

LGPS fund accounting – 2013-14

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What we're going to cover today

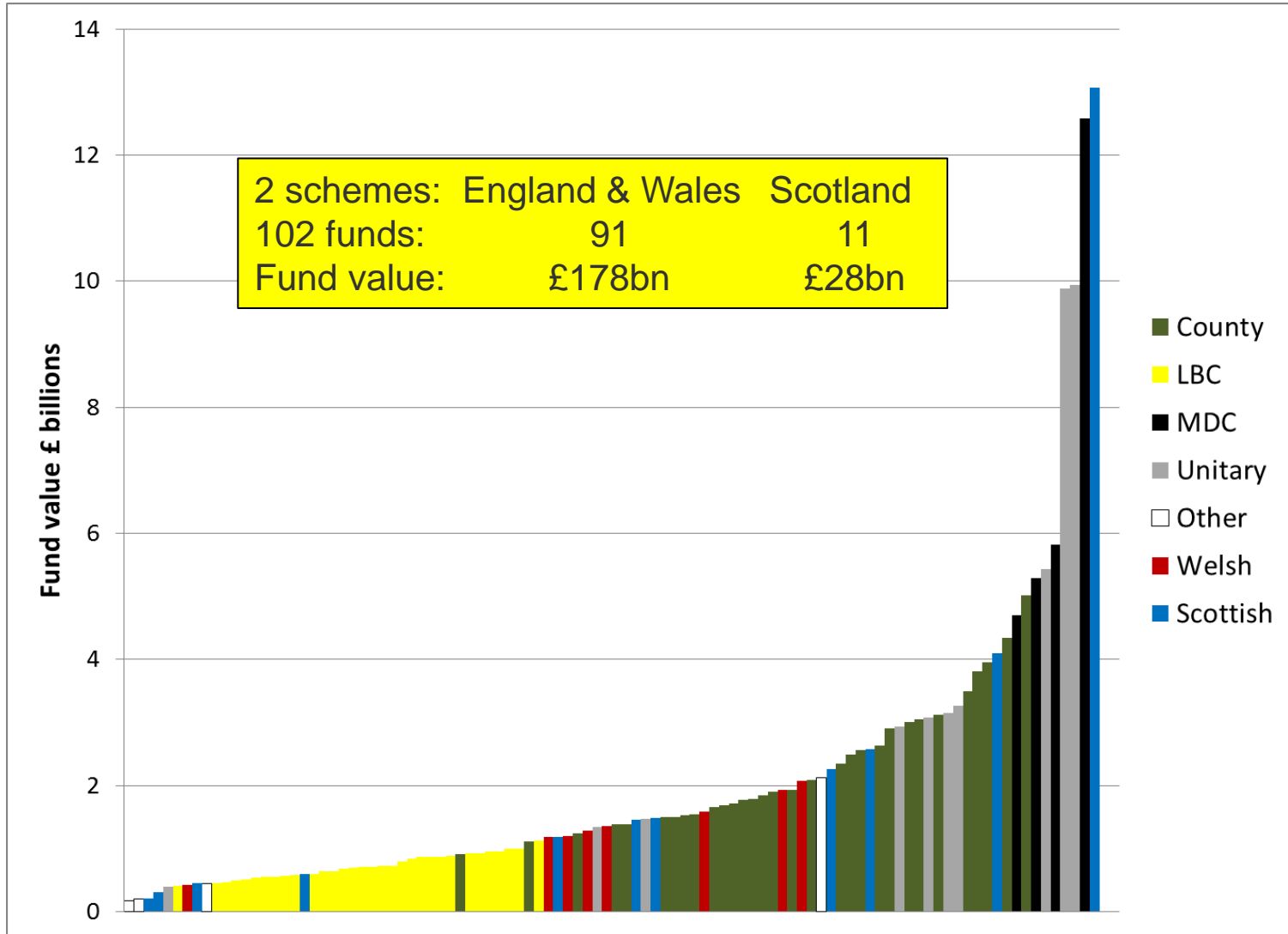
■ Setting the scene

- Financial Reporting framework
- The Pension Fund Accounts
- Fund Account
- Net Assets Statement
- Disclosures
- Annual Report

