance. Councillor members of the Panel make an annual declaration of their interests which is available on the council's website.

The council is also the single largest employer of members of the pension fund and contributed £37.3 million to the fund in 2016-17 (£39.9 million in 2015-16).

#### **15. FAIR VALUE HIERARCHY**

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

- Level 1 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. Listed investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.
- Level 2 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 and where these techniques use inputs that are based significantly on observable market data. They comprise property unit trusts.
- Level 3 are those where at least one input that could have a significant effect on the instruments valuation is not based on observable market data

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Description of asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivities affecting the valuations provided
<b>Market quoted investments</b>	Level 1	Published bid market price ruling on the final day of the accounting period	Not required	Not required
<b>Quoted bonds</b>	Level 1	Fixed interest securities are valued at a market value based on current yields	Not required	Not required
<b>Futures and options in UK bonds</b>	Level 1	Published exchange prices at the year-end	Not required	Not required
<b>Exchange traded pooled investments</b>	Level 1	Closing bid value on published exchanges	Not required	Not required
<b>Unquoted bonds</b>	Level 2	Average of broker prices	Evaluated price feeds	Not required
<b>Forward foreign exchange derivatives</b>	Level 2	Market forward exchange rates at the year-end	Exchange rate risk	Not required
<b>Overseas bond options</b>	Level 2	Option pricing model	Annualised volatility of counterparty credit risk	Not required
<b>Pooled investments – overseas unit trusts and some property funds</b>	Level 2	Closing bid price where bid and offer prices are published Closing single price where single price published	NAV-based pricing set on a forward pricing basis	Not required
<b>Freehold, leasehold properties</b>	Level 3	Valued at fair value at the year-end by independent valuers	Existing lease terms and rentals Independent market research Nature of tenancies Covenant strength for existing tenants Assumed vacancy levels Estimated rental growth Discount rate	Significant changes in rental growth, vacancy levels or the discount rate could affect valuations as could more general changes to market prices

The following table shows the fair value valuation hierarchy of Fund assets and liabilities.

Value as at 31 March 2017	Quoted market price	Using observable inputs	With significant un-observable inputs	Total
	Level 1	Level 2	Level 3	
	£000	£000	£000	£000
Financial assets at fair value through profit and loss	1,002,635	243,524	80,057	<b>1,326,216</b>
Non-financial assets at fair value through profit and loss	-	-	160,200	<b>160,200</b>
Financial liabilities at fair value through profit and loss	(19)	-	-	<b>(19)</b>
<b>Total</b>	<b>1,002,616</b>	<b>243,524</b>	<b>240,257</b>	<b>1,486,397</b>

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Value as at 31 March 2016*	Quoted market price	Using observable inputs	With significant un- observable inputs	Total
	Level 1	Level 2	Level 3	
	£000	£000	£000	£000
Financial assets at fair value through profit and loss	1,025,601	43,989		<b>1,069,590</b>
Non-financial assets at fair value through profit and loss	-	-	167,000	<b>167,000</b>
Financial liabilities at fair value through profit and loss	-	-	-	-
<b>Total</b>	1,025,601	43,989		<b>1,236,590</b>

The following table shows the reconciliation of fair value measurements within level 3.

	Value at 31/03/2016 £000	Transfers in/ (out) of level 3	Purchase £000	Sales £000	Realised gain/(loss)	Unrealised gain/(loss)	Value at 31/03/2017 £000
Property	167,000	43,989	40,123	(6,913)	(519)	(3,423)	240,257
<b>Total</b>	<b>167,000</b>	<b>43,989</b>	<b>40,123</b>	<b>(6,913)</b>	<b>(519)</b>	<b>(3,423)</b>	<b>240,257</b>

Transfers into level 3 comprise property unit trusts that were classified as level 2 for 2015-16. The explanation for this transfer is set out as part of Note 4.

