SOMERSET COUNTY COUNCIL PENSION FUND

ANNUAL REPORT AND FINANCIAL STATEMENTS

2011/12

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SOMERSET County Council

Contents

Chairman's report

This annual report sets out the activities of the pension fund for the year ending 31 March 2012. It is produced to provide information for the following four groups.

- **Those responsible for managing the fund (our elected members).**
- **Those currently receiving benefits from the fund (the pensioners).**
- **Those who will receive benefits from the fund in the future (the deferred pensioners).**
- **Those who contribute to the fund (the active scheme members and employers).**

At the time of last year's report the government had already implemented a change from RPI to CPI for calculating the annual inflationary increase in pensions in payment. The Coalition Government had also announced plans to increase employee contributions by an average of 3.2% to be introduced in stages from April 2012 and the Government and Unions were negotiating on this point. Finally we had already received the report of the commission charged with recommending the future shape of all public sector pension provision led by Lord Hutton. We were expecting the process for negotiation and the resulting changes to take us through to a new scheme in 2015.

Having just reviewed where we stood last year, and with the benefit of hindsight, considerable progress on these proposals has been made and not necessarily in the ways we might have expected. The funded nature of the Local Government Pension Scheme (LGPS) has meant that any change in the future benefit structure instantly lowers employer contributions and as a result the overall increase in members contributions has been dropped against a concession of lower benefits compared to what was originally proposed. Part of this negotiation has also seen the date from which the new scheme will become effective brought forward one year to April 2014.

In June 2012 a joint statement from the unions and the Local Government Association announced an agreed structure for what the benefits and employee contributions might look like for the LGPS from 2014. An outline of what the proposals are is contained later in this annual report. We anticipate a formal Government consultation process to take place during the autumn and then legislation in the early part of 2013 to allow the actuaries to take account of the new scheme when doing their work on the 2013 valuation. This is a very tight timescale but all sides appear committed to meeting it. Inevitably this will mean the benefits administration team will be very busy both on implementing the necessary changes to systems and in communicating the new scheme to all of the fund's stakeholders.

Investment returns for the year, at 2.6%, were positive but below the level we need to maintain the overall funding position. We achieved positive returns from all of our non-equity assets and equities within the global, UK, US and Japan portfolios. Given the on going sovereign debt issues it is not surprising that we did not achieve positive returns in European equities.

Since 2004 the fund has had a customised benchmark. The fund's return for the year was disappointingly below the benchmark return of 3.6%. While we measure ourselves against our own benchmark, we are also aware of how other local-authority funds perform. A typical local-authority pension fund's return for the 2010-11 year was also 2.6%.

During the year, contributions paid into the scheme were greater than the pensions paid out. We made this extra money available to investment managers. The end result can be seen in the revenue account, where an extra £7.5 million is shown at the end of the financial year.

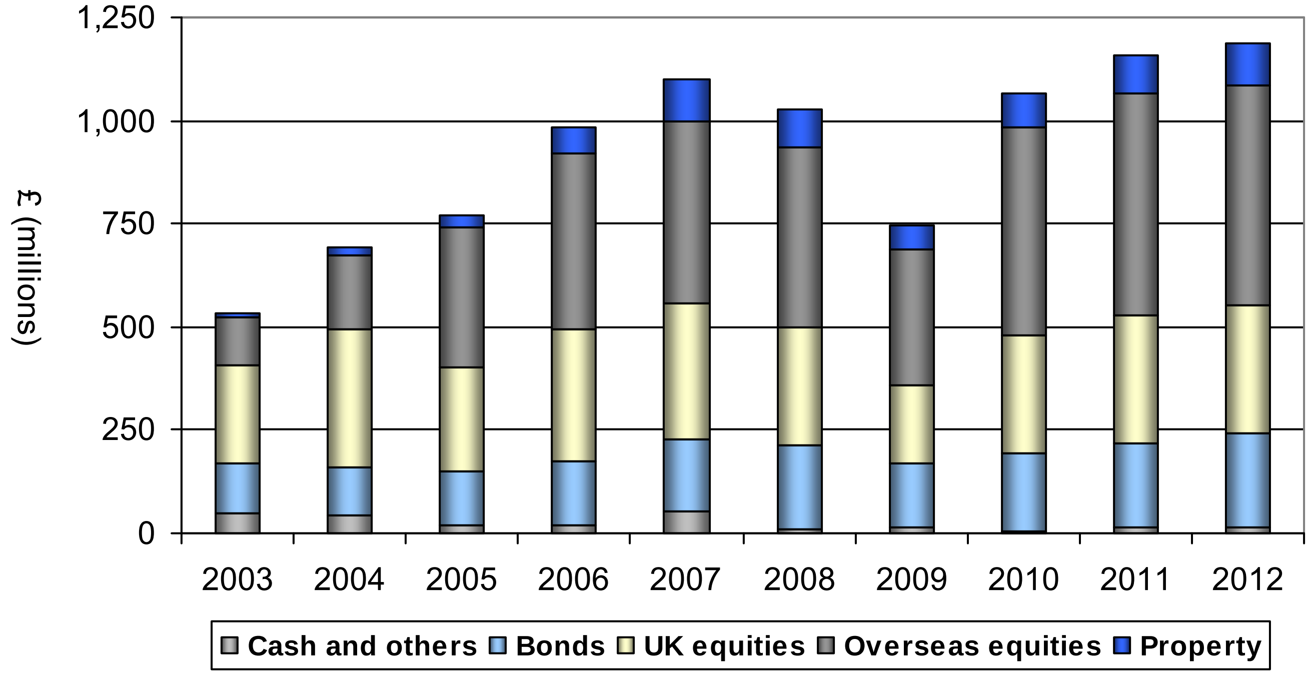
I would like to thank my fellow committee members for their commitment and support over the last year and the officers for their efforts throughout the year in providing an excellent fund for the member organisations and their employees. I would particularly like to mention Alan Ham, who returned to the committee after a brief sabbatical during the year. Alan sat on this committee and its predecessors for more than 18 years and contributed hugely to the fund. Alan passed away during the year after a short illness and we will all miss his presence and his input. This is my last report as Chairman of the pensions committee as other commitments I now have within Somerset County Council mean I am not able to commit the time to the pensions committee which it deserves. I have thoroughly enjoyed the last three years as Chairman. I wish my successor as Chair, Councillor Dawn Hill, and the new members of the committee, William Wallace, Tim Carroll and Anthony Trollope-Bellew, good fortune in taking on the stewardship of the fund.

Bob Little
Chairman of the pensions committee

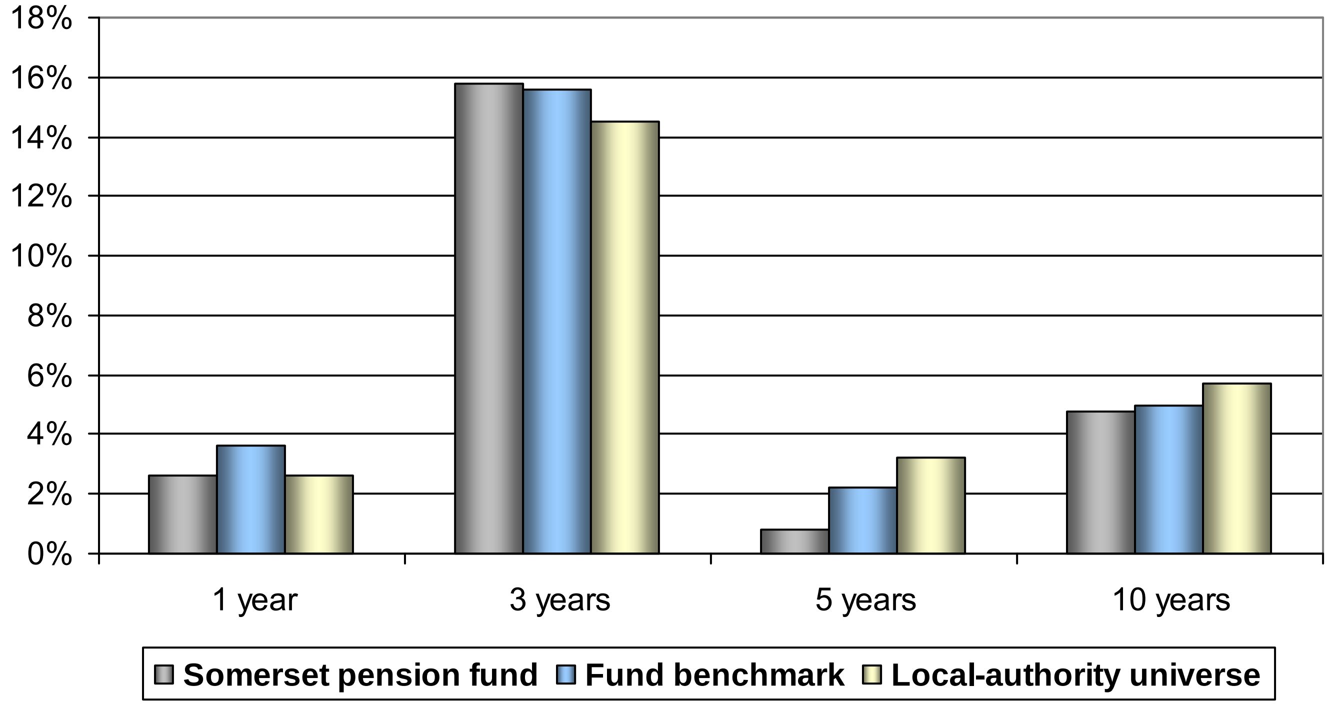
Summary of the scheme

Statistics

Fund investment assets

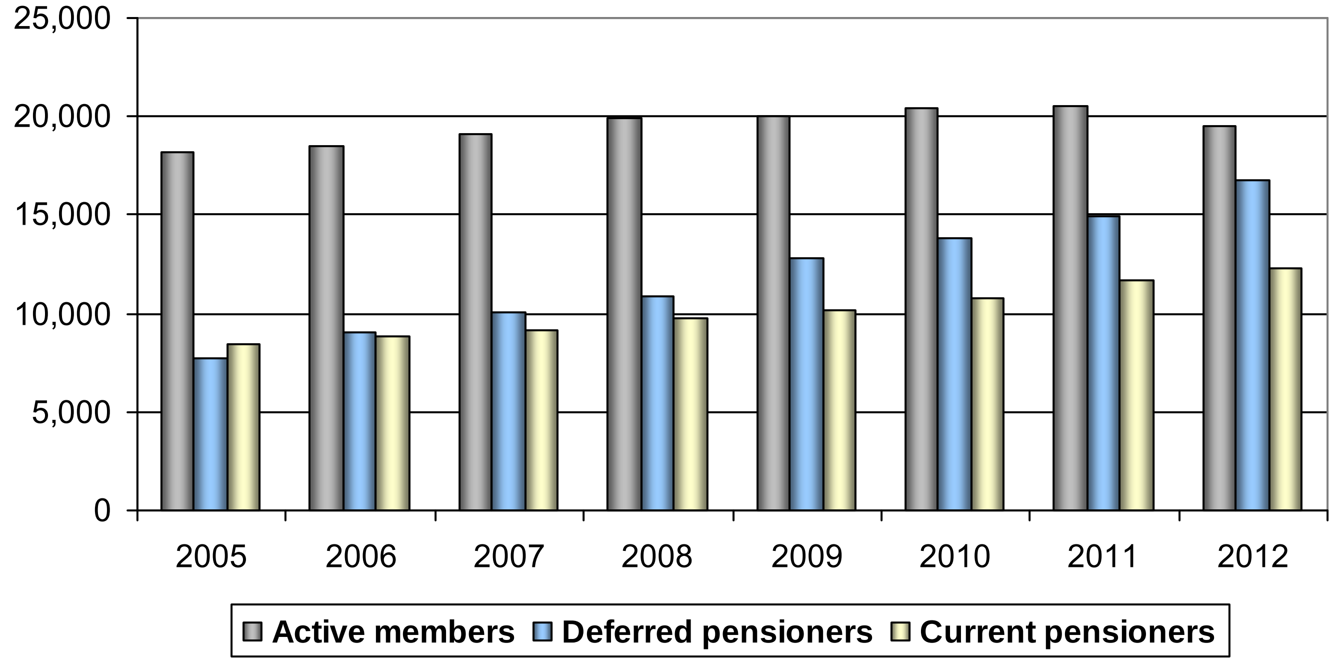


Annualised fund investment performance



Source: WM Company

Fund membership statistics



Financial Statistics – five-year trends

	2007/2008 £ millions	2008/2009 £ millions	2009/2010 £ millions	2010/2011 £ millions	2011/2012 £ millions
Income from contributions	75.245	80.682	89.100	90.801	82.370
Spending on benefits	-56.673	-60.251	-68.524	-78.102	-74.836
Contributions less benefits	**18.572**	**20.431**	**20.576**	**12.699**	**7.534**
Investment income	33.248	34.230	30.308	28.686	34.812
Change in value of investments	-120.631	-327.662	262.391	52.568	-12.774
Net return on investments	**-87.383**	**-293.432**	**292.699**	**81.254**	**22.038**
Change in net assets	**-68.811**	**-273.001**	**313.275**	**93.953**	**29.572**

Pensions committee

Somerset County Council, the administering authority for the pension fund, has delegated its responsibility to manage the fund to the pensions committee under the county council's constitution.

The pensions committee meets regularly to consider all aspects of the administration of the fund. In line with legal regulations, they get advice from professional advisors, the fund's managers and officers, as necessary. The pensions committee makes decisions about the fund's overall policy and investment strategy, taking account of the professional advice it has received.

Unless stated otherwise members sat on the committee for the full year covered by this report.

Bob Little (Chairman)

Bob is one of the four county council representatives on the committee and is the councillor for Castle Cary. Bob joined the committee in May 2009.

Sam Crabb

Sam is one of the four county council representatives on the committee and is the councillor for Ilchester. Sam has been a member of the pensions committee since May 2008.

Dawn Hill

Dawn is one of the four county council representatives on the committee and is the councillor for Cheddar. Dawn joined the committee in May 2009.

John Wilkins

John is one of the four county council representatives on the committee and is the councillor for Lydeard. John joined the committee in May 2009.

Duncan McGinty (district councils' representative)

Duncan represented the five district councils that are members of the fund. Duncan is the leader of Sedgemoor District Council. Duncan joined the committee in May 2010. Duncan stepped down from the committee in October 2011.

Tim Carroll (district councils' representative)

Tim represents the five district councils that are members of the fund. Tim is the deputy leader of South Somerset District Council. Tim joined the committee in October 2011 to replace Duncan McGinty. Tim previously represented the district councils on the committee between 1998 and May 2010.

Alan Ham (police authority representative)

Alan represented the Avon and Somerset Police Authority, where staff who are not eligible for the police officers' pension scheme are entitled to join the fund. Alan was a member of the police authority. Alan joined the committee in May 2011 as the police representative having stood on the committee as a county council representative from 1990 to 2009. Alan was stood down in September 2011.

William Wallace (police authority representative)

William represents the Avon and Somerset Police Authority, where staff who are not eligible for the police officers' pension scheme are entitled to join the fund. William is a member of the police authority as a representative of Somerset County Council. William joined the committee in October 2011 to replace Alan Ham.

Caroline Moore (represents other employers)

Caroline represents all of the employers except those specifically covered by another committee member. Caroline is Executive Director (Finance, Development and Corporate Services) for Yarlington Housing Group (YHG). She also acts as Company Secretary for YHG and its subsidiaries, and is a member of the National Housing Federation's Finance Policy Committee.

Caroline joined YHG in 2002, having previously spent eight years as Senior Manager (Public Services) at PricewaterhouseCoopers (PWC), where she was a national manager responsible for all services to housing clients. She spent the last three years at PWC advising on housing transfers (both on the council and housing association sides).

Caroline is an ACA-qualified accountant and has a degree in Business and Organisational Studies. Caroline has been a member of the pensions committee since 2005.

Sarah Payne (employees' and members' representative)

Sarah is the employees' and members' representative on the pensions committee. Until 2010 she was employed by the county council as their Extended Schools Services Manager within the Children and Young Person's Directorate and during her career she worked in a variety of roles and directorates, giving her a wide range of experience of local-government services. She is now self employed and a deferred member of the fund. Sarah still retains contact with the trade union UNISON who support her position as employees' and members' representative on the committee. Sarah joined the pensions committee as the members' representative in 2004.

As well as the committee members, an independent advisor and officers attend all committee meetings.

Independent advisor – Caroline Burton

After graduating from Oxford University, Caroline joined Guardian Royal Exchange plc in 1973 as a trainee investment analyst. She moved from analysis to portfolio management and became manager of international investments in 1978. In 1987 she became Managing Director of the newly-incorporated Guardian Asset Management. She joined the board of Guardian Royal Exchange plc as the Executive Director for Investment in 1990, a post she held until the company was taken over by AXA in 1999.

Caroline currently advises a number of pension schemes. She is a member of the board of TR Property Investment Trust plc, a director of Blackrock Smaller Companies Investment Trust, a director of Rathbone Brothers plc, a member of the management committee of Hermes Property Unit Trust and a non-executive director of LV= Insurance.

Caroline has been the independent advisor to the pensions committee since 2002.

Officer – Kevin Nacey (Director of Finance and Performance)

Kevin has been the lead officer for the pension fund since January 2011.

The work the committee has done this year

During the financial year 2011/2012, the committee formally met five times. At four of these meetings (quarterly) the committee received a report on the investment performance of the fund for the previous quarter and any related information, an update on the committee business plan and workplan and an update on the budget and membership statistics of the fund. They also receive an update on the status of all outstanding matters relating to the employer bodies within the fund. At two meetings every year the committee receive a report covering the voting activity at company meetings for the previous six months. Every September, the committee receive the report from the external auditor and the auditor's opinion on the accounts of the fund, a report from the WM Company on the investment returns for the previous financial year and an update on the funding position from the fund's actuary.

The committee also carried out a number of one-off reviews during the year. The committee reviewed and revised the Statement of Investment Principles, Governance Policy Statement, Governance Compliance Statement and Scheme of Delegation to ensure they continue to reflect the underlying practices of the fund and best practice. During the year, as part of an ongoing programme, the committee formally reviewed a number of the external fund managers, and decided to continue with those managers for the time being with the exception of the J.P. Morgan's US equity mandate and both of Record's currency mandates, the active having been suspended in June 2010. All of these mandates ended in December 2011. For the remaining managers committee agreed to review the managers again in the future.

As well as the formal meetings the committee have, they also meet with external fund managers. The committee also attend the annual meeting for employers every September, where they are available to answer any questions.

Committee training

As part of our new training policy, the committee members are committed to developing their skills and knowledge in relation to the pension fund. As part of this commitment, officers arranged two specific training days for the members. One training day focussed on the Hutton Report and its implications for the LGPS as well as training and discussions on the funds governance arrangements. The other training day focussed on the funds liabilities and asset allocation options. We have encouraged our members to attend appropriate outside training events and conferences.