Overview
Key players
Regulation



2 schemes, 102 Funds



Source: LGPS audited a/cs 2012/13

Pension fund overview



Fund Account

Dealings with members, employers and others directly involved in the fund

Contributions	(191,262)
Transfers in from other pension funds	(25,358)
Benefits	232,580
Payments to and on account of leavers	48,896
Administration expenses	5,970
Net (additions) / withdrawals from dealings with members	<u>70,946</u>

Minimum disclosure
Supporting disclosure
notes

Returns on investments

Investment income	(52,660)
Taxes on income	773
Profit and losses on disposals & changes in MV of investments	(300,444)
Investment management expenses	7,300
Net return on investments	<u>345,031</u>
Net (increase) / decrease in net assets available for benefits during the year	<u>(274,085)</u>

Net Assets Statement (NAS)

Net Assets Statement

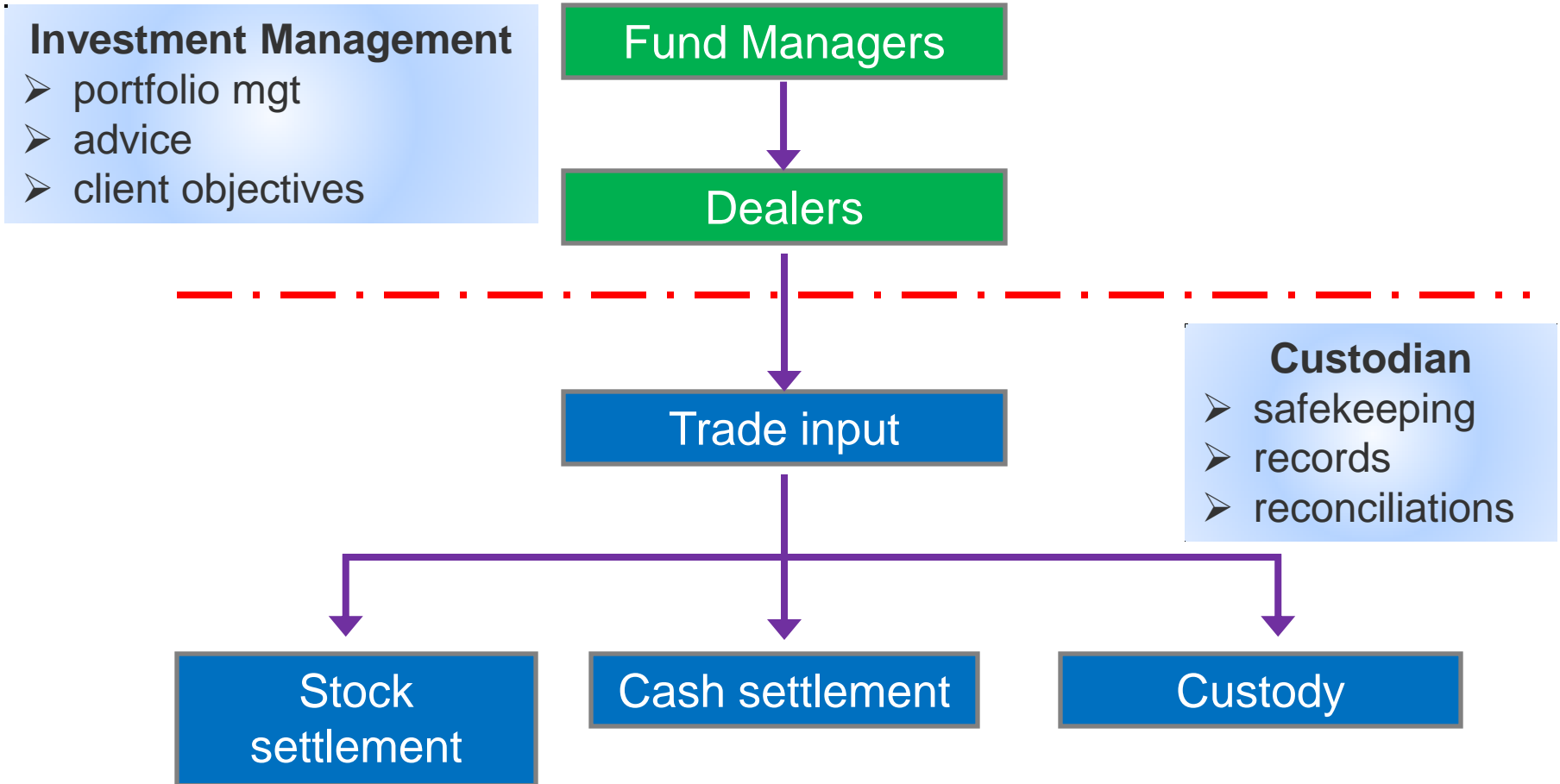
Investment assets		4,403,074
Cash deposits	Minimum disclosure	12,850
	Supporting disclosure notes	4,415,924
Investment liabilities		(11,051)
Borrowings		(436)
Current assets		104,178
Current liabilities		(11,506)
Net assets of the fund available to fund benefits at the period end		4,497,109