The sensitivity analysis for the valuation of property investments, classified as level 3, is included within Note 18.

## 16. FINANCIAL INSTRUMENTS

The following table shows the classification of the Fund's financial instruments:

	2016-17 £000	2015-16* £000
<b>Financial assets</b>		
Loans and receivables	23,157	16,079
Financial assets at fair value through profit and loss	1,318,117	1,069,590
<b>Financial liabilities</b>		
Financial liabilities at amortised cost	(6,462)	(5,136)
Financial liabilities at fair value through profit and loss	(19)	-
<b>Total</b>	<b>1,334,793</b>	<b>1,080,533</b>

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**17. CONTINGENT LIABILITIES AND CONTRACTUAL ARRANGEMENTS**

Outstanding capital commitments (investments) at 31 March 2017 totalled £19.2m (31 March 2016: £55.6m)

These commitments relate to outstanding call payments due on property. The amounts 'called' by these funds are irregular in both size and timing over a number of years from the date of each original commitment.

**18. NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS**

*Risk and Risk Management*

The Pension Fund's primary long-term risk is that the fund's assets will fall short of its liabilities (i.e. promised benefits 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 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 council manages these investment risks as part of its overall pension fund risk management programme.

Responsibility for the fund's risk management strategy rests with the strategic director for finance and governance advised by the pensions advisory panel. Risk management policies are established to identify and analyse the risks faced by the council's pensions operations. Policies are reviewed regularly to reflect changes in activity and in market conditions.

*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 council and its investment advisers undertake appropriate monitoring of market conditions and benchmark analysis.

*Price Risk*

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

The fund is exposed to share price risk. This arises from investments held by the fund for which the future price is uncertain. All securities investments present a risk of a loss of capital. The maximum risk resulting from financial instruments is determined by the fair value of the financial instruments.

The fund's investment managers mitigate this price risk through diversification and the selection of securities and other financial instruments is monitored by the council to ensure it is within limits specified in the fund investment strategy.

Potential price changes are determined based on historical data and volatility of asset class returns. For example, 'riskier' assets such as equities will display greater potential volatility than bonds. The following table demonstrates the change in the net assets available to pay benefits, if the market price had increased or decreased in line. In consultation with the fund's investment advisers, the council has determined that the following movements in market price risk are reasonably possible for the 2016-17 reporting period:

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2016-17 - Asset Type	31/03/2017 £000	Change %	Value on Increase £000	Value on Decrease £000
Total Equities	838,500	9.7	919,835	757,166
Total Bonds & Indexed linked	277,145	8.8	301,542	252,748
Multi-Asset	122,264	5.1	128,499	116,028
Property	240,257	4.1	250,108	230,407
Cash Deposits	8,100	0.0	8,101	8,099
Other Assets	1,576	0.0	1,576	1,576
<b>Investment Assets</b>	<b>1,487,842</b>		<b>1,608,517</b>	<b>1,364,279</b>

2015-16 - Asset Type	31/03/2016 £000	Change %	Value on Increase £000	Value on Decrease £000
<b>Total Equities</b>	672,462	9.7	737,692	607,234
<b>Total Bonds &amp; Indexed linked</b>	243,208	7.3	260,962	225,454
<b>Multi-Asset</b>	118,475	5.0	124,399	112,551
<b>Property</b>	210,989	3.7	218,796	203,183
<b>Cash Deposits</b>	100	0.0	100	100
<b>Other Assets</b>	1,348	0.0	1,348	1,348
<b>Total Assets</b>	<b>1,246,582</b>		<b>1,343,297</b>	<b>1,149,870</b>

The potential 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 advisers' most recent review. The analysis assumes that all other variables, in particular foreign currency exchange rates and interest rates, remain the same.

Had the market price of the fund's 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 shown in the table above.

*Interest Rate Risk*

The fund invests in financial assets for the primary purpose of obtaining a return on investments. Fixed interest securities and cash are subject to interest rate risks, which represent the risk that the fair value of 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 council and its investment advisers 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.