The table below shows how many formal meetings, informal meetings and training events committee members attended this year.

	Committee meetings	Annual meeting	Internal training days	External training days	Conference days
Number of meetings	5	1	2		
Committee members					
Bob Little (Chairman)	5	1	1		3
Sam Crabb	4	1	2		4
Dawn Hill	4	1	1		
John Wilkins	4		2		
Duncan McGinty	0 of 3				
Tim Carroll	0 of 2				
Alan Ham	2 of 2		1		
William Wallace	2 of 2				
Caroline Moore	4	1	2		1
Sarah Payne	5	1	2		2
Independent advisor					
Caroline Burton	4	1			

Fund managers

Under the regulations, we must consider:

- **the need to invest in a wide range of investment areas;**
- **the suitability of investments; and**
- **getting proper advice.**

The fund is divided into 13 sub-funds for investment-management purposes.

In-house

Background
Three sub-funds are managed under the direct control of the Director of Finance and Performance. The management is done in-house as it has proved over many years to be a cost-efficient way to invest.

Global Equity Portfolio

Aim
To track the benchmark.

Benchmark
FTSE All-World Developed Index. This index contains over 2,000 companies from the 25 countries that FTSE have defined as 'developed'.

Type of investments
Equities. A percentage of these investments are overseas.

Method
Since this fund has a passive investment style, a quantitative analysis system is used to identify suitable equity stocks to be held in the UK and overseas.

Allocation of the fund
The target allocation was 25% of the whole fund. This was revised to 23% of the whole fund with effect from 1st January 2012.

Appointed
The pension fund has been running an in-house tracking fund since February 1991.

US Equity Portfolio

Aim
To track the benchmark.

Benchmark
S&P 500 index

Type of investments
USA equities

Method
Since this fund has a passive investment style, a quantitative analysis system is used to identify suitable equity stocks to be held in the USA.

Allocation of the fund
The target allocation is 5% of the whole fund.

Appointed
The in-house team took over the running of the US equity fund on 1st January 2012

Cash Portfolio

Aim
To outperform Sterling deposit rates

Benchmark
7 day LIBID (London Interbank Bid Rate)

Type of Investments
Cash deposits and Money Market Funds

Allocation of the fund
The target allocation is 1% of the whole fund.

Appointed
The in-house team have been running the Sterling cash fund since at least 1990

Standard Life Investments

Background
Standard Life Investments manage two sub-funds. Standard Life Investments is a leading asset management company, with £160.6 billion of assets under management (as at 31 March 2012) invested across a wide range of mandates, asset classes and geographies. Employing over 1,000 individuals, Standard Life Investments is based in Edinburgh, with regional offices in Ireland, France, Hong Kong, Australia, Canada and the USA, and has representative offices in Germany, China and Korea.

Standard Life Investments is owned entirely by Standard Life plc, which is listed on the London Stock Exchange.

<u>UK equity portfolio</u>

Aim
To outperform the benchmark by an annualised return of 1.75% over continuous three-year periods after Standard Life's fees have been deducted.

Benchmark
FTSE All-Share index.

Type of investments
UK equities

Allocation of the fund
The target allocation is 23% of the whole fund.

Appointed
July 2004

<u>Fixed-income portfolio</u>

Aim
To outperform the benchmark by an annualised return of 0.75% over continuous three-year periods after Standard Life's fees have been deducted.

Benchmark
22% FTSE Actuaries UK government all-stock gilt total return index
21% FTSE Actuaries UK government index-linked all-stocks total return index
43% iBoxx Sterling non-gilt over 10-year total return index
15% Merrill Lynch European Currency High Yield Index

Type of investments
Bonds

Allocation of the fund
The target allocation is 19% of the whole fund.

Appointed
February 2008

Jupiter Asset Management

Background
Jupiter was founded in 1985 and has grown to become one of the most respected fund management groups in the UK, managing £24.2 billion (as at 31 March 2012) across equity and other asset classes. In 2007, Jupiter became majority owned by its employees. In June 2010, Jupiter's holding company (the company that owns it and other businesses in their group), Jupiter Fund Management plc, was listed on the London Stock Exchange.

Jupiter acts on behalf of clients ranging from pension funds and larger charities to asset managers, government organisations, businesses, local authorities, and private individuals. Jupiter manages assets across a wide range of international and UK-based mutual funds, multi-manager products and hedge funds. These assets include portfolios that focus on specific markets such as the UK, Europe, Asia and emerging markets in Europe, as well as specialist asset classes such as socially responsible investments (SRI), financials and global equities.

Aim
To outperform the benchmark by an annualised return of 1.5% over continuous three-year periods after Jupiter's fees have been deducted.

Benchmark
FTSE World Europe ex-UK Index.

Type of investments
European equities, not including UK equities

Allocation of the fund
The target allocation is 5% of the whole fund.

Appointed
April 1989 (revised mandate from July 2004).

UBS Global Asset Management

Background
UBS Global Asset Management offers investment capabilities and styles across all major traditional and alternative asset classes throughout the world. They have invested assets of approximately Swiss Franc 559 billion as at 31 March 2011. They are a leading fund manager in Europe, the largest mutual fund manager in Switzerland and one of the largest fund of hedge funds and real estate investment managers in the world.

UBS Global Asset Management employs around 3,700 people located in 25 countries. Their main offices are in London, Chicago, Frankfurt, Hartford, Hong Kong, New York, Paris, Singapore, Sydney, Tokyo, Toronto and Zurich.

UBS Global Asset Management (UK) Ltd is a subsidiary of the Swiss listed company UBS AG.

Aim
To outperform the benchmark by an annualised return of 1.5% over continuous three-year periods after UBS's fees have been deducted.

Benchmark
FTSE All-World Developed Asia Pacific ex-Japan Index

Type of investments
Far East equities. This will mainly be equities listed in South Korea, Hong Kong, Singapore, Australia and New Zealand, but other Asian countries are allowed.

Allocation of the fund
The target allocation is 3% of the whole fund.

Appointed
July 2004

Nomura Asset Management

Background

Owned entirely by the Nomura Group and founded in 1873, Nomura Asset Management is one of the largest investment managers in the world. They have total group assets under management of over US$293 billion, including US$57 billion (£35.6 billion) in Japanese equities, as at 31 March 2012.

Nomura's specialist investment approach relies on being based in Asia and having local investment managers and research analysts. The company has their headquarters in Tokyo, but also have offices in the large financial centres around the world, including London, New York, Frankfurt, Hong Kong and Singapore. They also have offices in Seoul , Shanghai and Kuala Lumpur.

Nomura Holdings Inc is listed on the Tokyo Stock Exchange.

Aim

To outperform the benchmark by an annualised return of 1.5% over continuous three-year periods after Nomura's fees have been deducted.

Benchmark

TOPIX Index

Type of investments

Japanese equities

Allocation of the fund

The target allocation is 3% of the whole fund.

Appointed

March 2010

Pioneer Investments

Background
Pioneer Investments is a leading asset manager with an 80-year history of providing investment management solutions to clients from institutions, corporations and private investors around the world. Pioneer is a worldwide organisation, employing around 2,000 people, including over 320 investment professionals, in 26 countries. Its main investment offices are based in Boston, Dublin and London, and are supported by 11 local investment offices to manage £130 billion of total assets under management as at 31 March 2012.

Pioneer Investments is a subsidiary of the Italian listed company, Unicredit SpA.

Aim
To outperform the benchmark by an annualised return of 1.5% over continuous three-year periods after Pioneer's fees have been deducted.

Benchmark
MSCI Emerging Markets Index

Type of investments
Equities from emerging markets around the world

Allocation of the fund
The target allocation is 3% of the whole fund.

Appointed
March 2009

Aviva Investors

Background

Aviva Investors is owned entirely by Aviva plc, one of the world's largest insurance groups. Aviva Investors has assets under management of more than £272 billion, across a range of funds. Their clients range from large financial institutions to advisors, who provide investment solutions for individuals. Aviva Investors is a significant business in its own right. They employ almost 1,300 people, including 433 investment professionals, in 17 countries around the world.

Aviva plc is listed on the London Stock Exchange.

Aim

To outperform the benchmark by an annualised return of 0.5% over continuous three-year periods after Aviva's fees have been deducted.

Benchmark

IPD All Balanced Funds Index

Type of investments

Property unit trusts

Allocation of the fund

The target allocation is 10% of the whole fund.

Appointed

February 2004

Neuberger Berman

Background
Founded in 1939, Neuberger Berman is an independent, employee-controlled global asset-management company serving the financial needs of institutional investors, consultants and individuals worldwide. The company provides a broad range of global investment solutions to investors through customised separately managed accounts and mutual funds.

Neuberger Berman manage traditional assets and alternative investments, including private equity and hedge funds. They also give portfolio advice. Managing over $194 billion of assets, Neuberger Berman is one of the world's largest independently controlled asset managers. They have more than 1,700 employees worldwide (including over 400 investment professionals) in over 27 cities in ten countries across the globe, as at 30 June 2012.

NB Alternatives, a specialist part of Neuberger Berman, is a significant investor in private equity, with over US$17 billion of committed capital (capital that is promised but may not have been invested yet) across our private equity fund, secondary investments and direct co-investment areas.

Aim
To outperform global equity stock markets over the life of each private equity fund.

Benchmark
Cash returns. This is the normal benchmark for private equity investments.

Type of investments
Companies that are not listed on stock exchanges

Allocation of the fund
The target allocation is 3% of the whole fund.

Appointed
March 2010

As well as the 11 funds mentioned previously, the Record passive currency fund was in run-off having been closed at the end of December and the pension fund has a small interest in the South West Regional Venture Capital Fund, which is managed by Yorkshire Fund Managers Ltd. For a table showing the split of the assets by fund manager at the date of the net asset statement, see note 9 of the accounts on page 85.

Other experts

We need to work with a number of experts to provide functions that are needed under various regulations.

Custodian – BNY Mellon

Custody services manage the records of the fund's cash and security investments and track and settle the investment transactions of the fund's appointed investment managers.

BNY Mellon is a specialist provider of custody and related services to pension funds in the UK. Among the services offered are:

- safe custody;
- managing cash;
- measuring investment performance;
- investment accounting;
- securities lending;
- transition management; and
- foreign-exchange facilities.

BNY Mellon is the corporate brand of The Bank of New York Mellon Corporation, which is listed on the New York Stock Exchange. The Bank of New York Mellon Corporation resulted from a merger, completed in late 2007, between The Bank of New York and the Mellon Financial Corporation, and operates in 36 countries and serves more than 100 markets. As at 31 December 2012, the company had total assets under custody of US$27.1 trillion

BNY Mellon has been the fund’s custodian since February 2005.

Auditors – Audit Commission

The role of the auditor is to test the accounts and confirm that they give a true and fair view of the fund’s financial position.

The Audit Commission is a public corporation set up in 1983 to protect the public purse. The Commission appoints auditors to councils, NHS bodies (excluding NHS foundation trusts), local police bodies and other local public services in England, and oversees their work. The auditors they currently appoint are either Audit Commission employees (their in-house Audit Practice) or one of the private audit firms. The Commission also helps public bodies manage the financial challenges they face by providing authoritative, unbiased, evidence-based analysis and advice.

The Audit Commission’s in-house Audit Practice became the auditor for the fund in 2008.

Actuary – Barnett Waddingham

The role of the actuary is to give the fund information about the fund's liabilities and the best way to meet them. Every three years, the actuary carries out a formal valuation of the fund, which shows how the fund's liabilities relate to its assets and recommends suitable rates of employers' contributions to prevent any shortfall in future years.

Barnett Waddingham LLP is the largest independent partnership of actuaries and consultants in the UK. The founding firm dates back to 1961. It is a limited liability partnership owned entirely by its 54 partners, with over 500 employees, including 61 associates, in seven offices across the UK.

Although they mainly provide actuarial advice to defined benefit pension funds, they do provide other services which include:

- scheme actuary and associated services to defined-benefit pension schemes;
- advice to defined-contribution pension schemes;
- accounting statistics for UK and international companies;
- advice on business transactions;
- independent advice to employers sponsoring pension arrangements;
- investment strategy reviews and advice on the funding strategy;
- communications programmes;
- administration and management services, including pensioner payroll, preparing annual accounts and secretarial services;
- managing closed schemes, wind-ups and reconstructions; and
- tax-efficient retirement planning for executives, directors and wealthy individuals.

Barnett Waddingham has been providing actuarial advice to local authorities about funds set up under the Local Government Pension Scheme Regulations and their predecessors for over 10 years

Barnett Waddingham has been the fund's actuary since April 2006.

Legal advisor – Osborne Clarke

The role of the legal advisor is to provide independent advice on legal matters affecting the fund.

Osborne Clarke is an international business law firm with around 700 staff and partners working in offices in major financial and commercial centres in the UK and across Europe. The firm's main areas of expertise include corporate, finance and property transactions and the full range of business law services, including commercial contracts, employment, pensions and resolving disputes.

The lawyers in Osborne Clarke's pensions team have a wide range of experience in advising large occupational pension schemes, and provide a wide range of legal services. These include legal issues relating to how Local Government Pension Scheme (LGPS) regulations are interpreted and applied, drafting investment management and custody agreements, and advising on commercial contracts.

Osborne Clarke was appointed as legal advisor to the fund in October 2006 as part of a unique joint tender involving a number of other local-authority pension funds in the southwest of England.

Performance measurement – The WM Company

The role of the performance measurer is to independently work out the return on the assets managed by each of the investment managers. It will also compare these figures with the benchmark given to each manager and the overall fund against its own benchmark and other local authorities' funds.

WM Performance Services (WM) is part of State Street Investment Analytics (SSIA), the global performance division of State Street Bank & Trust Company. WM has more than 30 years' experience of providing performance evaluation for a wide range of asset owners and managers

SSIA provide customers with industry-leading performance, risk, compliance and consultancy services by using the wealth of experience and services from 18 offices around the world. SSIA currently analyse assets of more than US$11 trillion worldwide and have one of the largest databases of actual fund information.

WM currently measures about 90% of UK local authority pensions funds, with a combined value of more than £143 billion as at 31 March 2012. As well as producing the Local Authority Universe and CIPFA Statistics, SSIA is also responsible for working out the returns for the annual Local Government Conference Awards.

WM has been providing the fund with performance measurement services since 1983.

Voting advice – Pensions Investment Research Consultants (PIRC)

PIRC provides us with background information about proposed votes at company meetings, along with a recommendation on how to vote in line with best corporate-governance practice. The in-house managed funds use this information and PIRC's recommendations to help us decide how to vote.

PIRC was founded by local-authority funds in 1986 to provide high-quality research on the social responsibility that businesses have. It now provides voting and engagement services to around 60% of the local government pensions market and is now the largest proxy-voting adviser in Europe. PIRC also holds the UK's largest single shareholder to provide engagement services in its partnership agreement with the Local Authority Pension Fund Forum. In total, PIRC carries out research and gives advice on environmental, social and governance issues to investors with assets of over £1.5 trillion.

Shareholder engagement on socially responsible investment and corporate governance – The Local Authority Pension Fund Forum (LAPFF)

Our fund is committed to working with companies to improve their awareness of environmental and social issues.

LAPFF is an association of (currently) 55 local-authority pension funds, which together have assets of £115 billion. It aims to bring about improvements in the way companies are run, such as improvements in corporate governance of the companies in which member funds invest. LAPFF is also concerned with promoting corporate social responsibility on environmental issues and issues relating to overseas employment standards. It does this by working with company boards to encourage them to improve standards.

Contributions and benefits

The Local Government Pension Scheme (LGPS) has been approved under the Local Government Superannuation Act 1972 and has been updated by the Pension Scheme Regulations 1997. The 'new-look' LGPS was introduced in April 2008 as a result of further legislation.

As an administering authority, we must maintain a pension fund for all the County Council's relevant employees (other than teachers) and those of all local-government staff in our area.

The fund also includes civilian employees of the Avon and Somerset Police Authority and the employees of further-education colleges and academy schools. Employees of certain other organisations (town councils, for example) have a right to be included. We have agreed to admit a number of other organisations, including several housing associations.

The fund is financed by contributions from employees and employers, together with interest and other income earned from investing funds not needed to meet pension payments in the short term.

Employees' contributions are fixed by government regulation. Employers' contributions are assessed by the fund's actuary every three years, but are reviewed every year to take account of early retirements. If there are a lot of early retirements, the contribution rate is increased immediately.

Contributions

Employees – Tiered contribution rates depending on annual salary, with seven contribution bands ranging from 5.5% to 7.5%.

Contribution rate	Salary range 2010-2011	Salary range 2011-2012	Salary range 2012-2013
5.50%	£0 to £12,600	£0 - £12,900	£0 to £13,500
5.80%	£12,601 to £14,700	£12,901 – £15,100	£13,501 to £15,800
5.90%	£14,701 to £18,900	£15,101 - £19,400	£15,801 to £20,400
6.50%	£18,901 to £31,500	£19,401 - £32,400	£20,401 to £34,000
6.80%	£31,501 to £42,000	£32,401 - £43,300	£34,001 to £45,500
7.20%	£42,001 to £78,700	£43,301 - £81,100	£45,501 to £85,300
7.50%	More than £78,700	More than £81,100	More than £85,300

Employers – Separate rates apply to the major employing authorities, to make sure the actuarial requirements are met and are expressed as a percentage of employees' pensionable pay.

	2010/2011	2011/2012		2012/2013		2013/2014	
	% of Payroll	% of Payroll	Cash payment £000	% of Payroll	Cash payment £000	% of Payroll	Cash payment £000
Common fund rate	14.7%	17.9%	0	17.9%	0	17.9%	0
Somerset County Council	15.1%	13.5%	3,770	13.5%	4,880	13.5%	5,830
Mendip District Council	17.6%	13.0%	240	13.0%	280	13.0%	320
Sedgemoor District Council	15.4%	12.9%	300	12.9%	410	12.9%	520
South Somerset District Council	15.5%	16.5%	0	17.5%	0	18.4%	0
Taunton Deane Borough Council	15.0%	16.1%	0	17.3%	0	18.4%	0
West Somerset District Council	15.4%	13.2%	90	13.2%	120	13.2%	160
Avon and Somerset Police	13.5%	13.7%	0	13.7%	0	13.7%	0
Avon and Somerset Probation	13.5%	13.2%	100	13.2%	160	13.2%	220
Further education colleges	14.1%	13.0%	Variable	13.0%	Variable	13.0%	Variable
Acadamies		15.1%	0	15.1%	0	15.1%	0
Town councils	17.7%	14.6%	Variable	14.6%	Variable	14.6%	Variable
Admitted organisations	12.9% to 19.6%	10.7% to 18.0%	Variable	10.7% to 18.0%	Variable	10.7% to 18.0%	Variable

A full actuarial valuation of the fund was carried out as at 31 March 2010 and this showed a funding level of 77%. This was lower than the level at the 2007 valuation, principally because investment returns have been disappointing through the credit crunch and ensuing recession.
A fall in the funding level at this valuation has inevitably seen increases in the contribution rates of most of the employers within the fund. In a departure from past practice most employers have chosen to make payments towards the funding deficit as prescribed cash amounts rather than as a percentage of payroll. This approach has been taken to ensure the deficit reduction plan is not affected by changes in the size of the employee base as local government undergoes a period of considerable change.