Meet the key players

- Investment Manager
- Custodian
- Pensions administrator
- Pensions Panel – Members (“Trustees”)
- Actuary
- Independent Investment Advisor



Investment Manager & Custodian



- Triennial/annual funding
- Rates & Adjustment certificate
- IAS19/FRS17
- Asset liability modelling

Valuation

- Common rate to secure solvency
- As nearly a constant rate as possible
- Funding Strategy Statement

Regulatory requirements

AON Hewitt

MERCER

Barnett
Waddingham

HYMANS  ROBERTSON

Process

Assumptions

- Data download
- Consistency/validation checks
- Report back

- Discount rate
- Inflation
- Pay
- Longevity
- Investment return

Regulatory environment

Superannuation Act 1972		Public Service Pensions Act 2013
To 31 March 2008	From 1 April 2008	From 1 April 2014
<ul style="list-style-type: none"> Local Government Pension Scheme Regulations 1997 30+ amendment Regulations 	<ul style="list-style-type: none"> LGPS (Administration) Regulations 2008 LGPS (Benefits, Membership and Contributions) Regulations 2007 	<ul style="list-style-type: none"> Local Government Pension Scheme Regulations 2013
<p>Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009</p>		

Other regulation (1)

Pensions Act 1993, 1995 & 2004

- Created new regulator - The Pensions Regulator (replaced OPRA)
- Occupational schemes generally
- Currently has restricted application to the LGPS – Internal Dispute Resolution Procedure required for each fund
- Public Service Pensions Act 2013 extends role from April 2015
- Consulted (December 2013) on
 - Draft Code of Practice – Governance and Administration for Public Service Pension Schemes
 - Draft Regulatory Strategy



Other Regulation (2)

Financial Services & Markets Act 2000, Financial Services Act 2012

- Financial Services Authority replaced 2013 by:

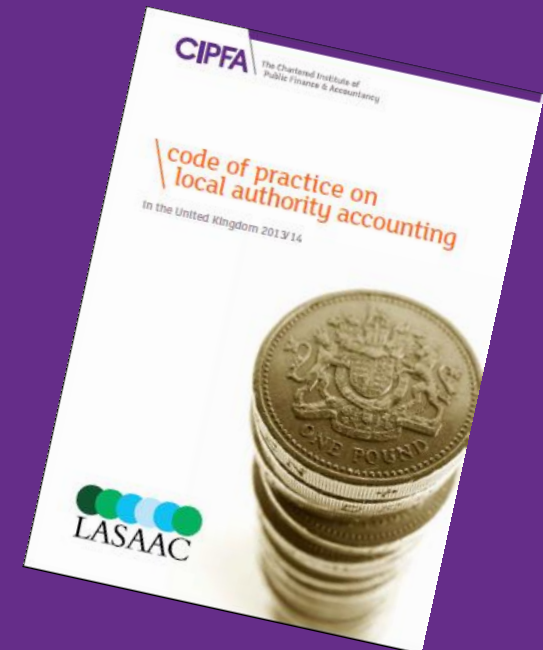
	Prudential Regulatory Authority	Financial Conduct Authority
Regulates & supervises	Banks, building societies, credit unions, insurers, major investment firms	26,000 financial advisory firms
	Part of Bank of England	Independent
Authorisation	Authorises firms & approved persons	Authorises firms Register firms
Supervision & regulation	Risk-based approach	FCA Handbook

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Code application of IAS 26

Accounting and Reporting by Retirement Benefit Plans

IAS 26	Code adaptation
Valuation of financial instruments	
Market value	Bid price (IAS 39)
Analysis of investment assets and income	
assets to be “suitably classified”	Follow Pension SoRP
AVCs	
Not covered	Disclosure note only
Actuarial present value of promised retirement benefits	
Measure at current salary levels or projected salary levels	Projected salary levels

The accounts in summary

	Where in the Code?
Fund Account	
Layout & content (incl. IAS 19 requirements)	6.5
Net Assets Statement	
Layout & content	6.5
Disclosures	
IAS 26 specific disclosures	6.5
Accounting Policies	3.3 & 3.4
Debtors	5.4
Creditors	8.2
Financial instruments	7.4 + IFRS 7
Related party transactions	3.9 + IAS 24

Dealings with members, employers and others directly involved in the fund

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Investment reconciliation table

Analysis as
per NAS?