Fixed interest securities, cash and cash equivalents are exposed to interest rate risk. The table below demonstrates the change in value of these assets had the interest rate increased or decreased by 1%:

Assets exposed to interest rate risks	Market value £000	Value on 1% rate increase £000	Value on 1% rate decrease £000
<b>As at 31 March 2017</b>	<b>146,725</b>	<b>148,192</b>	<b>145,257</b>
<b>As at 31 March 2016</b>	<b>133,757</b>	<b>135,095</b>	<b>132,419</b>

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*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 Sterling. A 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.

The fund's currency risk is routinely monitored by the council and its investment advisers in accordance with the fund's risk management strategy, including monitoring the range of exposure to currency fluctuations.

Overseas equities, fixed interest securities and futures, cash in foreign currencies and some elements of pooled investment vehicles are exposed to currency risk. The following table demonstrates the change in value of assets exposed to currency risk had there been a 10 per cent strengthening or weakening of the pound against foreign currencies.

Assets exposed to currency risk	Value £000	Change %	Value on foreign exchange rate increase £000	Value on foreign exchange rate decrease £000
<b>As at 31 March 2017</b>	<b>912,889</b>	<b>11.2</b>	<b>1,015,176</b>	<b>810,601</b>
<b>As at 31 March 2016</b>	<b>740,403</b>	<b>10.0</b>	<b>814,443</b>	<b>666,363</b>

*Credit Risk*

This is the risk the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. For example a stock may lose value or a dividend due may not be paid. The market values of investments generally reflect an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the fund's financial assets and liabilities.

The Fund has set out a series of restrictions in each investment manager's agreement. These restrictions are intended to limit the risks from each individual investment and prevent unsuitable investment activity. The Fund also employs a global custodian to ensure that all transactions are settled in a timely manner.

*Liquidity Risk*

This is the risk that the Pension Fund may not have the funds available to meet payments as they fall due. Historically the Fund has been cash positive (i.e. contributions received have been greater than benefits paid out). However this trend has begun to change. The reduction in active members and a resulting change in the membership profile have increased the liquidity risk of the Fund going forward.

The Fund currently has two bank accounts. One is held by the Global Custodian and holds cash relating to investment activities, the other is the Pension Fund Bank Account which holds the cash relating to member activities.

There is a strategy in place to ensure that if the Fund found itself in a position where it did not have the funds available to meet its commitments, alternative moneys could be drawn down. Funds could be called back from investment managers within a short period of time. Periodic cash flow forecasts are prepared to understand and manage the timing of the fund's cash flows. The appropriate strategic level of cash balances to be held forms part of the fund investment strategy.



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**19. ACTUARIAL POSITION OF THE FUND**

**Introduction**

The Scheme Regulations require that a full actuarial valuation is carried out every third year. The purpose of this is to establish that the London Borough of Southwark Pension Fund (the Fund) is able to meet its liabilities to past and present contributors and to review employer contribution rates. The latest full actuarial investigation into the financial position of the Fund was completed as at 31 March 2016 by Aon Hewitt Limited, in accordance with Regulation 62 of the Local Government Pension Scheme Regulations 2013.

**Actuarial Position**

The valuation as at 31 March 2016 showed that the funding ratio of the Fund had increased since the previous valuation with the market value of the Fund's assets at that date (of £1,256.4M) covering 88% of the liabilities allowing, in the case of pre- 1 April 2014 membership for current contributors to the Fund, for future increases in pensionable pay.

The valuation also showed that the aggregate level of contributions required to be paid by participating employers with effect from 1 April 2017 was:

- 15.3% of pensionable pay. This is the rate calculated as being sufficient, together with contributions paid by members, to meet the liabilities arising in respect of service after the valuation date (the primary rate). **Plus**
- Monetary amounts to restore the assets to 100% of the liabilities in respect of service prior to the valuation date over a recovery period of 18 years from 1 April 2017 (the secondary rate), equivalent to 5.6% of pensionable pay (or £10.7M in 2017/18, and increasing by 3.5% p.a. thereafter).