A further valuation of the fund will be carried out as at 31 March 2013. This will set employers' contribution rates for the following three years and confirm the funding level.

The benefits structure of the fund is set by government laws and we cannot change this.

Major benefits

- A retirement pension at the rate of 1/60 of the final year's pensionable pay (or the highest three years' pay out of the last 10 years of employment) for each year the individual has been a member of the scheme.
- Up to 25% of the pension can be exchanged for a tax-free lump sum.
- Lump-sum death benefits of three times pay for death in service.
- Lump-sum cover for death after retirement of a guarantee of 10 times' annual pension.
- A revised ill-health retirement package with three levels of benefits depending on the seriousness of the individual's illness.
- A nominated partner's pension and dependent children's pensions.
- Pensions that are protected from inflation through the Pensions (Increase) Acts.

Other benefits

- Scheme members can 'top up' their pension benefits by paying additional contributions. This facility has become more popular – both through the in-house scheme 'added benefits' facility and the in-house additional voluntary contributions (AVCs) plan. Prudential are now the fund's AVC provider, although a few members continue with their existing arrangements with Equitable Life.

All local-government pensions are protected against inflation under the public-sector index-linking arrangement. The increase applied from 9th April 2012 was 5.2%.

Possible future changes to the contributions and benefits

Following the review of public sector pension provision undertaken by the Hutton commission during 2011 the Government, Unions and Employers within local government have made a joint statement in June 2012 regarding an agreed template for a revised LGPS.

Under the proposals the employee contributions will still be based on salary bands however the calculation on which band an employee falls in will be based on actual pay not full time equivalent pay for part time workers. The new bands that are proposed are as follows:

Contribution rate	Salary range
5.50%	£0 to £13,500
5.80%	£13,501 to £21,000
6.50%	£21,001 to £34,000
6.80%	£34,001 to £43,000
8.50%	£43,001 to £60,000
9.90%	£60,001 to £85,000
10.50%	£85,001 to £100,000
11.40%	£100,001 to £150,000
12.50%	More than £150,000

It is estimated that the average percentage contribution for the LGPS as a whole will be broadly unchanged at 6.5%.

The key elements of the proposed revised benefits package are as follows:

- Calculation of benefits will move to CARE (Career Average) salary basis rather than the existing final salary basis;
- The revaluation of earnings as part of the CARE calculation will be based on CPI;
- The accrual rate will move from a 60^{th} to a 49^{th} of salary for each year of service;
- Normal retirement age will be synchronised with state retirement age rather than the current age of 65.

It is proposed that all service earned by members of the LGPS prior to the introduction of the new scheme will be preserved under the existing benefits rules.

It is also proposed that there will be a so called 50/50 option where an employee can chose to pay half the contributions but will accrue half of the benefits.

The timetable announced by the Government is that following informal discussions over the summer there will be a formal consultation process in the autumn with a view to the necessary legislation being agreed by parliament before the 31^{st} March 2013. Assuming that this timetable is met this will allow the actuaries to undertake the 2013 valuation exercise with the new benefits package and will see the new scheme come into force from 1^{st} April 2014.

Principles and policies

The statements, policies and principles listed below are those that were in place at 31st March 2012.

Funding strategy statement

Overview

This Statement has been prepared in accordance with Regulation 35 of the Local Government Pension Scheme (Administration) Regulations (the LGPS Regulations). The Statement describes Somerset County Council's strategy, in its capacity as Administering Authority (the Administering Authority), for the funding of the Somerset County Council Pension Fund (the Fund).

As required by Regulation 35(3a), the Statement has been prepared having regard to guidance published by CIPFA in March 2004.

Consultation

In accordance with Regulation 35(3b), all employers participating within the Somerset County Council Pension Fund have been consulted on the contents of this Statement and their views have been taken into account in formulating the Statement. However, the Statement describes a single strategy for the Fund as a whole.

In addition, the Administering Authority has had regard to the Fund's Statement of Investment Principles published under Regulation 9A of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (the Investment Regulations).

The Fund Actuary, Barnett Waddingham LLP, has also been consulted on the contents of this Statement.

Policy purpose

The three main purposes of this Funding Strategy Statement are:

- To establish a clear and transparent strategy, specific to the Fund, which will identify how employer's pension liabilities are best met going forward.
- To support the regulatory requirement in relation to the desirability of maintaining as nearly constant employer contribution rates as possible.
- To take a prudent longer-term view of funding the Fund's liabilities.

The aims of the fund

The aims of the Fund are:

1. To enable employer contribution rates to be kept as nearly constant as possible and at reasonable cost to the Scheduled bodies, Admitted bodies and to the taxpayers.

The Administering Authority recognises that the requirement to keep employer contribution rates as nearly constant as possible can run counter to the following requirements:

- the regulatory requirement to secure solvency,
- the requirement that the costs should be reasonable, and
- maximising income from investments within reasonable cost parameters (see 4 below)

Employers' contributions are set every three years following the triennial actuarial valuation. In the long term the key factor influencing levels of employer contributions will be the underlying investment strategy. Investment strategy will also have an impact on levels of employer contributions in the short term. However the funding model adopted to determine levels of employer contribution will also play an important part. The funding model adopted by the Somerset Fund seeks to produce stable levels of employer contributions using both implicit and explicit smoothing mechanisms.

The Administering Authority recognises that there is a balance to be struck between the investment policy adopted, the smoothing mechanisms used at valuations, and the resultant smoothness of employer contribution rates from one valuation period to the next.

The Administering Authority also recognises that the position is potentially more volatile for Admission Bodies with short term contracts where utilisation of smoothing mechanisms may be less appropriate.

2. To ensure that sufficient resources are available to meet all liabilities as they fall due.

The Administering Authority recognises the need to ensure that the Fund has, at all times, sufficient liquid assets to be able to pay pensions, transfer values, costs, charges and other expenses. It is the Administering Authority's policy that such expenditure is met, in the first instance, from incoming employer and employee contributions to avoid the expense of disinvesting assets. The Administering Authority monitors the position on a monthly basis to ensure that all cash requirements can be met.

3. To manage employers' liabilities effectively.

The Administering Authority seeks to ensure that all employers' liabilities are managed effectively. In a funding context, this is achieved by seeking regular actuarial advice, ensuring that employers and Panel members are properly informed, and through regular monitoring of the funding position.

4. **To maximise the income from investments within reasonable risk parameters.**

The Administering Authority recognises the desirability of maximising investment income within reasonable risk parameters. Investment returns higher than those available on government stocks are sought through investment in other asset classes such as stocks and property.

The Administering Authority ensures that risk parameters are reasonable by:

- restricting investment to the levels permitted by the Investment Regulations
- restricting investment to asset classes generally recognised as appropriate for UK pension funds
- analysing the potential risk represented by those asset classes in collaboration with the Fund's Actuary, Investment Advisors and Fund Managers.

Purpose of the fund

The purpose of the Fund is:

- To pay out monies in respect of scheme benefits, transfer values, costs, charges and expenses.
- To receive monies in respect of contributions, transfer values and investment income.
- To appropriately invest monies not immediately required to meet liabilities.

Responsibilities of key parties

The three parties whose responsibilities to the Fund are of particular relevance are the Administering Authority, the Individual Employers and the Scheme Actuary. Their key responsibilities are as follows:

Administering authority

The Administering Authority's key responsibilities are:

1. **Collecting employer and employee contributions and, as far as the Administering Authority is able to, ensure these contributions are paid by the due date.**

   Individual employers must pay contributions in accordance with Regulations 39 through to 42 of the LGPS Regulations. The Administering Authority will ensure that all employers are aware of these requirements especially the requirement of the Pensions Act 1995 that members' contributions are paid by the 19th of the month following the month that it is paid by the member. Employers not meeting these requirements will be subject to reporting requirements of the Pensions Regulator.

   The Administering Authority will ensure that action is taken to recover assets from Admission Bodies whose Admission Agreement has ceased by

   - requesting that the Fund Actuary calculates the funding position at the date of cessation of the Admission Agreement
   - notifying the Admission Body that it must meet any deficit at the cessation of the Agreement .

   In determining the funding position at the date of cessation, the Fund Actuary will make no allowance for future investment returns over and above those available from gilt edged securities unless another employer in the Fund acts as guarantor of the liabilities remaining in the Fund.

2. **Invest surplus monies in accordance with the regulations.**

   The Administering Authority will comply with Regulation 9 of the Investment Regulations.

3. **Ensure that cash is available to meet liabilities as and when they fall due.**

   The Administering Authority recognises this duty and discharges it in the manner set out in the Aims of the Fund above.

4. **Manage the valuation process in consultation with the Fund's actuary.**

   The Administering Authority ensures it communicates effectively with the Fund Actuary to:

   - agree timescales for the provision of information and provision of valuation results
   - ensure provision of data of suitable accuracy
   - ensure that the Fund Actuary is clear about the Funding Strategy
   - ensure that participating employers receive appropriate communication throughout the process
   - ensure that reports are made available as required by Guidance and Regulation

5. Prepare and maintain a Statement of Investment Principles and a Funding Strategy Statement after due consultation with interested parties.

The Administering Authority will ensure that both documents are prepared and maintained in the required manner.

6. Monitor all aspects of the Fund's performance and funding and amend these two documents if required.

The Administering Authority monitors the funding position of the Fund on a quarterly basis, and the investment performance of the Fund on a monthly basis. The Statement of Investment Principles and Funding Strategy Statement will be formally reviewed annually, unless circumstances dictate earlier amendment.

Individual employers

Individual Employers will:

- Deduct contributions from employees' pay;
- Pay all contributions, including their employer contribution as determined by the actuary, promptly by the due date;
- Exercise discretions within the regulatory framework;
- Pay for added years in accordance with agreed arrangements;
- Notify the administering authority promptly of all changes to membership, or other changes which affect future funding.

The fund actuary

The fund actuary will:

1. Prepare valuations including the setting of employers' contribution rates after agreeing assumptions with the administering authority and having regard to the Funding Strategy Statement.

Valuations will also be prepared in accordance with generally accepted actuarial methods and reported on in accordance with Guidance Note 9 issued by the Board of Actuarial Standards, to the extent that the Guidance Note is relevant to the LGPS.

2. Prepare advice and calculations in connection with bulk transfers and individual benefit-related matters.

Such advice will take account of the funding position and Strategy of the Fund, along with other relevant matters.

Solvency

The Administering Authority will prudentially seek to secure the solvency of the Fund. For this purpose the Administering Authority defines solvency as being achieved when the value of the Fund's assets is greater than or equal to the value of the Fund's liabilities when measured using 'ongoing' actuarial methods and assumptions.

'Ongoing' actuarial methods and assumptions are taken to be measurement by use of the projected unit method of valuation, using assumptions generally recognised as suitable for an open, ongoing UK pension fund with a sponsoring employer of sound covenant.

The financial assumptions used to assess the funding level will have regard to the yields available on long term fixed interest and index linked gilt edged investments. The Administering Authority has also agreed with the Fund Actuary that the assumptions will make partial allowance for the higher long term returns that are expected on the assets actually held by the Fund, and understands the risks of such an approach if those additional returns fail to materialise.

Consistent with the aim of enabling employer contribution rates to be kept as nearly constant as possible, and having regard to the risks inherent in such an approach, the Administering Authority has also agreed with the Fund Actuary the use of explicit smoothing adjustments in making the solvency measurement. It is unlikely that use of all of these smoothing adjustments will be extended to employers whose participation in the Fund is for a fixed period (for example, an employer admitted by virtue of having been awarded a best value outsourcing contract).

Funding strategy

Where a valuation reveals that the Fund is in surplus or deficiency against this solvency measure, employer contribution rates will be adjusted to target restoration of the solvent position over a period of years (the recovery period). The recovery period applicable for each participating employer is set by the Administering Authority in consultation with the Fund Actuary and the employer, with a view to balancing the various funding requirements against the risks involved due to such issues as the financial strength of the employer and the nature of its participation in the Fund.

The Administering Authority recognises that a large proportion of the Fund's liabilities are expected to arise as benefit payments over long periods of time. For employers of sound covenant, the Administering Authority is prepared to agree to recovery periods which are longer than the average future working lifetime of the membership of that employer. The Administering Authority recognises that such an approach is consistent with the aim of keeping employer contribution rates as nearly constant as possible. However, the Administering Authority also recognises the risk in relying on long recovery periods and has agreed with the Fund Actuary a limit of 40 years. The Administering Authority's policy is to agree recovery periods with each employer which are as short as possible within this framework.

For employers whose participation in the fund is for a fixed period it is unlikely that the Administering Authority and Fund Actuary would agree to a recovery period longer than the remaining term of participation.

Consistent with the requirement to keep employer contribution rates as nearly constant as possible, the Administering Authority permits some employers to be treated as a group for the purposes of setting contribution rates. In particular, contribution rates could be very volatile for smaller employers due to the increased likelihood that demographic movements would have a material effect. The Administering Authority recognises that grouping can give rise to cross subsidies from one employer to another over time. The Administering Authority's policy is to consider the position carefully at each valuation and to notify each employer that is grouped that this is the case, and which other employers it is grouped with. If the employer objects to this grouping, it will be offered its own contribution rate. For employers with significantly more than 50 contributing members, the Administering Authority would look for evidence of homogeneity between employers before considering grouping. For employers whose participation is for a fixed period grouping is unlikely to be permitted.

Again, consistent with the requirement to keep employer contribution rates as nearly constant as possible, the Administering Authority will consider, at each valuation, whether new contribution rates should be payable immediately, or should be reached by a series of steps over future years. The Administering Authority will discuss with the Fund Actuary the risks inherent in such an approach, and will examine the financial impact and risks associated with each employer. The Administering Authority's policy is that in the normal course of events no more than three equal annual steps will be permitted. Further steps may be permitted in extreme cases, but the total is very unlikely to exceed six steps.

Identification of risks and counter measures

The Administering Authority's overall policy on risk is to identify all risks to the Fund and to consider the position both in aggregate and at an individual risk level. The Administering Authority will monitor the risks to the Fund, and will take appropriate action to limit the impact of these both before, and after, they emerge wherever possible. The main risks to the Fund are:

<u>Demographic</u>

The main risks include changing retirement patterns and longevity. The Administering Authority will ensure that the Fund Actuary investigates these matters at each valuation or, if appropriate, more frequently, and reports on developments. The Administering Authority will agree with the Fund Actuary any changes which are necessary to the assumptions underlying the measure of solvency to allow for observed or anticipated changes.

If significant demographic changes become apparent between valuations, the Administering Authority will notify all participating employers of the anticipated impact on costs that will emerge at the next valuation and will review the bonds that are in place for Transferee Admitted Bodies.

<u>Regulatory</u>

The risks relate to changes to regulations, national pension requirements or HM Revenue and Customs rules. The Administering Authority will keep abreast of all proposed changes and, where possible, express their opinion during consultation periods after careful consideration. The Administering Authority's policy will be to ask the Fund Actuary to assess the impact on costs of any changes and, where these are likely to be significant, the Administering Authority will notify Employers of this likely impact and the timing of any change.

Governance

This covers the risk of unexpected structural changes in the Fund membership (for example the closure of an employer to new entrants or the large scale withdrawal or retirement of groups of staff), and the related risk of the Administering Authority not being made aware of such changes in a timely manner.

The Administering Authority's policy is to require regular communication between itself and employers, and to ensure regular reviews of such items as bond arrangements, financial standing of non-tax raising employers and funding levels.

Statistical and financial

This covers items such as the performances of markets, Fund investment managers, asset reallocation in volatile markets, pay and /or price inflation varying from anticipated levels or the effect of possible increases in employer contribution rate on service delivery and on Fund employers. The Administering Authority's policy will be to regularly assess such aspects to ensure that all assumptions used are still justified.

Solvency measure

The Administering Authority recognises that allowing for future investment returns in excess of those available on government bonds introduces an element of risk, in that those additional returns may not materialise. The Administering Authority's policy will be to monitor the underlying position assuming no such excess returns are achieved to ensure that the funding target remains realistic relative to the low risk position.

Smoothing

The Administering Authority recognises that utilisation of a smoothing techniques in the solvency measurement introduces an element of risk, in that the smoothing techniques may not provide a true market based measure of the solvency position. The Administering Authority's policy is to review the impact of the smoothing techniques at each valuation to ensure that the disclosed solvency position is within an acceptable limit of the underlying market based position.

Recovery period

The Administering Authority recognises that permitting surpluses or deficiencies to be eliminated over a recovery period rather than immediately introduces a risk that action to restore solvency is insufficient between successive measurements. The Administering Authority's policy is to discuss the risks inherent in each situation with the Fund Actuary and to limit the permitted length of recovery period to no longer than 40 years.

Stepping

The Administering Authority recognises that permitting contribution rate changes to be introduced by annual steps rather than immediately introduces a risk that action to restore solvency is insufficient in the early years of the process. The Administering Authority's policy is to discuss the risks inherent in each situation with the Fund Actuary and to limit the number of permitted steps to three annual steps or, in exceptional circumstances, to six annual steps.

Statement of investment principles

The Authority has produced this Funding Strategy Statement having taken an overall view of the level of risk inherent in the investment policy set out in the Statement of Investment Principles and the funding policy set out in this Statement. The Statement of Investment Principles is set out annually in the Fund's Annual Report and Accounts.

The Administering Authority will continue to review both documents to ensure that the overall risk profile remains appropriate including, where appropriate, asset liability modelling or other analysis techniques.

Future monitoring

The Administering Authority plans to formally review this Statement as part of the triennial valuation process unless circumstances arise which require earlier action.

The Administering Authority will monitor the funding position of the Fund on an approximate basis at regular intervals between valuations, and will discuss with the Actuary whether any significant changes have arisen that require action.

Approved by the Pensions Committee
Somerset County Council Pension Fund
May 2008

Statement of investment principles

1 Introduction

a The Local Government Pension Scheme has existed for many years, and is based on primary legislation (The Superannuation Act 1972), and regulations approved as statutory instruments. These regulations can be revised or updated.

b Somerset County Council are the statutory 'administering authority' for the Local Government Pension Scheme in the administrative county of Somerset (the 1974 boundaries). The pension fund provides a benefits package for local-authority employees who are not eligible to be members of other statutory schemes (for example, schemes for teachers, police officers and firefighters).

c There are other public-sector employers in the county whose staff are entitled to belong to the pension fund (for example, further education colleges). Certain other organisations can apply to be included in the pension fund.

d Because it is not a trust-based scheme, there is no group of trustees. In effect, Somerset County Council is 'the trustee'.

e The responsibility for the fund is passed to the pensions committee. The committee is made up of:

- four Somerset County Council members;
- a district councillor representing the five district councils;
- a representative of Avon and Somerset Police Authority;
- a representative of all other participating employers;
- a members representative;

In addition to the eight committee members an independent advisor and officers of the County Council will attend all meetings. All of the committee members may vote at meetings.