	Market value 1 April 2011 £'000	Purchases during the year and derivative payments £'000	Sales during the year and derivative receipts £'000	Change in market value during the year £'000	Market value 31 March 2012 £'000
Fixed Interest Securities	330,390	1,734,605	(1,656,820)	8,497	416,672
Equities	1,080,286	615,147	(585,803)	73,426	1,183,056
Pooled investments	1,794,391	942,834	(1,026,759)	157,860	1,868,326
Pooled Property investments	152,613	153,661	(152,853)	769	154,190
Private Equity/infrastructure	343,132	226,335	(185,628)	36,641	420,480
Property	364,001	10,548	(42,397)	8,087	340,239
Derivative contracts:					0
• Futures	1,495	5,160	(3,939)	(1,567)	1,149
• Purchased/Written Options	(117)	3,517	(4,565)	1,735	570
• Forward Currency Contracts	(18,072)	97,518	(90,426)	10,628	(352)
	4,048,119	3,789,325	(3,749,190)	296,076	4,384,330
Other Investment Balances:					
Cash deposits	108,959			12,368	12,850
Amount receivable for sales of investments	21,681				2,741
Investment income due	-				7,608
Amounts payable for purchases of investments	(2,125)				(2,656)
Net investment assets	4,176,634			308,444	4,404,873

Total agrees to
Fund A/c?



Comparator
table?

Balances should
agree to NAS



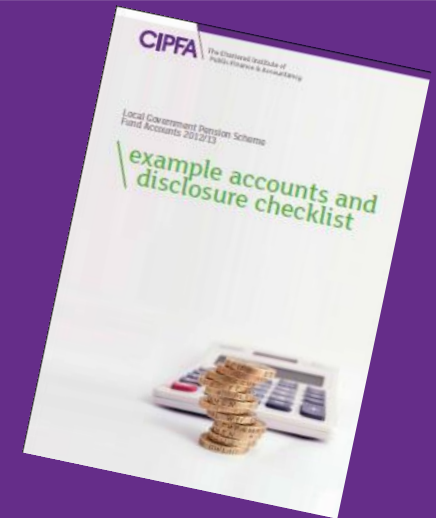
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- Setting the scene
- Financial Reporting framework

▪ The Pension Fund Accounts

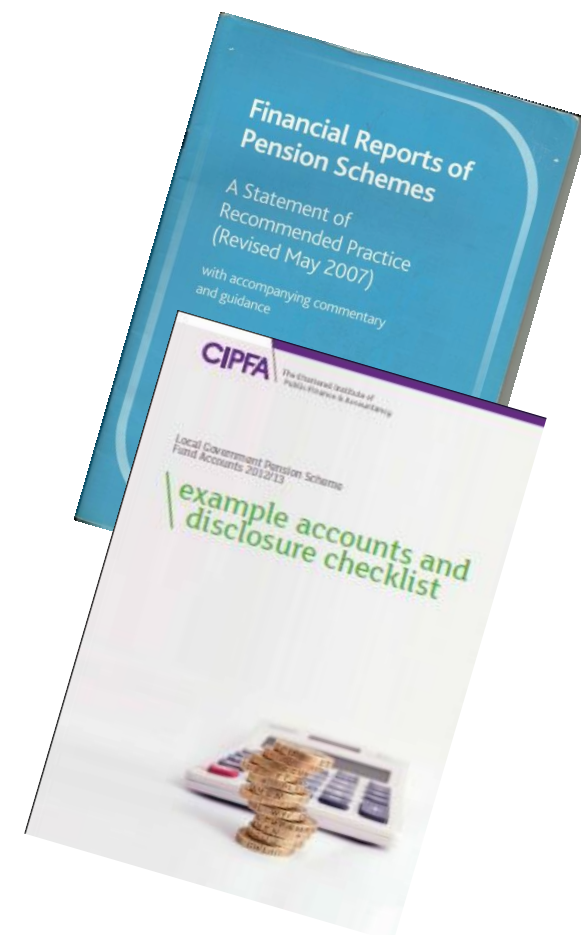
- Fund Account
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Basis of preparation
Valuation
Transaction costs
Future benefits
Accounting policies