In practice, each individual employer's or group of employers' position is assessed separately and contributions are set out in Aon Hewitt Limited's report dated 30 March 2017 (the "actuarial valuation report"). In addition to the contributions shown above, payments to cover additional liabilities arising from early retirements and ill-health retirements will be made to the Fund by the employers.

The funding plan adopted in assessing the contributions for each individual employer or group was in accordance with the Funding Strategy Statement in force at the time. The approach adopted, and the recovery period used for each employer was agreed with the administering authority reflecting the employers' circumstances.

The valuation was carried out using the projected unit actuarial method for most employers and the main actuarial assumptions used for assessing the funding target and the contribution rates were as follows.

Discount rate	4.55% p.a.
Rate of pay increases (additional allowance made for promotional increases)	3.50% p.a.
Rate of increase to pension accounts	2.00% p.a.
Rate of increases in pensions in payment (in excess of Guaranteed Minimum Pension)	2.00% p.a.

The key demographic assumption was the allowance made for longevity. The post retirement mortality assumption adopted for the actuarial valuation was in line with standard self-administered pension scheme (SAPS) S2P mortality tables with appropriate scaling factors applied based on the mortality experience of members within the Fund and included an allowance for improvements based on the Continuous Mortality Investigation (CMI) Core Projections Model released with Working Paper 91 with Core assumptions, with a long term annual rate of improvement in mortality rates of 1.5% p.a. The resulting average future life expectancies at age 65 were:

	Men	Women
Current pensioners aged 65 at the valuation date	22.4	26.1
Future pensioners aged 45 at the valuation date	24.0	27.8

The assets were valued at market value.

Further details of the assumptions adopted for the valuation were set out in the actuarial valuation report.

The valuation results summarised above are based on the financial position and market levels at the valuation date, 31 March 2016. As such the results do not make allowance for changes which have occurred subsequent to the valuation date.

The formal actuarial valuation report and the Rates and Adjustments Certificate setting out the employer contribution rates for the period from 1 April 2017 to 31 March 2020 were signed on 30 March 2017. Contribution rates will be reviewed at the next actuarial valuation of the Fund as at 31 March 2019 in accordance with Regulation 62 of the Local Government Pension Scheme Regulations 2013.

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This Statement has been prepared by the current Actuary to the Fund, Aon Hewitt Limited, for inclusion in the accounts of the Fund. It provides a summary of the results of their actuarial valuation which was carried out as at 31 March 2016. The valuation provides a snapshot of the funding position at the valuation date and is used to assess the future level of contributions required.

This Statement must not be considered without reference to the formal actuarial valuation report which details fully the context and limitations of the actuarial valuation.

Aon Hewitt Limited does not accept any responsibility or liability to any party other than our client, London Borough of Southwark, the Administering Authority of the Fund, in respect of this Statement.

The report on the actuarial valuation as at 31 March 2016 is available on request from London Borough of Southwark, the Administering Authority of the Fund.

Aon Hewitt Limited  
**May 2017**

*Actuarial Present Value of Promised Retirement Benefits*

IAS 26 (retirement benefit plans) requires the 'actuarial present value of promised retirement benefits' to be disclosed in the Pension Fund Accounts using the most recent actuarial valuation. The fund was last valued as at 31 March 2016.

	<b>31 March 2016 £m</b>	<b>31 March 2013 £m</b>
Fair value of net assets	1,256	995
Actuarial present value of promised retirement benefits	(1,671)	(1,451)
<b>Surplus/(deficit) in the fund as measured for IAS26</b>	<b>(413)</b>	<b>(456)</b>

**20. POST BALANCE SHEET EVENTS**

No such material events have occurred.