The Section 151 Officer is responsible for putting the committee's decisions into practice, and for the day-to-day management of the pension fund.

f As well as this statement, the committee maintains a range of specific policies and strategies, including:

- a governance policy statement;
- a communication policy statement;
- a funding strategy statement; and
- a forward-looking committee business plan.

g The committee has adopted this statement of investment principles.

2 Pensions committee responsibilities

a The terms of reference for the committee, which form part of the governance policy for the fund, say the committee's main responsibilities are to:

- Ensure the fund is run in line with all relevant law, statutory guidance and industry codes of best practice.
- Ensure all contributions due are collected from employers.
- Ensure that all benefits due are paid correctly and in a timely manner.
- Decide the aims of the investment policy.
- Make arrangements for managing the fund's investments.
- Regularly monitor investment performance.
- Make arrangements to publish the fund's annual report and accounts.
- Consult stakeholders, and publish the funding strategy statement, statement of investment principles and other policies and documents as necessary.
- Order actuarial valuations to be carried out in line with the Local Government Pension Scheme Regulations.
- Consider requests from organisations who want to join the fund as admitted bodies and consider any requests to change the terms of an existing admission agreement.
- Make representations to the Government about any planned changes to the Local Government Pension Scheme and all aspects of managing benefits.

b The committee meets at least quarterly to consider investment strategies and the performance of its managers. At these meetings, it takes advice from its officers, managers and independent advisors as necessary.

3 Investment policy

3.1 Overview

a In line with the fund's funding strategy statement, the committee has set an objective of the fund being at or above a 100% funding level, as calculated by the fund's actuary at the triennial valuation, so that it can meet its current and future liabilities. As the scheme provides for the actuary to value assets and liabilities regularly and to adjust the employers' contributions, our aim is to make sure that investment returns are as high as possible for a given acceptable level of risk so the cost to the employers is reduced as far as possible.

b Under the Local Government Pension Scheme Investment Regulations (the regulations), we must invest any income we have left after paying out pensions. The pension fund's income comes from contributions by employers and employees, together with interest and dividends on investments.

c The regulations have developed over the years and provide a legal framework within which the fund's money is managed. We keep to the limits on the maximum investment that can be made in various types of approved investment, as set out in the regulations and changed from time to time.

3.2 The type of investments to be held

a For the investment of pension fund money, we take account of:

- investments permitted by LGPS regulations;
- the need to spread funds over a wide range of investments;
- how suitable investments are; and
- proper advice, received at reasonable intervals.

b The fund may invest in the following types of asset:

- listed stocks and shares;
- government and corporate bonds;
- futures, forward currency contracts and options;
- cash deposits with suitable banks and building societies;
- to enter into stock-lending arrangements;
- to invest in unlisted collective investment schemes such as unit trusts and open-ended investment companies (OEICs);
- to invest in limited liability partnerships (LLPs) ; and
- to invest in unlisted shares.

c A management agreement is put in place with each external fund manager which clearly states the type of investments they are allowed to make for the fund, asset allocation ranges and any further restrictions we believe are necessary.

3.3 The balance between different types of investment

a The fund will at all times hold a widely diversified portfolio of investments to reduce risk. Investments are spread over a range of asset classes (bonds, equities, property, cash and so on) and a number of different investment managers with varying investment styles.

b The committee will regularly review the balance between different types of investment to make sure that it continues to meet the needs of the fund.

3.4 Risk

a Investment by its very nature is a risk business and the returns achieved will to a considerable extent reflect the risks taken.

b Investment risk includes the absolute risk of reduction in the value of assets through negative returns. It cannot be entirely avoided (for instance if all major investment markets were to decline in unison) but it can be managed by making sure that the investments of the fund are invested across a number of different assets and markets. This is widely recognised as being an effective way of minimising the risk of reductions in the value of the fund's assets.

c Different types of investment have different risk characteristics and return potential. Historically the returns from equities have been higher than from bonds but they are more volatile and risky. In setting the investment strategy the fund looks at the expected risks and returns from various asset classes and the correlation between these returns to target an expected return within an acceptable level of risk.

d Investment risk also includes the risk of under-performing the fund's benchmark. This is called relative risk. The adoption of a benchmark and the explicit monitoring of performance relative to that benchmark and a performance target, constrains the fund managers from deviating significantly from the intended approach, while permitting flexibility to manage the portfolio they have been given in such a way as to enhance returns.

e The appointment of more than one fund manager introduces a meaningful level of diversification of manager risk. Although each fund manager typically only invests in a single asset class, they are expected to maintain a diversified portfolio of investments for their individual benchmarks.

f The Committee does not impose specific portfolio risk limits on its investment managers, as it believes the out performance target set for each manager provides sufficient guidance as to the level of risk that each manager should be taking.

g Continuous dialogue with, and monitoring of, fund managers by the fund aids the management of investment risk for each fund manager's portfolio and for the fund as a whole.

h The most fundamental risk is that the fund's assets produce worse returns than those assumed by the Actuary, who values the assets and liabilities every three years, and that the solvency of the fund deteriorates.

3.5 The expected return on investments

a Investment performance is measured independently from the managers of the funds. This measurement is compared with specific relevant indexes every three months.

b Each manager has a specific target to outperform their relevant index. The targets are over a three-year period.

c If a manager fails to achieve benchmark performance in four three-month periods in a row, or in six three-month periods in any eight three-month periods in a row, a formal review will take place on their strategy and choice of stocks.

d The committee has a performance target for the fund of beating its own benchmark every year. The benchmark is set by the committee and revised from time to time. The current benchmark was formally agreed in February 2009 and introduced on 1 April 2009.

e Longer-term performance is measured against the assumptions made by the actuary as part of the three-yearly actuarial valuation process.

3.6 Security of investments

a To make investments as secure as they can be, where possible, external investments are maintained under the control of a safe custodian.

b Most of the investments are quoted on major stock markets and may be sold quickly if necessary. The committee consider the cash-flow needs of the fund as a whole, how easily investments can be sold and the effect on the whole fund of holding investments that cannot be sold quickly when judging the suitability of new investment classes. No more than 20% of the total investments will be put into assets that we consider could not be sold quickly.

c Only cash holdings and a small number of unit trusts stay under the control of the Chief Finance Officer.

d Stock certificates and cash holdings are never under the control of an external manager.

3.7 Social, environmental and ethically responsible investment

a The pensions committee have considered the implications of investing on a defined ethical basis. Evidence on performance and the spread of investment has led the committee to decide not to allocate funds on a specific ethical basis. Performance of ethical investments will be reviewed regularly.

b The most effective way of understanding and influencing the social, environmental and ethical policies of those companies is by reasonable discussion with the companies it invests in, through a third party, while at the same time achieving financial returns that are compatible with the fund's longer-term financial objectives.

c The corporate performance of companies and their value as investments are increasingly affected by social, environmental and ethical factors. To help companies to invest carefully and responsibly, the committee will encourage and support companies that have a positive response to social, environmental and ethical concerns. The committee expects companies to do the following.

- Make a commitment to achieving recognised social, environmental and ethical best practice.
- Regularly monitor their policies and practices.
- Set up procedures which will lead to gradual improvements in performance.
- Follow all current environmental and other relevant legislation and work to anticipate future changes to legislation.
- Make available to shareholders regular and detailed reports of progress made towards maintaining and, where necessary, improving standards.
- Work to take all reasonable and practical steps to reduce or get rid of damage to the environment.
- Work to take all reasonable and practical steps to reduce or eliminate the company's impact on climate change.
- Make available to shareholders information about the company's environmental and climate change impact so they can properly assess the risks to shareholders.
- Actively and openly discuss the social, environmental and ethical effects of their business.

3.8 Corporate governance

a Holding shares in public limited companies gives the fund the right to vote at company meetings. We have accepted this, and vote in line with a policy agreed by the committee.

b The policy adopted is:

- to give external managers the power to vote on our behalf in line with their own process within industry standards and the principles of this statement;
- for the in-house managed funds, to receive the Voting Issues Service of the Pension Investment Research Consultants (PIRC) and follow their recommendations in voting on all resolutions where practically possible; and
- to consider individual voting issues as they arise.

c The committee recognises its responsibility as an institutional investor to support and encourage good corporate-governance practices in the companies it invests in. The committee considers that good corporate governance can contribute to business health and success by encouraging boards, shareholders and other stakeholders to answer to each other. Good corporate governance also plays an important part in encouraging corporate responsibility to shareholders, employees and wider society.

d To achieve this responsibility, the committee uses its voting rights attached to investments to support its corporate-governance policies. The committee's voting rights are an asset and will be used to further the long-term interests of the fund's beneficiaries. As a general principle, votes will be used to:

- protect shareholder rights;
- reduce, as far as possible, risk to companies from corporate governance failing;
- improve long-term value; and
- encourage corporate social responsibility.

e The fund is also a member of the Local Authority Pension Fund Forum. This forum promotes the investment interests of local-authority pension funds, and makes the most of their influence as shareholders to promote corporate social responsibility and high standards of corporate governance among the companies they invest in.

f The fund is also a signatory to the Financial Reporting Council (FRC) Stewardship Code.

3.9 Stock lending

a The fund has a stock lending program within the limits allowed by the LGPS regulations.

b The fund derives a useful source of relative low risk return from stock lending.

4 Accounts and audit

a The investments of the pension fund are audited by both the internal and external auditors.

b As soon as possible after the end of the financial year and after the external audit of the pension fund has been finished, we send each organisation an annual report which includes:

- the revenue account and balance sheet of the pension fund; and
- any report by the auditor.

c We hold a meeting each year, and invite representatives of employers and employees to take part. We formally present the annual report, and those present may question the committee, officers, its managers and its advisors.

5 Working in line with Myners

a In 2000, the UK Government ordered a review of institutional investment in the UK. The review was carried out by Paul Myners, the chairman of a large fund-management group, and his findings were published in March 2001.

Myners sets out a number of principles of best practice and recommends that pension funds should set out what they are doing to apply these principles. In response to Myners' proposals, the Government issued a set of 10 investment principles in October 2001 that it said it would be taking forward. In November 2008, the Government published a revised set of principles, following on from this CIPFA had produced a set of Myner's principles specifically for Local Government Pension Schemes and guidance on how to compare compliance with the principles. The fund's performance against the CIPFA principles and guidance is set out below.

b Principle 1: Effective Decision Making

Administering authority should ensure that:

- **decisions are taken by people or organisations with the skills, knowledge, advice and resources necessary to make them effectively and monitor their implementations; and**
- **those persons or organisations have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.**

The fund is fully compliant with this principle but must continue to work to ensure that the knowledge base of officers and committee members remains comprehensive and current.

c Principle 2: Clear Objectives

An overall investment objective(s) should be set out for the fund that takes account of the scheme's liabilities, the potential impact on local tax payers, the strength of the covenant for non-local authority employers, and the attitude to risk of both the administering authority and scheme employers, and these should be communicated to advisors and investment managers.

The fund is fully compliant with this principle. The fund will look to make additional progress by further consideration of the needs of the disparate employers within the fund and how their differing needs are reflected in the objectives of the fund as a whole.

d Principle 3: Risk and Liabilities

In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of the liabilities.

These include the implications for local tax payers, the strength of the covenant for participating employers, the risk of their default and longevity risk.

The fund is fully compliant with this principle.

e Principle 4: Performance Assessment

Arrangements should be in place for the formal measurement of performance of the investments, investment managers and advisors.

Administering authorities should also periodically make a formal assessment of their own effectiveness as a decision making body and report on this to scheme members.

The fund is fully compliant with this principle with respect of measurement of investment performance and investment managers. The fund needs to consider more formal arrangements for the measurement of performance of other advisors and particularly formal assessment of the pensions committee's performance.

f Principle 5: Responsible Ownership

Administering authorities should:

- **adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee Statement of Principles on the responsibilities of shareholder and agents**
- **include a statement of their policy on responsible ownership in the statement of investment principles**
- **report periodically to scheme members on the discharge of such responsibilities.**

The fund is fully compliant with this principle.

g	Principle 6: Transparency and Reporting

Administering authorities should:

- **act in a transparent manner, communicated with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives**
- **provide regular communication to scheme members in the form they consider most appropriate.**

The fund is fully compliant with this principle.

6.0 Arrangements for reviewing this statement

6.1 This Statement of Investment Principles will be regularly reviewed by the pensions committee, particularly to ensure it continues to meet all regulatory and statutory requirements and that the level of compliance with the Myner's principles reflects the current status of the fund. Where there is significant change to the Statement the pensions committee will consult relevant stakeholders prior to amending the policy.

Approved by the Pensions Committee
Somerset County Council Pension Fund
September 2011

Financial Reporting Council Stewardship Code Statement

Principle 1 – Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.

The Somerset County Council Pension Fund takes its responsibilities as a shareholder seriously. It seeks to adhere to the Stewardship Code, and encourages its appointed asset managers to do so too. Stewardship is seen as part of the responsibilities of share ownership, and therefore an integral part of the investment strategy.

In practice the fund's policy is to apply the Code both through its arrangements with its asset managers, it's specialist voting advisor and through membership of the Local Authority Pension Fund Forum.

Principle 2 - Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.

The fund encourages the asset managers it employs to have effective policies addressing potential conflicts of interest. With respect to those equity managers whose own shares fall within the scope of their mandate each has an explicit policy not to invest in their own company's, or eventual parent's, shares.

In respect of conflicts of interest within the fund, pension committee members are required to make declarations of interest prior to committee meetings and a related parties disclosure is made annually in the fund's annual report.

Principle 3 - Institutional investors should monitor their investee companies.

Day-to-day responsibility for managing our equity holdings is delegated to our appointed asset managers, and the fund expects them to monitor companies, intervene where necessary, and report back regularly on activity undertaken. For the in-house managed fund we would expect PIRC, as our specialist voting advisor to monitor companies and engage with them prior to advising us on voting. Reports from our asset managers on voting and engagement activity are received by the fund on a quarterly basis and are augmented by quarterly meetings with officers and regular discussions.

In addition the fund receives an 'Alerts' service from Local Authority Pension Fund Forum which highlights corporate governance issues of concern at investee companies.

Principle 4 - Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.

As highlighted above, responsibility for day-to-day interaction with companies is delegated to the fund's asset managers and PIRC, including the escalation of engagement when necessary. Their guidelines for such activities are expected to be disclosed in their own statement of adherence to the Stewardship Code.

However on occasion, the fund may itself choose to escalate activity, principally through engagement activity through the Local Authority Pension Fund Forum.

Principle 5 - Institutional investors should be willing to act collectively with other investors where appropriate.

The fund seeks to work collaboratively with other institutional shareholders in order to maximise the influence that it can have on individual companies. The fund seeks to achieve this through membership of the Local Authority Pension Fund Forum, which engages with companies over environmental, social and governance issues on behalf of its members.

Principle 6 - Institutional investors should have a clear policy on voting and disclosure of voting activity.

In respect of shareholder voting, the fund exercises all votes attaching to its UK equity holdings, and seeks to vote where practical in overseas markets. Responsibility for the exercise of voting rights has been delegated to the fund's appointed asset managers and is undertaken by officers for the in-house managed fund following voting advice from PIRC. This includes consideration of company explanations of compliance with the Corporate Governance Code. Regular reports are received from the asset managers on how votes have been cast, and controversial issues are often discussed with fund managers as they arise.

The fund discloses a summary of voting activity of each of the segregated equity funds twice a year as a committee paper, all of the committee papers are published on the County Council's website. The fund is minded to disclose in full voting activity at a given company meeting on request. A number of our asset managers and PIRC publish their voting activity (advice).

Principle 7 - Institutional investors should report periodically on their stewardship and voting activities.

As noted above under principle 6 fund reports semi-annually on voting and stewardship activity through a report to the Pensions Committee. This includes both fund-specific information and an overview of activity undertaken through the Local Authority Pension Fund Forum.

Approved by the Pensions Committee
Somerset County Council Pension Fund
November 2010

Governance policy statement

Introduction

Under the Local Government Pension Scheme (Amendment) (number 2) Regulations 2005 [SI 2005/3199], each administering authority in England and Wales must prepare, maintain and publish a governance policy setting out whether they are going to delegate their function or part of their function in relation to maintaining the pension fund to a committee, a subcommittee or an officer.

Somerset County Council is the administering authority for the Somerset County Council Pension Fund (the fund).

The fund's governance arrangements have also been produced in line with guidance and best practice from the Chartered Institute of Public Finance and Accountancy (CIPFA).

Responsibility for the fund

The County Council has delegated its responsibility for managing the Somerset County Council Pension Fund to a specific committee known as the Somerset County Council Pensions Committee.

Membership of the pensions committee

The membership of the pensions committee allows for wider representation from all stakeholders, while keeping overall numbers to a manageable number to recognise the significant commitment, specialist knowledge and training that needs to be developed by committee members.

The approved arrangements for the make up of the pensions committee are:

- four county council elected members;
- one district councillor representing the five district councils;
- one representative for Avon and Somerset Police Authority;
- one representative of the admitted bodies and remaining smaller scheduled bodies; and
- a nominated member representative.

The committee will also be attended by:

- an officer; and
- a specialist adviser.

The total number of members on the committee will be 8.

All committee members have full voting rights.

Terms of reference

These terms of reference provide the main responsibilities for the pensions committee on how they will take on the functions of Somerset County Council in its role as administering authority of the fund.

Main responsibilities:

- Ensure the fund is run in line with all relevant law, statutory guidance and industry codes of best practice.
- Ensure all contributions due are collected from employers.
- Ensure that all benefits due are paid correctly and in a timely manner.
- Decide the aims of the investment policy.
- Make arrangements for managing the fund’s investments.
- Regularly monitor investment performance.
- Make arrangements to publish the fund’s annual report and accounts.
- Consult stakeholders, and publish the funding strategy statement, statement of investment principles and other policies and documents as necessary.
- Order actuarial valuations to be carried out in line with the Local Government Pension Scheme Regulations.
- Consider requests from organisations who want to join the fund as admitted bodies and consider any requests to change the terms of an existing admission agreement.
- Make representations to the Government about any planned changes to the Local Government Pension Scheme and all aspects of managing benefits.

In line with the Myners’ Investment Principles, members must consider their training and development needs. They should make sure they have enough resources in place to undertake their responsibilities and have developed a forward-looking business plan.

Meetings of the pensions committee

The pensions committee will normally meet formally every March, June, September and December. These meetings will be open to members of the public.

There will also be an annual general meeting, normally in September each year, for all employers whose employees are members of the fund.

Pensions committee members will also receive a range of specific training and development to help them fulfil their role effectively.

Supporting governance policies and statements

There is a range of policies and statements, which are also maintained to support effective governance arrangements for the fund as set out below.

- Statement of investment principles
- Funding strategy statement
- Communication policy
- Annual report and accounts
- Actuarial valuation
- Forward business plan

Arrangements for reviewing this policy

This policy statement will be regularly reviewed by the pensions committee. If it is necessary to make any significant changes, we will consult all of the employers whose employees are members of the fund.