Basis of preparation

- Accruals
- Current version of the Code of Local Authority Accounting Practice in the United Kingdom
 - **NOT** the Pension SoRP!
- Underpinned by Local Government Pension Scheme (Management & Investment of Funds) Regulations 2009



Valuation principles

Investment	Class	Measurement	Examples
Property		Fair value	Direct property
Financial assets	Loans & receivables	Amortised cost	Debtors
	Fair value through P&L	Fair value	All other inv'ts +ve derivatives
	Available for sale	N/A	
	Held to maturity	Code does not permit	
Financial Liabilities	Amortised cost	Amortised cost	Creditors, loans
	Fair value through P&L	Fair value	-ve derivatives

less

Due diligence req'ts

more

Easy to price, there is a liquid market for these securities

- UK and overseas equities
- Bonds
- Forwards and futures
- Deposits and short term investments
- Pooled investment vehicles invested in the above

1

Moderately difficult to price, limited visible market parameters

- Credit default, inflation, interest rate and other swaps
- Options
- Unquoted pooled investment vehicles
- Property
- Liquid asset backed securities (ABSs) and bonds
- Hedge funds
- Hedge fund of funds
- Pooled investment vehicles invested in the above

2

Difficult to price, lack of a liquid market, difficult to verify parameters used in valuation

- Structured investment vehicles (SIVs)
- Unquoted private equity investments
- Pooled investment vehicles invested in the above

3

Transparency

opaque

Reporting future retirement benefits

Objectives of IAS19 and FRS17:

1. Statements show fair value of assets & liabilities relating to members from that employer
2. Operating costs of providing retirement benefits recognised as earned & related finance costs etc recognised as they arise
3. Disclosure of costs of providing benefits & related gains, losses, assets & liabilities

Different reporting requirements

Pension Fund a/cs

3 options:

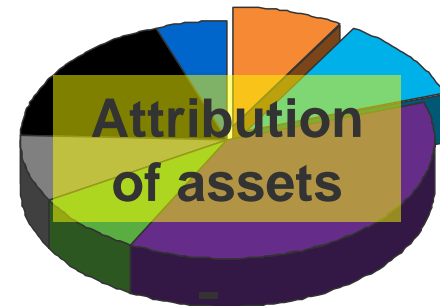
- A. In Net Assets Statement
 - B. In the notes to the a/cs
 - C. Cross referred to actuarial report
- If using A:
 - need to compare assets with liabilities at the same date
 - Analysis of movement in IAS 19 assets & liabilities **NOT** disclosed
 - Will need actuarial valuation of all pension liabilities including smaller bodies

LG employer a/cs

- IAS 19 charge recognised in CIES
- Statutory override applied for council tax charging:
 - IAS 19 charge transferred to Pension Reserve via MiRS
 - Replaced by actual contributions payable to pension fund
- Disclose analysis of movement in IAS19 assets & liabilities

FRS 17/IAS19 – an employer issue

- Each body accounts for its own share of assets/liabilities & pension costs
- Actuary estimates assets & liabilities for employers
- Methodology:
 - Roll forward membership data from last triennial funding valuation
 - Different assumptions to funding valuation
 - Key difference is discount rate
- Pension fund involvement:
 - Providing data on cashflows
 - Not all employers have same year-end



=

Net asset/liability

Accounting policies

- Code requires a summary of significant accounting policies
- May be different from single entity a/cs

Specific issues:

- Estimation uncertainty
 - Disclose material estimations
 - Separate note or information in specific notes
 - Not required for balances at fair value based on recent market prices
- Significant judgments
 - In applying accounting policies
 - “significant” effect on the accounts
- Future changes in accounting policies