Approved by the Pensions Committee
Somerset County Council Pension Fund
September 2011

Governance Compliance Statement

Introduction

Under Regulation 31 of the Local Government Pension Scheme (Administration) Regulations 2008 (as amended) an Administering Authority must, after consultation with such persons as it considers appropriate, prepare, publish and maintain a Governance Compliance Statement.

This statement is required to set out:

(a) whether the Administering Authority delegates its function or part of its function in relation to maintaining a pension fund to a committee, a sub-committee or an officer of the administering authority;

(b) if it does:-

1 the terms of reference, structure and operational procedures of the delegation;

2 the frequency of any committee or sub-committee meetings; and

3 whether the committee or sub-committee includes representatives of employing authorities (including non-Scheme employers) or members, and if so, whether those representatives have voting rights;

(c) the extent to which a delegation, or absence of delegation, complies with guidance given by the Secretary of State and, if it does not comply, the reason for not complying.

The statement must be revised and published by the Administering Authority following a material change in their policy on any of the matters referred to above.

Approved by the Pensions Committee
Somerset County Council Pension Fund
September 2011

Governance Compliance Statement

Statutory Guidance Governance Standards and Principles	Our compliance status	Evidence of compliance and justification for non-compliance
A – Structure		
a) The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing council.	**Compliant**	Somerset County Council has established the Somerset County Council Pensions Committee for this purpose. The specific terms of reference for the Committee are set within the fund's Governance Policy Statement.
b) 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.	**Compliant**	The Pensions Committee includes representation of all the participating employers. Scheme Members (active, pensioner and deferred) are represented through a Unison nominated representative on the Pensions Committee.
c) That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	**Not Applicable**	There are no secondary committees or panels in place.
d) That where a secondary committee or panel has been established, at least one seat on the main committee is allocated for a member from the secondary committee or panel.	**Not Applicable**	There are no secondary committees or panels in place.

B – Representation		
a) That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include:		
i) employing authorities (including non-scheme employers, e.g., admitted bodies);	**Compliant**	The Pensions Committee includes representation of all the scheme employers, including the County Council, District Councils, the Police Authority and the Admitted Bodies.
ii) scheme members (including deferred and pensioner scheme members);	**Compliant**	Scheme Members (active, pensioner and deferred) are represented through a Unison nominated representative on the Pensions Committee.
iii) where appropriate, independent professional observers;	**Compliant**	The independent investment advisor attends all Pensions Committee Meetings.
iv) expert advisors (on an ad-hoc basis).	**Compliant**	Our in-house officer expert advisors attend all Pension Committee meetings, including the Chief Financial Officer, investments manager and fund administration manager. The appointed actuary, external auditors and performance advisors also attend on an ad-hoc basis at least once per annum.

b) 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.	**Compliant**	All members of the Pensions Committee receive equal access to the papers and training and have equal speaking rights in the consideration and discussion of all matters as part of the decision making processes.
C – Role of members		
a) That Committee or panel members are made fully aware of the status, role and function they are required to perform on either a main or secondary committee.	**Compliant**	All new members receive regular specific training and access to external training and seminars. On appointment this includes specific time with lead officers to provide an induction into the role and a background to the Fund. Copies of relevant Committee Reports and Annual Reports are also made available. A specific Terms of Reference is also in place for the Pensions Committee (copy at Annex 1) and specific legal guidance as to the role of Members has been provided to the Committee by the County Council Monitoring Officer. All Committee Members also understand that they are not there to represent or promote their own personal or political interests, and that they must declare any self-interest or conflicts of interest of a financial or non-financial nature and abstain from participation in that item on the agenda if appropriate.

b) 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.	**Compliant**	Since the inauguration of the Pension Committee the declaration of interests by members has been a standing item on the agenda.
D – Voting		
a) 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.	**Compliant**	All members of the Pensions Committee have full voting rights.
E – Training, facility time and expenses		
a) 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.	**Compliant**	A formal training policy for members has been adopted by the Pensions Committee. The Committee forward work plan provides for specifically tailored training days, together with access to, and support for, external training provision and attendance at appropriate seminars. All members are encouraged to undertake regular training including attendance at the specific training days. All costs in relation to training, including expenses are met from, and reimbursed by, the Pension Fund as appropriate.

b) 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.	**Compliant**	All Pensions Committee members have equal access and rights to training and related support.
c) That the administering authority considers the adoption of annual training plans for committee members and maintains a log of all such training undertaken	**Compliant**	A training policy has been adopted by the Pensions Committee under which attendance at Committee meetings and training undertaken will be reported annually.
F – Meetings (frequency/quorum)		
a) That an administering authority's main committee or committees meet at least quarterly.	**Compliant**	The Pensions Committee meets on a quarterly basis and forward dates have been agreed for at least twelve months in advance. A forward meeting plan is also in place
b) That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committee sits.	**Not Applicable**	There are no secondary committees or panels in place.
c) That an administering authorities who does not include lay members in their formal governance arrangements, provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	**Compliant**	The Pensions Committee does include lay members and this allows for the representation of all key stakeholders.

G – Access		
a) 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.	**Compliant**	All members of the Pensions Committee receive the same agenda and papers containing advice for each meeting. All our Pensions Committee members can ask questions of our professional advisors who attend the Pensions Committee meetings.
H – Scope		
a) That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements	**Compliant**	Each meeting of the Pensions Committee receives a report on the performance of our pension fund, progress against the Forward Business Plan and key issues in respect of benefits administration. The Committee also receives regular reports and updates on approved policies including the communications policy statements. There are also annual reports from the appointed actuary, external auditor and performance advisors.

I – Publicity		
a) 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 an interest in wanting to be part of those arrangements.	**Compliant**	The Governance Arrangements of the Pensions Committee are formally reviewed every four years as part of the Forward Business Plan. There are procedures in place for the re-appointment of individuals to the Pensions Committee at least every four years. All of the policies adopted by the Pensions Committee on behalf of the administering authority including the Statement of Investment Principles, Funding Strategy Statement, Governance Policy Statement and Communications Policy Statement are published annually in the Fund's annual report and financial statement and are available on the County Council's website. All of the policies and the annual report are available in hard or electronic copy on request.

Pensions Committee Scheme of Delegation

Introduction

In order to meet its obligations from time to time the Pensions Committee will find it necessary to delegate certain functions to officers. This document provides a clear framework around standard operating functions as to what decisions and operations have been delegated to officers and what has been retained by the Committee.

This scheme of delegation will refer in turn to each of the main responsibilities of the Committee as laid out in the Committee's terms of reference, which form part of the fund's Governance Policy Statement.

<u>Ensure the fund is run in line with all relevant law, statutory guidance and industry codes of best practice.</u>

The Chief Financial Officer is responsible for ensuring the legal operation of the fund and will bring matters of significance to the attention of the Committee.

<u>Ensure all contributions due are collected from employers.</u>

The Chief Financial officer will maintain procedures to ensure relevant employers pay contributions and that these contributions meet the requirements set by the fund's actuary.

<u>Ensure that all benefits due are paid correctly and in a timely manner.</u>

The Chief Financial officer will maintain procedures to ensure the correct calculation and payment of benefits by the fund

<u>Decide the aims of the investment policy.</u>

Committee agree the aims of the investment policy and publish this in the form of the funding strategy statement and statement of investment principles.

Make arrangements for managing the fund's investments.

The Committee will decide the fund's asset allocation both in terms of asset classes and investment mandates that will be managed either internally or by external fund managers.

The Committee will decide the fund's voting, engagement and socially responsible investment policies. The Chief Financial Officer will make arrangements for the implementation, monitoring and any necessary reporting against the agreed policies.

The Committee will advise the Chief Financial Officer of their preferences when appointing external fund managers, under County Council contract standing orders all contracts must be awarded and managed by officers. The Committee will advise the Chief Financial Officer if they wish a fund manager's contract to be terminated.

The Chief Financial Officer is responsible for the appointment of a global custodian for the fund and the management of this contract.

Where the Committee decide that assets will be managed in-house the Chief Financial Officer will make suitable arrangements for these assets in accordance with any guidelines provided by Committee.

The strategic asset allocation of the fund is set by the Committee. Once agreed by Committee the Chief Financial Officer is responsible for the monitoring of the investment assets against the strategic asset allocation and periodically rebalancing of the fund to optimise the balancing of risk and return. The Chief Financial Officer will report on all actions in this regard to the Committee at each formal meeting.

The Chief Financial Officer is responsible for the day to day monitoring and recording of the investment assets.

Regularly monitor investment performance.

The Committee will review the performance of all fund managers quarterly and receive an annual presentation from the external performance measurement provider. The Committee will meet with external fund managers periodically to discuss performance.

The Chief Financial Officer will review the performance of all fund managers monthly and officers will meet with external fund managers quarterly to discuss performance.

Make arrangements to publish the fund's annual report and accounts.

The Chief Financial Officer will make arrangements for the production and audit of the fund's annual report and accounts. The Committee will receive the external auditor's report annually.

Consult stakeholders, and publish the funding strategy statement, statement of investment principles and other policies and documents as necessary.

The Chief Financial Officer will make arrangements for the drafting of all policies and statements and undertake consultations as applicable. The Committee will be responsible for approving all policies and statements after receiving feedback from any consultations undertaken.

Order actuarial valuations to be carried out in line with the Local Government Pension Scheme Regulations.

The Chief Financial Officer will appoint a suitable actuary for the fund in consultation with the Committee and instigate the valuation process. The Committee will receive the actuary's draft valuation report and approve it. The Committee will meet with the actuary at least annually to receive an update.

Consider requests from organisations who want to join the fund as admitted bodies and consider any requests to change the terms of an existing admission agreement.

The Committee will approve or reject all requests from organisations who wish to join the fund as admitted bodies and any requests to alter the terms of an existing admission agreement.

Make representations to the Government about any planned changes to the Local Government Pension Scheme and all aspects of managing benefits.

The Committee will instruct the Chief Financial Officer on what it wishes to be included in any representations, which he will then draft and send accordingly.

Approved by the Pensions Committee
Somerset County Council Pension Fund
September 2011

Pensions Committee Training Policy

Introduction

The 2004 Pensions Act requires that trustees of occupational pension schemes should be trained and have knowledge and understanding of the law relating to pensions and role of trustees, the principles of scheme funding and investment, and the management and administration of pension scheme benefits. Members of the Pensions Committee are not legally trustees and are not bound by this law, however they should aspire to reach a similar standard.

Within the Local Government Pension Scheme (LGPS) the statutorily required Governance Compliance Statement requires the fund to compare its practice to the following statement:

“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.”

Pension Committee members will be expected to undertake regular training to ensure they have sufficient knowledge of the LGPS, pension benefits and investment issues to make informed decisions for the benefit of all stakeholders.

CIPFA Knowledge and Skills Framework

The Chartered Institute of Public Finance and Accountancy (CIPFA) in 2010 published a Pensions Finance Knowledge and Skills Framework and accompanying guidance for elected representatives, non-executives and officers.

The fund has formally adopted the framework, will assess all relevant individuals against the suggested standards of knowledge and ensure relevant training is made available.

An assessment of competence against the framework and training undertaken by relevant individuals will be provided in the fund’s annual report as required by the framework.

Annual Training Commitment

Pension Committee members are encouraged to undertake training within the following guidelines:

Level 1 - New Pensions Committee members 1st year of office

New members should have 1-3 days training via:

- Receiving1/2 day in-house induction training on the LGPS and its benefits, the membership and role of the Committee and the current investment structure of the fund.
- Reading the Pension Committee Members Handbook containing key documents such as the Fund Members guide, the Fund Annual Report and Financial Statement and background reading and knowledge building for 1/2 day.
- Attending at least one days external training on relevant topics.
- Attending the annual employers communications meeting.

Level 2 – Members 2nd and 3rd year of office

Should undergo 1 or 2 days a year personal training to build their knowledge and skills in specific topics in greater depth such as:

- Investing in specific asset classes
- Fund manager performance measurement
- SRI, corporate governance, and activism
- Actuarial valuation
- Fund accounting and taxation
- Third party pensions administration

Level 3 - Member serving longer than 3 years

Should seek to have at least 2 days a year of "updating and refreshment" personal training and/or more advanced training in specialist topics, on either fund investment or pensions administration.

The training undertaken by each member of the committee in each financial year will be reported annually in the fund’s annual report and financial statement along with their attendance record at Committee Meetings.

Suitable Events

It is anticipated that at least 1 days annual training will be arranged and provided by officers to address specific training requirements to meet the Committee’s forward business plan, all members will be encouraged to attend this event.

A number of specialist courses are run by bodies such as the Local Government Employers and existing fund manager partners, officers can provide details of these courses.

There are a number of suitable conferences run annually, officers will inform members of these conferences as details become available. Of particular relevance are the National Association of Pension Funds (NAPF) Local Authority Conference, usually held in May, the LGC Local Authority Conference, usually held in September, and the Local Authority Pension Fund Forum (LAPFF) annual conference, usually held in December.

All direct costs and associated reasonable expenses for attendance of external courses and conferences will be met by the fund.

Approved by the Pensions Committee
Somerset County Council Pension Fund
June 2010

Communication policy statement

Introduction

Under the Local Government Pension Scheme (Amendment) (number 2) Regulations 2005 [SI 2005/3199], each administering authority in England and Wales must prepare, maintain and publish a statement by no later than 1 April 2006, setting out their policy on communicating with members, members' representatives, future members and employers whose employees are members in the fund.

This document represents the communication policy based on good custom and practice that has developed over many years. This policy will be continually reviewed to make sure it provides for effective and efficient communication with the range of stakeholders in the Somerset County Council Pension Fund.

Scheme members

The fund will communicate with scheme members in the following ways.

- The fund will send new members appropriate scheme literature within 15 days of receiving confirmation that a new employee is eligible for the scheme. The fund will issue a formal statutory notice of scheme membership within 20 days of receiving filled-in entry forms or confirmation of the transfer of pension rights.

- The fund will issue annual benefit statements confirming the current value of benefits and estimated retirement benefits to all current scheme members and deferred members.

- The fund will send newsletters to current scheme members and pensioners once a year.

- The fund will send pensioners advice slips every month.

- The fund will arrange pre-retirement seminars for members approaching retirement.

- The fund will arrange pensions presentations for groups of members, and will consider regular ‘roadshows’ for the future.

It is also important to recognise that not all individuals who are eligible to join the scheme will be aware of the benefits of being a member. The fund will contact people who are non-members to remind them of the benefits and the process for joining the scheme.

Scheme employers

The employers whose employees are members of the Somerset County Council Pension Fund are key stakeholders. The fund needs to communicate with them effectively so we can build the partnerships needed to manage the scheme efficiently and effectively.

Communication provided will include:

- an annual general meeting to give an update on the investment and administration of the fund, together with key developments affecting the LGPS (this will include details of the current actuarial position of the fund);

- a meeting every year for employers about administration;

- site visits to larger employers every year, and to others when requested;

- formal consultation on regulatory issues with employers; and

- training seminars for employers.

Elected members

This includes communicating with the members of the pensions committee and the county council as administering authority.

- The pensions committee meeting is made up of elected members from both the county council and employing authorities. These meetings are open to all stakeholders and members of the public.

- The fund will provide specific technical training sessions.

- We will report to the County Council every year.

Miscellaneous

The fund will communicate with a range of stakeholders in the following ways.

- The fund will issue an annual report and accounts to employing authorities, elected members and other interested stakeholders.

- The fund will review and maintain a funding strategy statement after consulting employing authorities.

- The fund will review and maintain the statement of investments principles after consulting employing authorities.

- The fund will develop a website providing up-to-date scheme information with help from the Local Government Pensions Committee.

Arrangements for reviewing this policy

This policy statement will be regularly reviewed by the pensions committee. If we need to make any significant changes, we will consult all employers whose employees are members of the fund and publish the amended policy.

Approved by the Pensions Committee
Somerset County Council Pension Fund
July 2009

Director of Finance and Performance's report

Investment activity

During the 2011-2012 financial year, the planned-asset allocation of the fund was changed with effect from 1st January 2012. The change was to increase the planned proportion of the fund invested in emerging market equity from 3% of the total fund to 5%, this was achieved by lowering the proportion invested in the in-house global equity fund from 25% to 23%. We have continued to gradually build up the private equity investment, which has risen from 0.4% to 0.5% of the fund as we move to ultimately having 3% of the fund invested in private equity.

During the year J.P. Morgan Asset Management were removed from the US equity fund and it was decided that this would be managed on a passive basis in-house. The effect of this change on the underlying assets was relatively small.

Finally it was decided that the fund would cease all currency management through Record Currency Management. With effect from December 2011 the passive currency fund was put into run-off and the active fund was moved from suspended to closed.

Investment market background

Interest rates

With the economy being slow to recover and then ultimately moving back into recession during the financial year as the European crisis evolved, the Bank of England kept UK interest rates at 0.5% for the third full year. The Bank also added considerably to the unconventional method of trying to lower interest rates in the real economy by purchasing a further £125bn of UK gilts under the quantitative easing program.

Investment returns

Returns for the year were positive if a little subdued taking the whole fund over the whole year. This masked periods of very strong and very weak performance and a wide variety of returns from different assets. Performance was strongly negative in the quarter to September and then recovered all of the loss and then a little over the second half of the financial year. Returns from bonds were in double figures and better than equities, returns within equities varied considerably from good returns in North America to sizeable losses in Europe and emerging markets.

Key market indicators

	Start of year	End of year	Percentage change for the year
Base rate	0.50%	0.50%	
Strength of sterling			
against US dollars	1.60	1.60	0%
euro	1.13	1.20	6%
yen	133.24	132.64	0%
Stock markets (quoted in local currency)			
FTSE 100 (UK)	5,909	5,768	-2%
FTSE All Share (UK)	3,068	3,003	-2%
Dow Jones (USA)	12,320	13,212	7%
S&P 500 (USA)	1,326	1,408	6%
FTSE Eurofirst 300 ex UK (Europe)	1,264	1,154	-9%
Nikkei 225 (Japan)	9,755	10,084	3%
MSCI Emerging Market	1,171	1,041	-11%

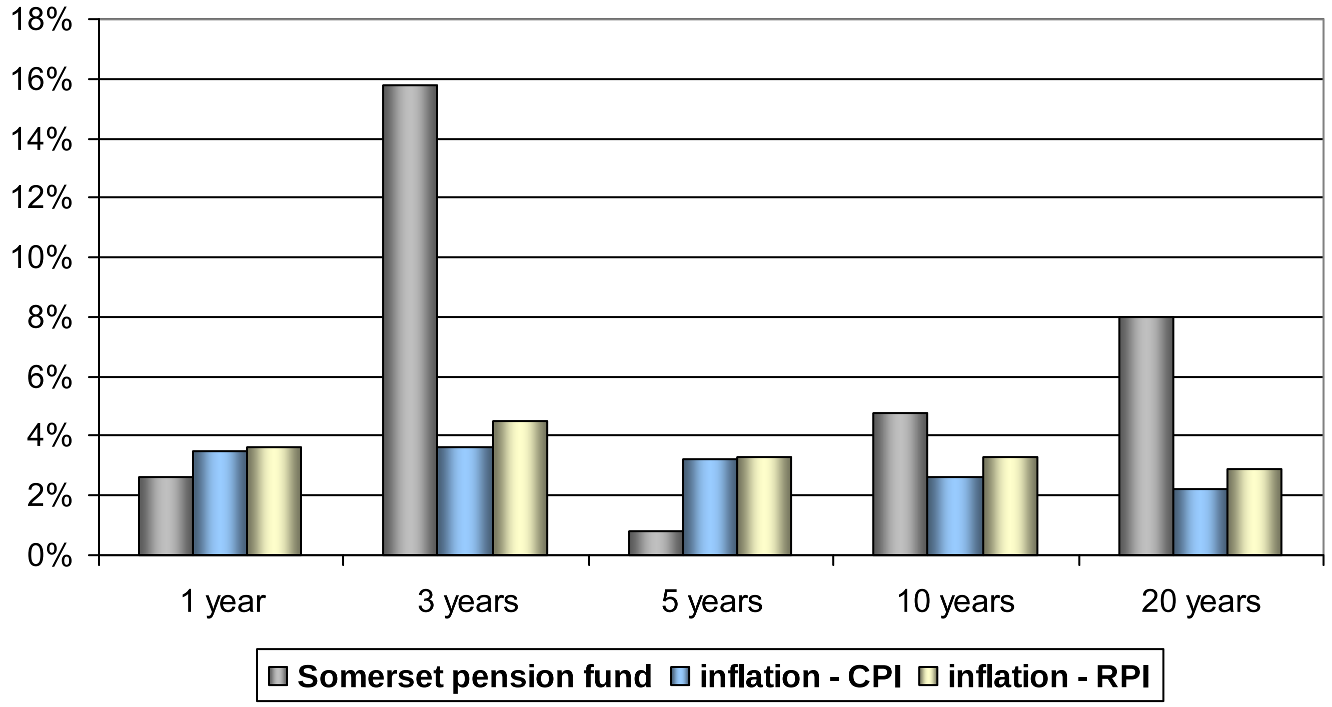
Source: Bank of England
Bloomberg

Investment performance

The success or failure of a pension fund depends largely on the performance of its investments. Benefits are worked out based on final salary, and these benefits are 'index-linked' to protect their value over time. Taking the above into account, there is one simple but important comparison that can be made. This is to compare the growth in value of the fund with the rate of inflation.

For 2011/2012, the fund grew at a rate that was below inflation. Looking back over five-, 10- and 20-year periods, we can see from the chart below that the fund has grown more strongly than inflation over the longer term.

Annualised fund investment performance in relation to inflation



Source: WM Company
Bloomberg

Another measure of performance is how the fund has performed against other funds with similar structures and aims (a ‘peer group’). The WM Company provides us with statistics on the performance of a peer group of local-authority pension funds.

Against this peer group of local-authority funds, we are ranked 47th out of 81 funds for 2011/2012, compared with being 39th out of 86 in 2010/2011.

The aims of pension-fund management are long term so it is important to measure performance over, say, five-, 10- or 20-year periods. The WM Company statistics also give these figures for comparison.

For the five-year period, we are placed 75th out of 77 local-authority funds. Over the 10-year period, we are placed 60th out of 71 funds. Over 20 years, we are 42nd out of 56 funds.

Annualised time-weighted return

	One year %	Five years %	10 years %	20 years %
Best	23.5	9.9	7.9	9.9
Upper 25%	4.2	4.0	6.1	8.5
Weighted average	2.6	3.2	5.7	8.3
Lower 25%	2.1	2.1	5.0	8.0
Worst	-1.0	-1.1	2.7	6.7
Somerset	2.6	0.8	4.8	8.0
Position out of 100	58	97	84	75
Ranked	47	75	60	42
out of	81	77	71	56

Source: WM Company

Overall fund performance

Like most pension funds, the fund's total return was positive but unremarkable for the financial year at a return of 2.6%. We measure how good we think this figure is against our scheme-specific benchmark. This benchmark is basically a combination of the benchmarks we give to the individual asset managers and is worked out for us by the WM Company. The return on our scheme-specific benchmark was 3.6% and the fund under performed against this by 1.0%. The performance of each of the fund managers is shown in the table below.

1 year fund performance

Manager	Asset class	Fund	Benchmark	Fund relative to benchmark
Somerset County Council	Passive global equity	1.2%	1.0%	0.2%
Standard Life	UK equity	2.5%	1.4%	1.1%
Somerset County Council	Passive US equity	Initial investment in December 2011		
Jupiter	European equity	-5.5%	-11.4%	5.9%
Nomura	Japanese equity	4.1%	1.6%	2.5%
UBS	Far East equity	-3.3%	-5.1%	1.8%
Pioneer	Emerging market equity	-14.2%	-8.5%	-5.7%
Standard Life	Bonds	11.6%	13.0%	-1.4%
Aviva	Property	5.2%	5.7%	-0.5%
Neuberger Berman	Global private equity	1.8%	0.5%	1.3%
Yorkshire Fund Managers	Venture capital	0.0%	0.5%	-0.5%
Somerset County Council	Cash	1.0%	0.5%	0.5%
Whole Fund		**2.6%**	**3.6%**	**-1.0%**

Source: WM Company

3 year (annualised) fund performance

Manager	Asset class	Fund	Benchmark	Fund relative to benchmark
Somerset County Council	Passive global equity	15.7%	16.6%	-0.9%
Standard Life	UK equity	19.9%	18.8%	1.1%
Somerset County Council	Passive US equity	Initial investment in December 2011		
Jupiter	European equity	20.7%	12.3%	8.4%
Nomura	Japanese equity	Initial investment in March 2010		
UBS	Far East equity	21.1%	22.5%	-1.4%
Pioneer	Emerging market equity	16.5%	20.6%	-4.1%
Standard Life	Bonds	13.4%	13.7%	-0.3%
Aviva	Property	8.1%	8.8%	-0.7%
Neuberger Berman	Global private equity	Initial investment in March 2010		
Yorkshire Fund Managers	Venture capital	0.0%	0.0%	0.0%
Somerset County Council	Cash	Comparable data not available		
Whole Fund		**15.8%**	**15.6%**	**0.2%**

Source: WM Company

5 year (annualised) fund performance

Manager	Asset class	Fund	Benchmark	Fund relative to benchmark
Somerset County Council	Passive global equity	6.2%	6.2%	0.0%
Standard Life	UK equity	-4.3%	-5.1%	0.8%
Somerset County Council	Passive US equity	Initial investment in December 2011		
Jupiter	European equity	3.6%	-1.0%	4.6%
Nomura	Japanese equity	Initial investment in March 2010		
UBS	Far East equity	8.2%	8.4%	-0.2%
Pioneer	Emerging market equity	Initial investment in March 2009		
Standard Life	Bonds	Initial investment in February 2008		
Aviva	Property	-4.6%	-3.6%	-1.0%
Neuberger Berman	Global private equity	Initial investment in March 2010		
Yorkshire Fund Managers	Venture capital	0.0%	2.0%	-2.0%
Somerset County Council	Cash	Comparable data not available		
Whole Fund		**0.8%**	**2.2%**	**-1.4%**

Source: WM Company

Financial statements

Our responsibilities

As the trustee of the fund, Somerset County Council must:

- appoint an officer to manage the fund’s financial affairs – for us, that officer is the Director of Finance and Performance; and
- manage the fund's affairs to protect its assets and make sure resources are used economically, efficiently and effectively.

Responsibilities of the Director of Finance and Performance

The Director of Finance and Performance is responsible for preparing the pension fund's statement of accounts which, in terms of the CIPFA Code of Practice on Local Authority Accounting in Great Britain (‘the code’), must give a true and fair view on the financial position of the pension fund at the accounting date and its income and spending for the year ended 31 March 2012.

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

- selected suitable accounting policies and then applied them consistently;
- made judgements and estimates that were reasonable and cautious; and
- followed the code.

The Director of Finance and Performance has also:

- kept proper accounting records which were up to date; and
- taken reasonable steps to prevent and detect fraud and other irregularities.

Background

The Somerset County Council pension fund is a defined benefit pension plan for the employees of the County Council and other employers in Somerset.

The fund receives contributions and investment income to meet pension benefits and other liabilities related to a large number of the County Council's employees. It does not cover teachers (whose pensions are managed through the Government's Department for Children, Schools and Families). The fund also extends to cover employees of district councils, civilian employees of the Avon and Somerset Police Authority (police officers have a separate scheme) and employees of other member bodies. A full list of employers who participate in the fund is provided on the next page.

Contributions by employees are based on seven tiered contribution bands dependent on the individual employee’s pay, the seven contribution bands range from 5.5% to 7.5%. Nationally the Government estimate the average employee contribution is 6.3%.

All employers' contribution rates are decided by the fund's actuary every three years as part of his valuation of the fund. The last valuation of the fund was made as at 31 March 2010. For Somerset County Council, for example, the employer's contribution rate for the three years covered by this valuation is 13.5% for each of the years from 2011 to 2014 plus a fixed sum of £3.77m for 2011/2012, £4.88m for 2012/2013 and £5.83m for 2013/2014. This compares with a rate of 15.1% for the 2010/2011 year set under the 2007 valuation. A common contribution rate will, in the long term, be enough to meet the liabilities of the fund assessed on a full-funding basis – this was 17.9% at the 2010 valuation (14.7% at the 2007 valuation). This common contribution rate can be split into amounts that meet new service and an amount needed to make up the deficit in the fund, the common rate of 17.9% is made up of a rate of 13.1% for new service and 4.8% for deficit funding. As part of the 2010 valuation most employers have agreed to meet the deficit funding portion by paying a fixed monetary amount rather than a percentage of pensionable pay (as demonstrated by the example of Somerset County Council above). The aim of this is to remove the volatility caused by changing staff levels. At the valuation the actuary estimated that the fund’s assets covered 77% of the fund’s liabilities.

The pension and lump-sum payments that employees receive when they retire are related to their final year’s salary and also how long they have worked for an employer within the fund. Increases in pension payments linked to inflation come out of the fund.

Administering authority
Somerset County Council

Member bodies

Scheduled bodies with contributors

County council
Somerset

Police authority
Avon and Somerset (civilian staff)

District councils
Mendip
Sedgemoor
South Somerset
Taunton Deane
West Somerset

Parish and town councils
Axbridge Town Council
Berrow Parish Council
Burnham and Highbridge Town Council and Burial Board
Chard Town Council
Crewkerne Town Council and Burial Board
Frome Town Council
Glastonbury Town Council
Ilminster Town Council
Langport Town Council
Lower Brue Drainage Board
Minehead Town Council
Shepton Mallet Town Council
Somerton Town Council
Street Parish Council
Wellington Town Council
Wells Burial Board and Parish Council
Williton Parish Council
Wincanton Town Council
Yeovil Town Council

Other bodies
Avon and Somerset Probation Board
Exmoor National Park

Further-education colleges
Bridgwater College
Richard Huish Sixth Form College
Somerset College of Art and Technology
Strode College
Yeovil College

Academies
Ansford Academy
Avishayes Academy
Bishop Fox's Academy
Brookside Academy
Bruton Sexey's School
Buckler's Mead Academy
Castle Academy
Crispin Academy
Enmore Academy
Haygrove Academy
Holyrood Academy
Huish Episcopi Academy
Kings of Wessex Academy
Kingsmead Academy
Maiden Beech Academy
Minehead Middle School
North Town Academy
Oakfield Academy
Preston Academy
Redstart Academy
Selwood Academy
St. Dunstan's Academy
Stanchester Academy
Tatworth Academy
Taunton Academy
The Blue School, Wells
Weare Academy
Wedmore Academy
West Somerset Community College
Westfield Academy
Whitstone Academy

Member bodies (continued)

Admitted bodies with contributors
Aster Communities Ltd
Care Focus Somerset Ltd
Connect South West
DHI Ltd
Edward and Ward Ltd
Homes in Sedgemoor
ICM
Learning South West
Leisure East Devon
Lovell Partnership
Magna West Somerset Housing Association
May Gurney Ltd
National Autistic Society
SHAL Housing Ltd
1610 Ltd
Society of Local Council Clerks
Somerset Care Ltd
Somerset Rural Youth Project
South West Regional Assembly Board
Tone Leisure Ltd
Yarlington Housing Group

Fund Account

2010/2011 £ millions	£ millions		2011/2012 £ millions	£ millions	Notes
Restated					
		Contributions and other income			
21.633		Contributions from employees - normal	19.979		1
0.577		- additional	0.496		1
54.341		Contributions from employers	55.389		1
1.535		Recoveries from member organisations	1.825		1
12.715		Transfer values received	4.681		2
90.801			**82.370**		
		Less benefits and other payments			
-46.672		Recurring pensions	-52.217		1
-20.296		Lump sum on retirement	-17.528		1
-1.250		Lump sum on death	-1.126		1
-8.874		Transfer values paid	-2.951		2
-0.016		Refund of contributions to leavers	-0.009		3
-0.994		Administrative expenses	-1.005		4
-78.102			**-74.836**		
	12.699	**Net additions from dealings with members**		**7.534**	
		Investment income			
28.524		Investment income received	34.184		5
5.629		Investment income accrued	4.545		5
-4.032		Less investment management expenses	-3.354		6
-1.441		Less irrecoverable tax	-0.573		
0.006		Other income (such as commission)	0.010		
28.686			**34.812**		
		Change in market value of investments			
18.006		Realised profit or loss	9.791		
34.562		Unrealised profit or loss	-22.565		
52.568			**-12.774**		
	81.254	**Net return on investments**		**22.038**	
	93.953	**Net increase in the net assets available for benefits during the year**		**29.572**	
		Change in actuarial present value of promised retirement benefits			
329.429		Vested benefits	-320.544		
-84.186		Non-vested benefits	-109.767		
	245.243	**Net change in present value of promised benefits**		**-430.311**	
	339.196	**Net increase/(decrease) in the fund during the year**		**-400.739**	
	-1,033.661	Add net liabilities at beginning of year		-694.465	
	-694.465	**Net liabilities at end of year**		**-1,095.204**	

Net Asset Statement

On 31 March 2011 £ millions Restated		On 31 March 2012 £ millions	Notes
	Investment assets and liabilities		
1,165.113	Investment assets	1,191.087	7
-6.138	Investment liabilities	-2.350	7
6.287	Other investment balances	4.897	10
	Current assets		
5.542	Contributions due from employers	4.936	
0.000	Cash at bank	0.021	
2.375	Other debtors	3.502	
	Current liabilities		
0.000	Unpaid benefits	0.000	
-0.173	Bank overdraft	0.000	
-3.529	Other creditors	-3.044	
1,169.477	**Net assets of the scheme available to fund benefits at end of year**	**1,199.049**	
	Actuarial present value of promised retirement benefits		
-1,518.541	Vested benefits	-1,839.085	
-345.401	Non-vested benefits	-455.168	
-694.465	**Net liabilities at end of year**	**-1,095.204**	

Accounting policies

The Pension Fund financial statements have been prepared in line with the conditions of Chapter 2 – Recommended Accounting Practice of the Pension SORP 2007;and

The Pension Fund financial statements have also been prepared in line with the Code of Practice on Local Accounting in the UK 2011/12, which is based upon the International Financial Reporting Standard (IFRS), as amended for the UK public sector.

The Fund account is prepared on a full accruals basis, with the exception of transfer values. As a result the following apply:

- investments are included at market value;
- the majority of listed investments are stated at the bid price or the last traded price, depending on the convention of the stock exchange on which they are quoted, at the date of the net assets statement;

- fixed interest securities are valued excluding accrued income;

- pooled investment vehicles are stated at bid price for funds with bid/offer spreads, or single price (typically net asset value) where there are no bid/offer spreads, as provided by the investment manager;

- forward foreign exchange contracts are valued using the foreign exchange rate at the date of the net asset statement;

- The Neuberger Berman Crossroads 2010 fund is valued using data supplied by the fund quarterly;

- the South West Regional Venture Fund is valued at cost;

- contributions and benefits are accounted for in the period in which they fall due;

- interest on deposits and fixed interest securities are accrued if they are not received by the end of the financial year;

- interest on investments are accrued if they are not received by the end of the financial year;

- all dividends and interest on investments are accounted for on 'ex-dividend' dates;

- all settlements for buying and selling of investments are accrued on the day of trading;

- transfer values are accounted for when money is received or paid. This treatment is in line with the revised SORP which applied fully from 1 April 1998. 1 transfer into the scheme amounting to £6,000 was agreed but not settled on 31 March 2012. There was 1 transfer out for £342,000 which was outstanding at the end of the financial year. Neither of these appear in these accounts; and

- the fund has significant investments overseas. The value of these investments in the net asset statement is converted into sterling at the exchange rates on 31 March. Income receipts, and purchases and sales of overseas investments, are normally converted into sterling at or about the date of each transaction and are accounted for using the actual exchange rate received. Where the transaction is not linked to a foreign exchange transaction to convert to sterling the exchange rate on the day of transaction is used to convert the transaction into sterling for accounting purposes.