What we're going to cover today

- Setting the scene
- Financial Reporting framework
- The Pension Fund Accounts

■ Fund Account

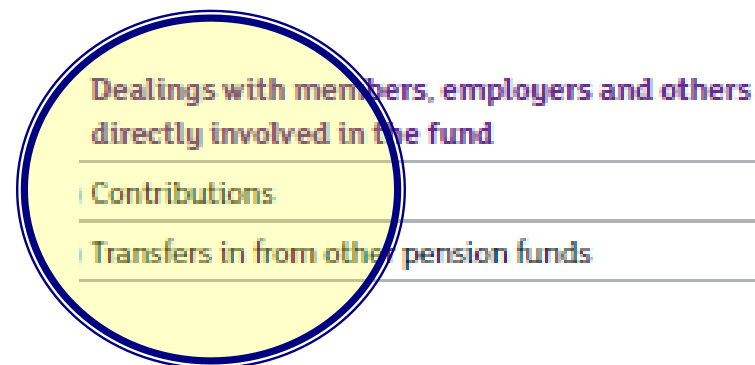
- Net Assets Statement
- Disclosures
- Annual Report

2011/12		2012/13
£000	Notes	£000
Deals with members, employers and others directly involved in the fund		
(193,229)	Contributions	(216,476)
(34,454)	Transfers in from other pension funds	(25,238)
(227,693)		(241,714)
226,858	Benefits	232,580
29,536	Payments to and on account of leavers	48,896
5,833	Administration expenses	5,970
256,227		287,446
28,534	Net (additions)/withdrawals from dealings with members	45,732
Returns on investments		
(39,167)	Investment income	(52,660)
	604 Taxes on income	773
	Profit and losses on disposal of investments and (820,896) changes in the market value of investments	(300,444)
8,175	Investment management expenses	7,300
851,284	Net return on investments	345,031
(822,750)	Net (increase)/decrease in the net assets available for benefits during the year	(299,299)

Contributions receivable

Includes:

- Employers - includes:
 - Normal - individual to employer
 - Augmentation
 - Deficit funding
- Employees
 - banded rates
 - Employers determine banding before the financial year



Include: Added years AVCs

Exclude: Money purchase AVCs

Pension fund strain - what is it?