Notes to the Accounts

Note 1: Contributions and benefits

	Somerset County Council £ millions	Other scheduled employers £ millions	Admitted employers £ millions	Total £ millions
Employees' contributions				
- Normal	9.024	9.429	1.526	**19.979**
- Additional	0.253	0.240	0.003	**0.496**
Total	9.277	9.669	1.529	**20.475**
Employers' contributions				
- Normal	19.520	19.602	2.843	**41.965**
- Augmentation	2.973	2.072	0.277	**5.322**
- Deficit funding	3.770	2.203	2.129	**8.102**
Total	26.263	23.877	5.249	**55.389**
Recurring pension and lump sum payments	-32.176	-32.424	-6.271	**-70.871**
Money recovered from member organisations	0.111	1.383	0.331	**1.825**
	3.475	**2.505**	**0.838**	**6.818**

Note 2: Transfer Values

2010/2011 £ millions		2011/2012 £ millions
0.000	Group transfer values received	0.000
12.715	Individual transfer values received	4.681
12.715		**4.681**
0.000	Group transfer values paid	0.000
-8.874	Individual transfer values paid	-2.951
-8.874		**-2.951**

Note 3: Refunds

2010/2011 £ millions		2011/2012 £ millions
-0.017	Contributions refunded to people who leave with less than three months' service	-0.008
-0.002	Interest accumulated on refunds agreed in the past	-0.001
-0.019		**-0.009**
0.002	Deductions from contributions equivalent premium	0.001
0.001	Less payments to Department for Work and Pensions contributions equivalent premium	-0.001
-0.016		**-0.009**

Note 4: Administration Expenses

2010/2011 £ millions		2011/2012 £ millions
-0.844	Administration costs charged by Somerset County Council	-0.844
-0.045	Audit fees	-0.022
-0.055	Actuary's fees	-0.120
-0.016	Legal expenses	0.000
-0.034	Other expenses	-0.019
-0.994		**-1.005**

Note 5: Investment Income

2010/2011 £ millions		2011/2012 £ millions
9.159	Fixed interest	10.274
0.751	Index linked	0.693
9.274	UK equities	10.029
10.700	Foreign equities	11.711
3.924	Property unit trusts	5.611
0.120	Cash invested internally	0.248
0.000	Venture capital	0.000
0.001	Commission recapture	0.003
0.224	Stock lending	0.160
34.153		**38.729**

Note 6: Investment Expenses

2010/2011 £ millions	2010/2011 £ millions		2011/2012 £ millions	2011/2012 £ millions
		Fund manager fees		
-0.152		Aviva Investors	-0.177	
-0.452		JP Morgan Asset Management	-0.135	
-0.470		Jupiter Asset Management	-0.424	
-0.191		Pioneer	-0.162	
-0.280		Record Currency Management	-0.054	
-1.002		Standard Life Investments	-0.906	
-0.232		UBS Global Asset Management	-0.126	
	-2.779			**-1.984**
		Other expenses		
-0.094		Professional services and subscriptions	-0.146	
-0.137		Specialist IT systems	-0.160	
-0.173		Custody fees	-0.155	
-0.018		Performance measurement fees	-0.020	
-0.831		Property unit trust managers' fees	-0.889	
	-1.253			**-1.370**
	-4.032			**-3.354**

Note 7: Investment Assets & Liabilities

31 March 2011 £ millions	£ millions	%	%		31 March 2012 £ millions	£ millions	%	%
				UK equities				
303.421		26.2		Quoted	306.718		25.8	
5.780		0.5		Standard Life smaller companies fund	5.869		0.5	
	309.201		**26.7**			**312.587**		**26.3**
				Overseas equities				
229.867		19.8		North America	232.162		19.5	
136.831		11.8		Europe	121.460		10.2	
27.348		2.4		Japan	25.105		2.1	
73.211		6.3		Pacific (not including Japan)	67.851		5.7	
1.142		0.1		Middle East	0.642		0.1	
33.134		2.9		Nomura Japan fund	34.507		2.9	
36.816		3.2		Pioneer emerging markets fund	51.429		4.3	
	538.349		**46.5**			**533.156**		**44.8**
				Bonds				
17.090		1.5		UK fixed-interest - public sector	19.140		1.6	
106.093		9.1		- corporate sector	112.793		9.5	
43.591		3.8		UK index-linked - public sector	52.037		4.4	
1.109		0.1		- corporate sector	0.000		0.0	
0.538		0.0		Overseas index-linked - public sector	0.685		0.1	
0.000		0.0		Overseas - public sector	0.000		0.0	
35.797		3.1		- corporate sector	39.483		3.3	
	204.218		**17.6**			**224.138**		**18.9**
				Property				
83.957		7.2		UK property funds	93.436		7.9	
8.430		0.7		Overseas property funds	8.520		0.7	
	92.387		**7.9**			**101.956**		**8.6**
				Private equity				
2.320		0.2		Neuberger Berman Crossroads 2010 fund	3.295		0.3	
2.000		0.2		South West regional venture fund	2.000		0.2	
	4.320		**0.4**			**5.295**		**0.5**
				Derivatives				
1.758		0.1		Forward foreign-exchange contracts	1.526		0.1	
0.000		0.0		Government bond futures	0.000		0.0	
	1.758		**0.1**			**1.526**		**0.1**
				Cash and others				
14.880		1.3		Cash invested internally	12.429		1.0	
	14.880		**1.3**			**12.429**		**1.0**
	1,165.113		**100.5**	**Investment assets**		**1,191.087**		**100.2**

Table continued on next page

Note 7: Investment Assets & Liabilities (continued)

31 March 2011 £ millions	£ millions	%	%		31 March 2012 £ millions	£ millions	%	%
				Derivatives				
-6.138		-0.5		Forward foreign-exchange contracts	-2.350		-0.2	
0.000		0.0		Government bond futures	0.000		0.0	
	-6.138		**-0.5**			**-2.350**		**-0.2**
	-6.138		**-0.5**	**Investment liabilities**		**-2.350**		**-0.2**
	1,158.975		**100.0**	**Net investment assets**		**1,188.737**		**100.0**
				Made up of				
	958.126			Historical cost		1,010.453		
	200.849			Unrealised profit or loss		178.284		
	1,158.975					**1,188.737**		

Note 8: Movement in Investment Assets

Manager	Asset class	Investment assets as at 1 April £ millions	Change in cash invested internally £ millions	Purchases £ millions	Sales proceeds £ millions	Realised profit or loss £ millions	Unrealised profit or loss £ millions	Investment assets as at 31 March £ millions
2010/2011	Total	1,063.739	-22.873	3,989.576	-3,924.035	18.006	34.562	1,158.975
Somerset County Council	Global equity	319.360	0.000	41.717	-54.331	2.315	-11.196	297.865
Standard Life	UK equity	279.733	0.000	95.920	-80.024	-4.756	-5.419	285.454
JP Morgan / SCC	US equity	61.979	0.000	80.379	-78.627	4.583	-1.464	66.850
Jupiter	European equity	72.678	0.000	22.689	-18.030	-3.440	-5.823	68.074
Nomura	Japanese equity	33.134	0.000	0.050	0.000	-0.050	1.373	34.507
UBS	Far East equity	43.850	0.000	14.670	-14.245	1.644	-4.355	41.564
Pioneer	Emerging Market equity	36.816	0.000	20.000	0.000	0.000	-5.387	51.429
Standard Life	Bonds	204.218	0.000	72.559	-62.769	1.807	8.323	224.138
Standard Life	Derivatives	-1.644	0.000	442.516	-442.428	-0.095	2.018	0.367
Aviva	Property	92.387	0.000	17.909	-3.962	-2.319	-2.059	101.956
Aviva	Currency	-0.261	0.000	69.480	-69.480	0.000	0.424	0.163
Record	Currency	-2.475	0.000	2,249.115	-2,244.175	-4.941	1.122	-1.354
Neuberger Berman	Global private equity	2.320	0.000	1.594	-0.612	-0.032	0.025	3.295
Yorkshire	UK venture capital	2.000	0.000	0.000	0.000	0.000	0.000	2.000
Somerset County Council	Cash	14.880	-17.379	0.000	0.000	15.075	-0.147	12.429
2011/2012	**Total**	**1,158.975**	**-17.379**	**3,128.598**	**-3,068.683**	**9.791**	**-22.565**	**1,188.737**

Transaction costs for the year amount to £854,000

Note 9: Management Structure

31 March 2011 £ millions	%	Manager	Asset class	31 March 2012 £ millions	%
319.360	28	Somerset County Council	Passive global equity	297.865	25
279.733	24	Standard Life	UK equity	285.454	24
61.979	5	JP Morgan	US equity	0.000	0
0.000	0	Somerset County Council	Passive US equity	66.850	6
72.678	6	Jupiter	European equity	68.074	6
33.134	3	Nomura	Japanese equity	34.507	3
43.850	4	UBS	Far East equity	41.564	3
36.816	3	Pioneer	Emerging market equity	51.429	4
202.574	18	Standard Life	Bonds	224.505	19
92.126	8	Aviva	Property	102.119	9
-2.475	0	Record Currency Management	Currency	-1.354	0
2.320	0	Neuberger Berman	Global private equity	3.295	0
2.000	0	Yorkshire Fund Managers	UK venture capital	2.000	0
14.880	1	Somerset County Council	Cash	12.429	1
1,158.975	**100**	**Net investment assets**		**1,188.737**	**100**

Note 10: Other investment balances

31 March 2011 £ millions		31 March 2012 £ millions
	Assets	
5.057	- Accrued income	4.545
0.489	- Accrued Recoverable tax	0.544
2.125	- Payments due on investments sold	2.019
7.671		**7.108**
	Liabilities	
-1.384	- Payments not made on purchases and losses due on sales	-2.211
6.287		**4.897**

Note 11: Major Holdings

31 March 2011 Rank	£ millions	Stock	Description	31 March 2012 Rank	£ millions
1	36.816	Pioneer Emerging Market Equity Fund	Pooled fund of emerging market equities	1	51.429
2	33.134	Nomura Japan Fund	Pooled fund of Japanese equities	2	34.507
4	20.167	Royal Dutch Shell	UK oil company	3	21.576
3	20.498	HSBC	UK bank	4	16.714
7	14.927	BP	UK oil company	5	15.413
6	17.087	Vodafone	UK mobile phone company	6	14.382
9	11.513	Glaxosmithkline	UK drugs producer	7	14.287
5	19.020	Rio Tinto	UK mining company	8	11.323
8	12.750	BHP Billiton	UK mining company	9	10.155
18	6.313	Apple	US electronics company	10	9.234
-	0.000	Schroders Exempt PUT	UK property unit trust	11	9.087
12	8.610	Aviva Pooled Pension PUT	UK property unit trust	12	9.024
11	10.097	BG Group	UK gas company	13	8.983
13	8.191	Blackrock property fund	UK property unit trust	14	8.232
37	4.701	British American Tobacco	UK tobacco company	15	7.929
10	10.174	Xstrata	UK mining company	16	7.715
17	6.367	Standard Chartered	UK bank	17	7.129
14	7.232	Exxon Mobil	US oil company	18	6.747
15	6.898	Hercules PUT	UK property unit trust	19	6.690
16	6.631	Tullow Oil	UK oil company	20	6.683

None of the holdings of the fund makes up more than 5% of the net investment assets. The largest holding (Pioneer Emerging Market Equity Fund) makes up 4.3% of the net investment assets.

Note 12: Derivatives

Investment in derivative instruments may only be made if they contribute to a reduction of risk or facilitates more efficient portfolio management.

During the year the fund used forward foreign exchange contracts and bond futures.

The year end value of derivatives is as follows:

31 March 2011 £ millions Asset	Liability	Net value		31 March 2012 £ millions Asset	Liability	Net value
			Forward foreign-exchange contracts			
0.031	-1.675	-1.644	Standard Life fixed Interest	0.386	-0.019	0.367
0.000	-0.261	-0.261	Aviva	0.163	0.000	0.163
1.727	-4.202	-2.475	Record passive fund	0.977	-2.331	-1.354
1.758	**-6.138**	**-4.380**		**1.526**	**-2.350**	**-0.824**
			Government bond futures			
0.000	0.000	0.000	UK Government gilt future	0.000	0.000	0.000
0.000	0.000	0.000	Euro bond futures	0.000	0.000	0.000
0.000	0.000	0.000	US Government treasury future	0.000	0.000	0.000
0.000	**0.000**	**0.000**		**0.000**	**0.000**	**0.000**
1.758	**-6.138**	**-4.380**		**1.526**	**-2.350**	**-0.824**

Standard Life hold forward foreign exchange contracts to hedge the foreign exchange risk of holding investments that are not valued in sterling in their fixed income portfolio. The non-sterling bonds are either government bonds or high yield bonds. Typically Standard Life chose to hedge 100% of their currency risk.

Aviva also hold forward foreign exchange contracts to hedge the foreign exchange risk of holding investments that are not valued in sterling in their property portfolio. The non-sterling investments are 4 funds that invest in European property and are priced in euros. Typically Aviva chose to hedge 100% of their currency risk.

In the Record passive fund the aim is to hedge 60% of the currency exposure of the currencies we have exposure to in our equity holdings. The currencies hedged are Australian dollars, Canadian dollars, Danish krone, euros, Hong Kong dollars, Japanese yen, Norwegian krone, Singapore dollars, Swedish krona, Swiss francs and US dollars. The management of these exchange risks should reduce the volatility of returns of the overall fund in the long term.

The fair value of these contracts at year end is based on market foreign exchange rates at the year end date. All forward foreign exchange contracts are over the counter trades.

The bond futures are used by Standard Life to gain exposure to overseas government bonds with lower trading costs and better liquidity than trading the underlying bonds themselves. There are significant restrictions in how Standard Life use bond futures to ensure they do not increase the overall risk of the portfolio they are managing. The bond futures are exchange traded contracts.

The gross exposure values (the value of the assets bought and sold within the derivatives contracts) are shown in the following table.

31 March 2011 £ millions Asset exposure value	Liability exposure value	Net value		31 March 2012 £ millions Asset exposure value	Liability exposure value	Net value
			Forward foreign-exchange contracts			
36.843	-38.487	-1.644	Standard Life fixed Interest	47.387	-47.020	0.367
8.049	-8.310	-0.261	Aviva	8.860	-8.697	0.163
269.223	-271.698	-2.475	Record passive fund	125.476	-126.830	-1.354
314.115	**-318.495**	**-4.380**		**181.723**	**-182.547**	**-0.824**
			Government bond futures			
2.343	-2.343	0.000	UK Government gilt future	0.916	-0.916	0.000
0.432	-0.432	0.000	Euro bond futures	0.000	0.000	0.000
0.000	0.000	0.000	US Government treasury future	1.242	-1.242	0.000
2.775	**-2.775**	**0.000**		**2.158**	**-2.158**	**0.000**
316.890	**-321.270**	**-4.380**		**183.881**	**-184.705**	**-0.824**

Note 13: Stock Lending

31 March 2011 £ millions		31 March 2012 £ millions
30.398	Value of stock on loan	22.506
32.254	Value of collateral held against loaned stock	23.803

31 March 2011 %		31 March 2012 %
	Form of collateral provided	
20.1	UK Government debt	16.8
13.8	UK equities	3.0
0.0	US denominated corporate debt	0.6
61.1	US equities	75.5
5.0	€ denominated corporate debt	4.1
100.0		**100.0**

Note 14: Membership Statistics

As at 31 March	2006	2007	2008	2009	2010	2011	2012
Active scheme members	**18,463**	**19,071**	**19,886**	**20,022**	**20,450**	**20,492**	**19,505**
Pensioners							
Current (in payment)	8,818	9,126	9,706	10,126	10,821	11,664	12,301
Deferred (future liability)	9,025	10,059	10,897	12,787	13,817	14,923	16,816
Total (active plus pensioners)	**36,306**	**38,256**	**40,489**	**42,935**	**45,088**	**47,079**	**48,622**
Active members for each current pensioner	2.09	2.09	2.05	1.98	1.89	1.76	1.59

Note 15: Additional voluntary contributions

During the year some members of the fund paid additional voluntary contributions (AVCs) to Equitable Life and Prudential to buy extra pension benefits when they retire. The pension fund accounts, in accordance with regulation 5 (2)(C) of the Pension Scheme (Management and Investment of Funds) Regulations 1998 do not include AVC transactions. The contributions for the year and the outstanding value of assets invested via AVCs at 31 March are shown in the following table.

31 March 2011 £ millions		31 March 2012 £ millions
	Value of additional voluntary contributions	
3.834	Prudential	4.063
0.636	Equitable Life	0.511
4.470		**4.574**

2010/2011 £ millions		2011/2012 £ millions
	Additional voluntary contributions paid during the year	
0.658	Prudential	0.597
0.001	Equitable Life	0.000
0.659		**0.597**

Note 16: Related Parties

Pensions Committee members, Tim Carroll, Sam Crabb, Caroline Moore, Sarah Payne, William Wallace and John Wilkins are members of the Somerset County Council Pension Scheme.

Pensions Committee member Sarah Payne has personal investments that are managed by Jupiter Asset Management.

The fund holds shares in a number of companies that Somerset County Council and the other member bodies have commercial dealings with. Decisions about the suitability of companies for the fund to invest in are taken by Standard Life, Jupiter Asset Management, UBS Global Asset Management, Nomura Asset Management, Pioneer Investments and Aviva Investors for their parts of the fund, without referring to the county council, its officers or other member bodies. Decisions about suitable investments for the in-house funds are made based only on the recommendations of a quantitative analysis system, so officers do not have the power to include or exclude specific companies.

No other related party transactions other than normal contributions, benefits and transfers occurred during the year. In note 1 we analyse the total contributions we were due to receive and benefits the fund paid for scheduled and admitted bodies.

Note 17: Statement of Investment Principles

We have prepared a Statement of Investment Principles, which explains the strategies and policies that we use in the administration of the pension fund's investments. The full details of the statement are published in the Pension Fund Annual Report and Financial Statement and is also available on the County Council website.

Note 18: Contingent liabilities

There were no contingent liabilities as at 31 March 2012.

Note 19: Post balance sheet events

There were no post balance sheet events as at 30th June 2012.

Note 20: Nature and Extent of Risks Arising from Financial Instruments

As a result of the adoption of IFRS the fund is required to make disclosures of the risks arising from holding Financial Instruments. For the purpose of this disclosure financial instruments means all of the fund's investment assets and investment liabilities as shown in note 7 of these accounts, the approximation of the fair value of the net of these assets and liabilities at 31 March 2012 being £1,189m.

The main risks from the fund's holding of financial instruments are market risk, credit risk and liquidity risk. Market risk includes price risk, interest rate risk and currency risk.

The fund's assets are managed by a mixture of officers and external fund managers as described in note 9 of these accounts. A management agreement is put in place with each external fund manager which clearly states the type of investments they are allowed to make for the fund, asset allocation ranges and any further restrictions we believe are necessary.

To make investments as secure as they can be, where possible, external investments are maintained under the control of a safe custodian. Only cash holdings and a small number of unit trusts stay under the control of officers.

Because the fund adopts a long term investment strategy, the high level risks described below will not alter significantly during the year unless there are significant strategic or tactical changes in the portfolio.

Market Risk

Market risk represents the risk that the fair value of a financial instrument will fluctuate because of changes in the market prices of assets or currencies where the assets are priced in currencies other than British pounds.

The fund is exposed to market risk on all of its investment assets with the exception of the cash holdings in Sterling. The aim of the investment strategy is to manage and control market risk within acceptable parameters, while optimising the return from the investment portfolio

The fund holds a diversified portfolio of different assets, which are managed by a variety of fund managers which have a variety of investment styles. This diversification is the most effective way of managing market risk.

The fund particularly manages the effect of market movements on exchange rates by hedging a portion of its foreign currency exposure using currency forwards. Details of this are given in note 12 of these accounts.

The sensitivity of the fund's investments to changes in market prices have been analysed using the volatility of returns experienced by asset classes. The volatility data has been provided by the WM Company, the fund's performance measurement advisor, and is broadly consistent with a one-standard deviation movement. The volatility is measured by the (annualised) estimated standard deviation of the returns of the assets relative to the liability returns. Such a measure is appropriate for measuring "typical" variations in the relative values of the assets and liabilities over short time periods. It is not appropriate for assessing longer term strategic issues.

Movements in market prices would have increased or decreased the investment assets valued at 31 March 2012 by the amounts shown below.

Asset class	**Value of Assets £ millions**	**Volatility**	**Increase in Assets £ millions**	**Decrease in Assets £ millions**
UK equities	312.587	17.90%	55.953	-55.953
Foreign equities	533.156	15.30%	81.573	-81.573
UK bonds	131.933	7.70%	10.159	-10.159
Overseas bonds	40.168	13.20%	5.302	-5.302
UK index-linked bonds	52.037	7.20%	3.747	-3.747
Property	101.956	6.20%	6.321	-6.321
Cash	12.429	0.00%	0.000	0.000
Others	4.471	7.50%	0.335	-0.335
Net investment assets	**1,188.737**		**163.390**	**-163.390**

Credit Risk

Credit risk represents the risk that the counterparty to a financial instrument will fail to meet an obligation and cause the fund to incur a financial loss. This is often referred to as counterparty risk.

The fund is subject to credit risk within its general debtors although none of these would represent a material risk to the fund.

The fund has credit risk to each of its employer bodies in that they could become insolvent and default on a pension deficit owed to the fund. The majority of the employers in the fund are statutory bodies backed to a greater or lesser extent by the UK government. For the admitted bodies the credit risk is mitigated and managed by the holding of guarantee bonds or having their deficit guaranteed by one of the statutory bodies within the fund.

Bankruptcy or insolvency of the custodian may affect the fund's access to its assets. However, all assets held by the custodian are ring-fenced as "client assets" and therefore cannot be claimed by creditors of the custodian. The fund manages its risk by monitoring the credit quality and financial position of the custodian.

A source of credit risk is the cash balances held to meet operational requirements or by the managers at their discretion and cash deposits with various institutions. Internally held cash is managed on the fund's behalf by the Council's Treasury Management Team in line with the fund's Counterparty Policy which sets out the permitted counterparties and limits. The exposure within the cash management part of the portfolio to a single entity is limited to £10m and all counterparties must be rated at least “A” or higher by a major rating agency. In this context the fund’s cash balances (including the cash held at bank or net of bank overdraft) of £12.4m is subject to credit risk.

Through its securities lending activities, the fund is exposed to the counterparty risk of the collateral provided by borrowers against the securities lent. This risk is managed by restricting the collateral permitted to high grade sovereign debt and baskets of liquid equities. Cash collateral is not permitted. Details of the collateral held are provided within note 13 of these accounts.

Forward foreign exchange contracts are subject to credit risk in relation to the counterparties of the contracts, which are primarily banks. The maximum credit exposure on foreign currency contracts is the full amount of the contractual settlement should the counterparty fail to meet it obligations to the fund when it falls due. The fair value and full exposure levels of the forward foreign exchange contracts held are provided in note 12 of these accounts.

It is arguable that the fund has significant exposure to credit risk within its bond holdings, the reality is that as the perception of the credit quality of the bond issuer varies through time the market price of the bond varies accordingly, this means that the market risk of these holdings effectively encompasses the counterparty risk.

Liquidity risk

Liquidity risk represents the risk that the fund will not be able to meet its financial obligations as they fall due. The fund mitigates this risk by monitoring and projecting its cash flow to enable it to have cash resources as they are required and maintains a cash balance to meet working requirements.

A substantial portion of the fund's investments consist of cash and readily realisable securities, in particular equities and fixed income investments. This gives the fund access to in excess of £1bn of assets which could be realistically liquidated into cash in less than a week.

The main liability of the fund is the benefits payable, which fall due over a long period and the investment strategy reflects the long term nature of these liabilities. The estimated present value of these obligations is shown on the net asset statement of these accounts and the value of these benefits that fell due in the past financial year is shown on the fund account of these accounts.

The forward foreign exchange contracts held by the fund do give rise to a liquidity risk as they must be settled at a prescribed date agreed at the time of placing the contract. The exact size of this liability varies in line with foreign exchange prices on an on-going basis. The furthest date at which some of these contracts expire is never more than 6 months and the cash flows involved are regularly monitored to ensure we can meet these liabilities as they fall due. The fair value and full exposure levels of the forward foreign exchange contracts held are provided in note 12 of these accounts.

The bond futures have daily margin calls and no cash liability beyond these. The size of the daily margin calls are typically around £10,000 and therefore do not pose a significant liquidity risk to the fund.

Note 21: Fair Value Hierarchy

The fund measures fair values using the following hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: Unadjusted quoted prices in an active market for identical assets or liabilities that the fund has the ability to access at the measurement date.
- Level 2: Inputs other than quoted prices under Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: Unobservable inputs for the assets or liability used to measure fair value that rely on the fund's own assumptions concerning the assumptions that market participants would use in pricing an asset or liability.

The table below analyses the fund's investment assets at 31 March 2012 into the 3 levels of the fair value hierarchy.

Asset Class	Level 1 £ millions	Level 2 £ millions	Level 3 £ millions	Total £ millions
UK equities	312.587			312.587
Overseas equities	533.156			533.156
Bonds	224.138			224.138
Property funds		101.956		101.956
Private Equity funds			5.295	5.295
Forward foreign-exchange contracts	-0.824			-0.824
Government bond futures	0.000			0.000
Cash	12.429			12.429
Net investment assets	**1,081.486**	**101.956**	**5.295**	**1,188.737**

Note 22: Disclosures

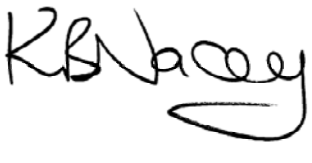
A non material error was made in the preparation of the 2010-2011 accounts that has been corrected and the prior year comparators shown in these accounts have been restated. This has led to an increase in “recurring pensions” on the fund account of £0.021m to £46.672m for 2010-2011 and an increase in “other creditors” on the net asset statement of £0.021m to £3.529m at 31 March 2011.

There is also a restatement on the net asset statement within current assets at 31 March 2011. An amount of £4.054m was incorrectly shown as “other debtors” when it should have been shown as “contributions due from employers”. As a result “other debtors” has been reduced by this amount to £2.375m and “contributions due form employers” increased to £5.542m.

JP Morgan Asset Management ceased to manage the US equity mandate on behalf of the fund on 31st December 2011. From the 1st January 2012 this mandate has been run by the in-house team on a passive basis. This change is reflected in note 9.

Under IFRS the fund must disclose what consideration it has given to accounting standards that have not been adopted. For the 2011-12 accounts the only such standard relates to the transfer of financial assets. Transfers of financial assets do not occur for the fund and as such no disclosure would be necessary if the fund adopted this standard.

The present value of promised retirement benefits is an estimate of the value of the lump sums and pensions that the fund will pay in the future. The estimate has been calculated by the fund’s actuary and has been prepared in accordance with International Accounting Standard (IAS) 26. In calculating the disclosed numbers the actuary has adopted methods and assumptions that are consistent with IAS19. In accordance with IAS 19 the assumptions used to make the calculations are set with reference to market conditions at the net asset statement date. The principle change in assumptions between 31 March 2011 and 31 March 2012 is to the real discount rate assumption. The discount rate is the yield on the iBoxx AA rated over 15 year corporate bond index as at the date of the net asset statement, which has been chosen to meet the requirements of IAS19. As the yield on these bonds has fallen from 5.5% to 4.6% this has significantly increased the value of the present value of the promised retirement benefits over the year.



Kevin Nacey, Director of Finance and Performance
September 2012

Actuary's statement

Introduction

The last full triennial valuation of the Somerset County Council Pension Fund was carried out by Barnett Waddingham as at 31 March 2010 in accordance with Regulation 38 of the Local Government Pension Scheme (Administration) Regulations 2008 (as amended). The results were published in our report dated March 2011.

2010 Valuation

The results for the Fund were as follows

- The funding level was calculated to be 77% i.e. the value of the accumulated assets represented 77% of the value of the accrued liabilities of Fund as at the valuation date.
- The common contribution rate was set at 17.9% of payroll assuming the funding level was to be restored over a 25 year period. This is the average contribution rate required from employers to restore the funding level to 100% over the next 25 years.
- However each employing body pays their own contribution rate to reflect its own particular circumstances and funding position within the Fund. The County Council is paying an ongoing contribution of 13.5% of payroll plus additional monetary amounts in respect of deficit recovery.
- Details of each employer's contribution rate are contained in the Statement to the Rates and Adjustment Certificate in the triennial valuation report.

Asset Value and Key Financial Assumptions

The value of the Fund's assets as at 31 March 2010 for valuation purposes was £1,068m.

The contribution rates were calculated using the Projected Unit Method taking account of market conditions as that date as follows.

Rate of return on investments	7.1% per annum
Rate of increase in pay	5.0% per annum
Rate of increase to pensions in payment	3.0% per annum

Post Valuation Events

In the 2 years to March 2012, investment returns and changes in market conditions have not been as favourable as assumed and overall there has been a slight deterioration in the financial position of the Fund level since the last valuation.

The next actuarial valuation is due as at 31 March 2013 and the resulting contribution rates required by the employers will take effect from 1 April 2014.

Graeme Muir FFA
Partner
16 May 2012

Independent auditor's report to the Members of Somerset County Council on the Pension Fund

Opinion on the pension fund financial statements

I have audited the pension fund financial statements for the year ended 31 March 2012 under the Audit Commission Act 1998. The pension fund financial statements comprise the Fund Account, the Net Assets Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of Somerset County Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and of Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Director of Finance and Performance and auditor

As explained more fully in the Statement of the Director of Finance and Performance Responsibilities, the Director of Finance and Performance is responsible for the preparation of the pension fund's financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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 fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance and Performance; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on financial statements

In my opinion the pension fund's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2012 and the amount and disposition of the fund's assets and liabilities as at 31 March 2012; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

Opinion on other matters

In my opinion, the information given in the annual report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

I report to you if, in my opinion the governance compliance statement does not reflect compliance with the Local Government Pension Scheme (Administration) Regulations 2008 and related guidance. I have nothing to report in this respect.

Simon Garlick
District Auditor
Audit Practice of the Audit Commission
Collins House
Bishopstoke Road
Eastleigh
Hampshire
SO50 6AB

27 September 2012

Glossary of terms

Absolute annual investment return
An investment return that is an exact amount, for example 7%, rather than a return compared to a benchmark.

Accrual (to accrue)
An amount to cover income or spending that has not yet been paid but which belongs to that accounting period.

Active members
Members of the pension fund who are currently working and contributing to the fund.

Actuary
An independent consultant who advises the fund and reviews the financial position of the fund every three years.

Actuarial present value of promised retirement benefits
A calculated value for the amount of money needed today to meet the pension payments the fund will make in the future. In calculating this value the actuary takes account of factors such as investment returns, inflation and life expectancy.

Actuarial valuation
A valuation to check that the funding is on track to cover liabilities and review employers' contributions.

Administering authority
The organisation that runs the pension fund.

Admitted organisations
An organisation that takes part in the pension scheme under an 'admission agreement' (that is, an agreement and terms under which they are allowed to join our scheme).

Annualised return
The average yearly return over a period of more than one year.

Asset allocation
The percentage of the fund set aside for each type of investment.

Augmentation
Payments to provide new benefits or improved benefits such as early retirement.

Benchmark
An index (for example, the FTSE 100) or peer group that the fund, or a section of the fund, is measured against to work out whether the fund has performed well.

Bid price
The price at which investments can be sold.

Bid-offer spread
The difference between the bid price and the offer price.

CIPFA
Chartered Institute of Public Finance and Accountancy

Co-investment
Investing alongside someone else in the same investment.

Collateral
Assets placed with a lender as security against a borrower failing to make agreed payments. For example, in the case of a mortgage, the house would usually be the collateral against which the bank lent money to an individual.

Common contribution rate
The normal contributions of member authorities and organisations must meet 100% of benefits. The common contribution rate is the future service cost of members' contributions, including an allowance for expenses.

Corporate governance
The system by which companies are controlled and directed, and the way they respond to their shareholders, employees and society.

Currency hedges
Assets that are owned to reduce the effects of foreign-exchange movements on the fund.

Deferred benefits
Built-up pension rights, for ex-employees, that are kept in the pension fund.

Deferred pension
The pension benefit that is paid from the normal retirement date to a member of the fund who no longer pays contributions as a result of leaving employment or opting out of (leaving) the pension scheme before their retirement age.

Derivatives
A type of investment that is linked to another asset. Examples of derivatives are options, forwards and futures.

Developed markets
Countries that index providers (such as FTSE or MSCI) have decided have strong regulation and large investment markets that are well developed.

Dividend
The distributed profits of a company.

85-year rule
The 85-year rule allows members to retire before 65 without reduced benefits if their age and their service together add up to more than 85.

Emerging markets
Countries that index providers (such as FTSE or MSCI) have decided have weak regulation and new or small investment markets.

Employer of sound covenant
An employer who is unlikely to become insolvent (unable to pay its debts).

Engagement
Discussions between investors or their fund managers and companies about corporate governance or socially responsible investment.

Equities
Ordinary shares in a company.

Ethical investments
Investments that are moral and are not linked to companies that, for example, are involved in trading weapons, exploiting developing countries or contributing to climate change.

Ex-dividend
A share is ‘ex-dividend’ on a date set by a company when current shareholders are entitled to a dividend on their holding. Even if the holding is sold, the previous owner will receive the income. On that date, the market price of a share will be adjusted to reflect the income due to the holder. (For example, a share which goes ex-dividend with a dividend of 10p will see the market price reduce by that amount.) Stock may be sold ex-dividend (without dividend entitlement) or 'cum-div' (with dividend entitlement).

Full-funding basis
When the future value of assets matches the future value of liabilities. At the last actuarial valuation, which was carried out as at 31 March 2007, the fund was 95% funded. This means that the value of the assets was 95% of the estimated value of the liabilities.

Futures or forwards
Buying or selling a package of shares, currency or commodities (for example, coffee or metal) at a specific point in the future at a price agreed when the contract is taken out.

Hedging
A process of reducing or removing the risk of a portfolio by buying or selling assets that act in an opposite way to those already owned.

Historical cost
The amount paid for an investment when it was bought.

Index-linking
When pension benefits are updated in line with inflation.

Liquid assets
Assets that can be sold to provide cash very quickly.

Mandate
An agreement with an investment manager to manage a particular type of asset.

Mid price
The price halfway between the bid price and the offer price.

Myners
Paul Myners was commissioned by the Government to review and report on UK institutional investment.

Option
The right to buy or sell shares within a set timescale at a price confirmed at the time the option is bought.

Over-the-counter trades
A trade for an investment that has not taken place on a stock exchange and has been made to meet the particular needs of the investor.

Passive management or passive investment
Tracking an index and not taking active investment decisions.

Peer group
Other local-authority pension funds.

Pooled investments
Investments where the assets are not held directly by the investors, but are held in a 'pool'. Examples of pooled investments are unit trusts, life funds, open-ended investment companies and limited liability partnerships.

Portfolio
A collection of stocks, shares and other securities.

Preserved benefits
The benefits to which members would be entitled if they left service, based on the service they had completed up to the date they left. As long as members had enough service, the benefits they had earned up to the date they left would be held (preserved) in the fund for them and would be paid when they retired. Between leaving service and retirement, the benefits would be increased broadly in line with price inflation.

Projected unit method
One of the common methods actuaries use to estimate the cost of future benefits from a pension scheme. The method works out the cost of the benefits members are expected to earn over a period (often one year) following the valuation date, allowing for predicted future increases in pay until members retire or leave service. The cost is set out as a percentage of members' contributions. As long as the distribution of members remains stable (that is, new members join the scheme to replace scheme members who have left), the cost is expected to remain stable.

Quantitative analysis system
A computer model to help analyse share holdings and make investment decisions.

Quoted investment
A company listed on a stock exchange.

Realised profit
A realised profit is the profit (or loss) when an investment is sold and is the difference between what it was sold for and what was paid for it.

Recoverable tax
Tax that has been paid but can be claimed back.

Recurring pension
A pension that is paid regularly, usually every month.

Real discount rate
The discount rate is the return that the actuary uses to work out how much money needs to be saved today to pay future liabilities. For example, if the discount rate is 5.25% then you need to save £95 today to have £100 in a year's time. The real discount rate is a discount rate where the effects of inflation have been removed.

Safe custody
The responsibility for keeping the fund's financial assets safe, settling transactions, collecting income, and other procedures relating to investments.

Scheduled organisations
Local-government organisations which have the automatic right to take part in the pension scheme.

Secondary investments
A private equity fund that is bought from an existing investor, rather than being an investor when the fund was first created.

Settle transactions
Swapping money for assets when you buy or sell shares or bonds. Financial assets usually settle two or three days after the trade is agreed.

Shareholder engagement
Where the owners of shares try to influence a company's behaviour by campaigning in the press, voting at company meetings or talking to company managers. Typical issues that might be raised are the company's effect on the environment, their labour standards and pay for the board of managers.

Smoothed market value, smoothing mechanism
Most shares and bonds that the fund owns change value every few minutes and the price can vary quite a lot. The fund's actuary will make an adjustment for this when valuing the fund so that extreme highs and lows are ignored.

Solvency
Whether the assets of the fund are greater than the liabilities.

Specific ethical investment
Investing in companies that do not invest in, for example, the arms trade, third-world exploitation, animal testing or tobacco, or in companies which promote environmentally-friendly products, education and training, waste management and so on.

S&P 500
A broad-based equity index made up of the 500 largest equity stocks quoted in the US.

Statutory instrument
Secondary legislation made by government ministers.

Statutory pension scheme
A pension scheme established by an Act of Parliament and run in line with statutory instruments.

Stock lending or securities lending
Shares owned are lent on the stock market to generate income. The owner keeps all benefits, except for the voting rights.

Tender
A process of assessing and choosing a business to do work on your behalf.

Time-weighted return
Estimating the performance of a fund, taking into account the effect of money coming into, or leaving the fund, during the period of time you are looking at, so those money movements don't give an inaccurate return.

Transfer value
The capital payment made from one pension fund to another when the person paying contributions changes to another pension scheme.

Transition management
Organising the complex movements of assets that happen when a scheme changes its investments or its asset managers.

Unlisted shares
Shares for companies not listed on the stock exchange.

Unrealised loss
An unrealised loss is the loss suggested when an asset was bought for more than it is currently worth, but the loss is not 'available' (or 'realised') until the asset is sold.

Unrealised profit
An unrealised profit is the profit suggested when an asset was bought for less than it is currently worth, but the profit is not 'available' (or 'realised') until the asset is sold.

Venture capital
Investments in small companies that are not listed on a stock exchange.

Vested benefits
Benefits due now and in the future to members of the fund that are already drawing their pension.

WM Company
The company appointed by most local authorities to collect performance statistics.

Yield
The yearly interest paid by a bond divided by its price. When we refer to yields, this usually means the yield on UK government bonds.

Contacts

If you would like more information, please contact one of the following people.

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• The actuary	Graeme Muir Barnett Waddingham 163 West George Street Glasgow G2 2JJ Phone: 0141 243 4400
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The pensions committee page of the Somerset County Council website is available using the following link. You will find all of the committee's papers and minutes on this page.

http://www1.somerset.gov.uk/council/boards.asp?boardnum=26

These accounts are also available on the internet at.

http://www.somerset.gov.uk/irj/public/services/directory/service?rid=/wpccontent/Sites/SCC/Web%20Pages/Services/Services/Resources/Pensions%20-%20Pension%20Fund%20Accounts

These accounts are also available in Braille, in large print, on tape and on CD and we can translate them into different languages.

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