**Pay retirement
benefits early**

**Enhanced
retirement
benefits?**

**Loss of ees & ers
contributions**

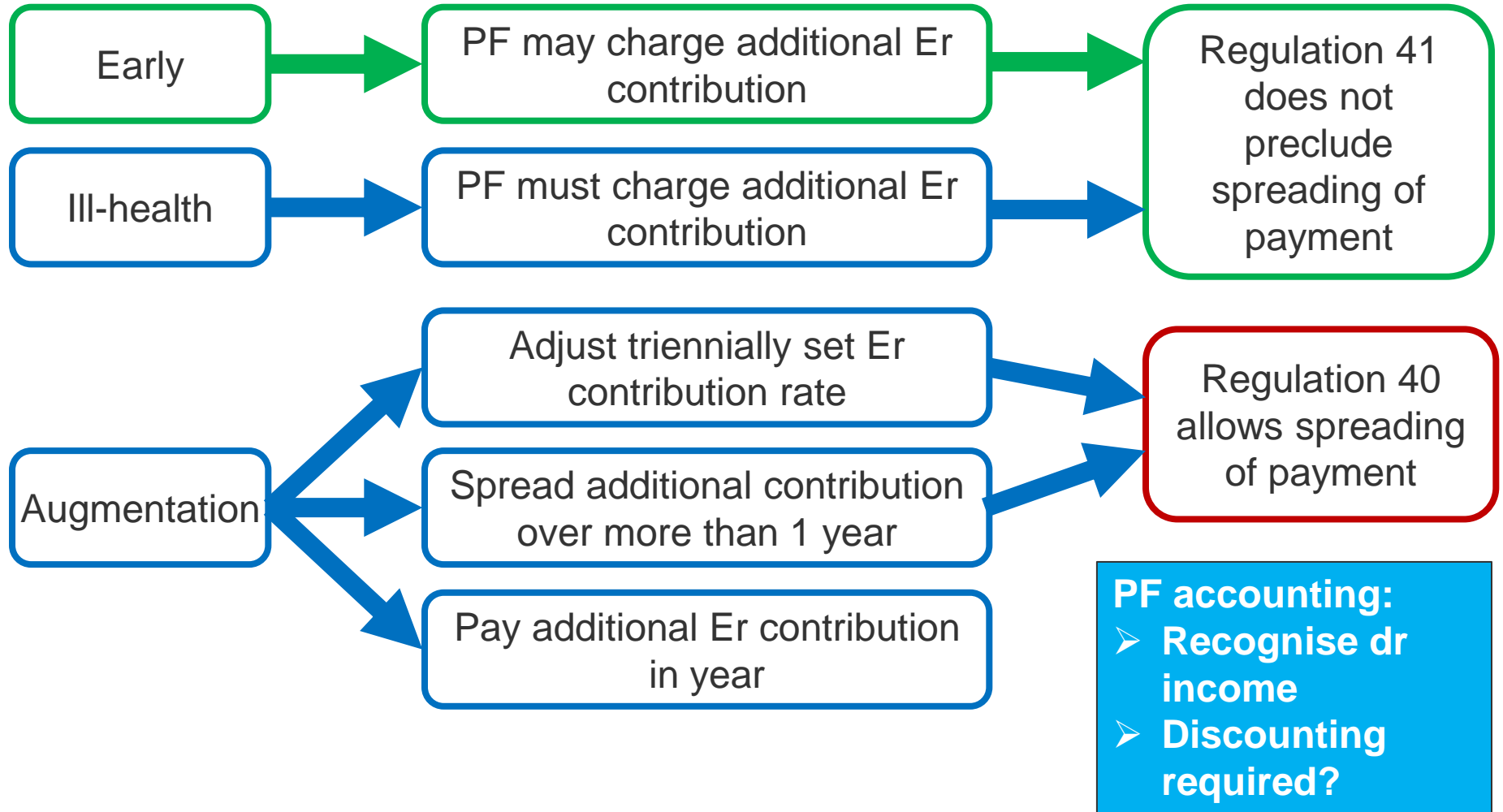
**Loss of investment
return**

“Pension Strain”

Recovery of strain from employer depends on benefit provided:

- Include in next triennial funding
- Additional employer's contribution in year
- Additional employer's contribution spread more than 1 year

Pension Strain: When are contributions payable?



PF accounting:

- Recognise dr income
- Discounting required?

Additional Voluntary Contributions

- a member may elect to pay AVCs
 - Reg 15 LGPS (Benefits, Membership & Contributions) Regs 2007
- Employer to notify administering authority
- Administering authority ensure paid over

Reg 25 LGPS
(Admin) Regs
2008

N.B. Money purchase AVCs still have to be included as disclosure note to pension fund accounts

Employer/ee contributions

What systems of control might I expect?

- At pension fund administering authority
 - Exception testing
 - Holding a/cs by employer
 - Monitoring against forecast levels of income per employer
 - Testing by internal audit at employers & admin authority
- At employer body
 - DoF certification
 - Payroll exception reporting
 - Testing by internal audit

Transfers in & out

	Individual	Bulk
Example	Employee tsfrs to another LA/admitted body	Group of employees trsfr to another body eg LSVT
Accounting	Cash	Accrual
Valuation	Standard actuarial formula	Actuarial valuation

Accounting policy disclosed?

Benefits payable

- Pensions
- Lump sums on retirement
- Lump sum death benefits

2011/12		2012/13
£000		£000
185,417	Pensions	189,193
38,864	Commutation and lump sum retirement benefits	38,621
2,577	Lump sum death benefits	4,762
226,858		232,576

Lump sums

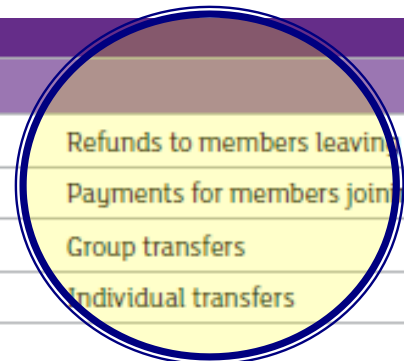
- On retirement
 - Lump sum plus ongoing pension
 - Lump sum maybe called 'retirement grant'
 - Commutation of pension into lump sum
- On death in service
 - Lump sum/death grant
 - Survivor's pension

Based on actual date of retirement or death

Payments to and on behalf of leavers

- Refund of contributions
- Purchase of annuities to match preserved benefits
- Group transfers out
- Individual transfers out

2011/12	
£000	
48	Refunds to members leaving service
3	Payments for members joining state scheme
9,182	Group transfers
14,303	Individual transfers
23,536	



Refunds of contributions

What is covered:

- Leave with less than 2 years membership
 - Refund ee's contributions, net of tax
 - May have option to retain benefits in scheme
 - May have option to transfer to another arrangement

Accounting:

- Apply IAS 37

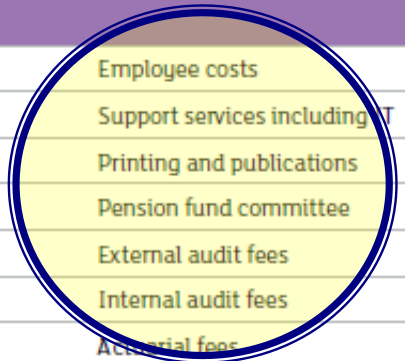
Administrative and other expenses

- Premiums on term insurance policies
- Administration fees
 - In-house costs:
 - CECs
 - Overhead recovery
 - Out-sourcing
- Actuarial fees
- Legal and other professional fees
 - **NOTE** excludes investment advisors fees!

Reliability of systems?

SERCOP compliant?

2011/12	
£000	
3,850	Employee costs
1,683	Support services including IT
40	Printing and publications
63	Pension fund committee
98	External audit fees
67	Internal audit fees
32	Actuarial fees
5,833	



Returns on investments

- Investment income
- Change in market value of investments
- Investment managers' expenses

Returns on investments		
(39,267)	Investment income	12 (52,660)
604	Taxes on income	13 773
(82,896)	Profit and losses on disposal of investments and changes in the market value of investments	15a (300,444)
8,175	Investment management expenses	14 7,300
851,284	Net return on investments	345,031

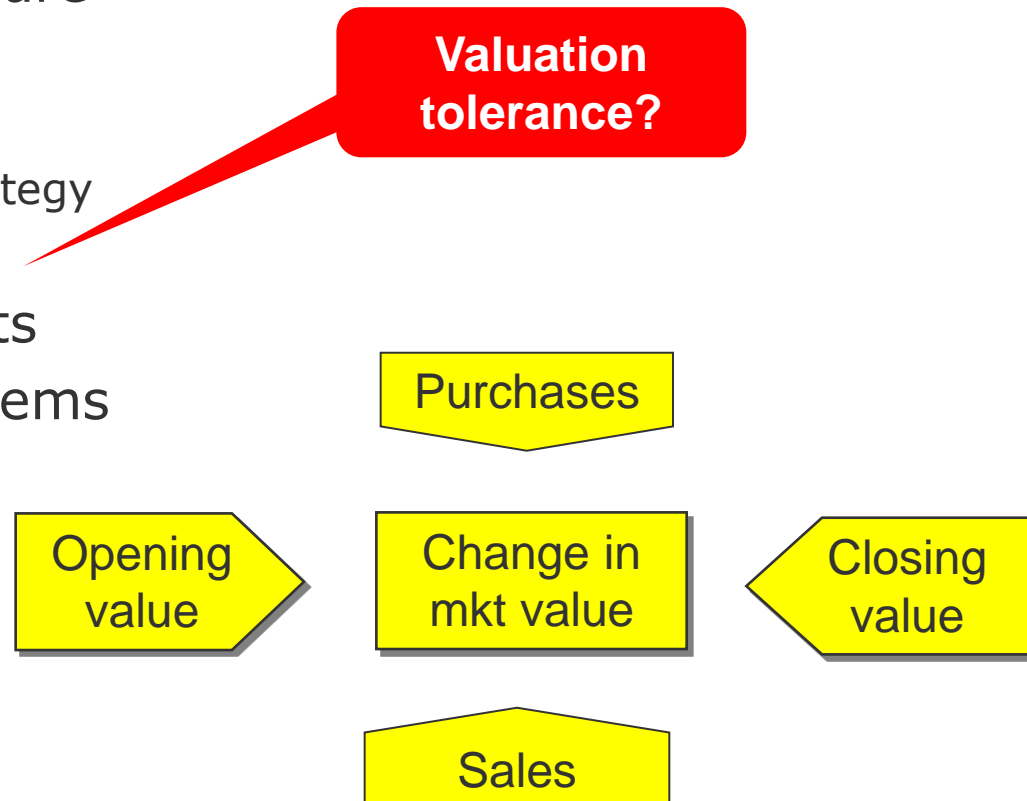
Investment income

- Fixed interest securities
- Equities
- Index-linked securities
- Private equity
- Hedge funds
- Pooled investment vehicles
- Property rentals
- Interest on cash deposits
- Share of profits/losses of associates & JVs
- Income from derivatives

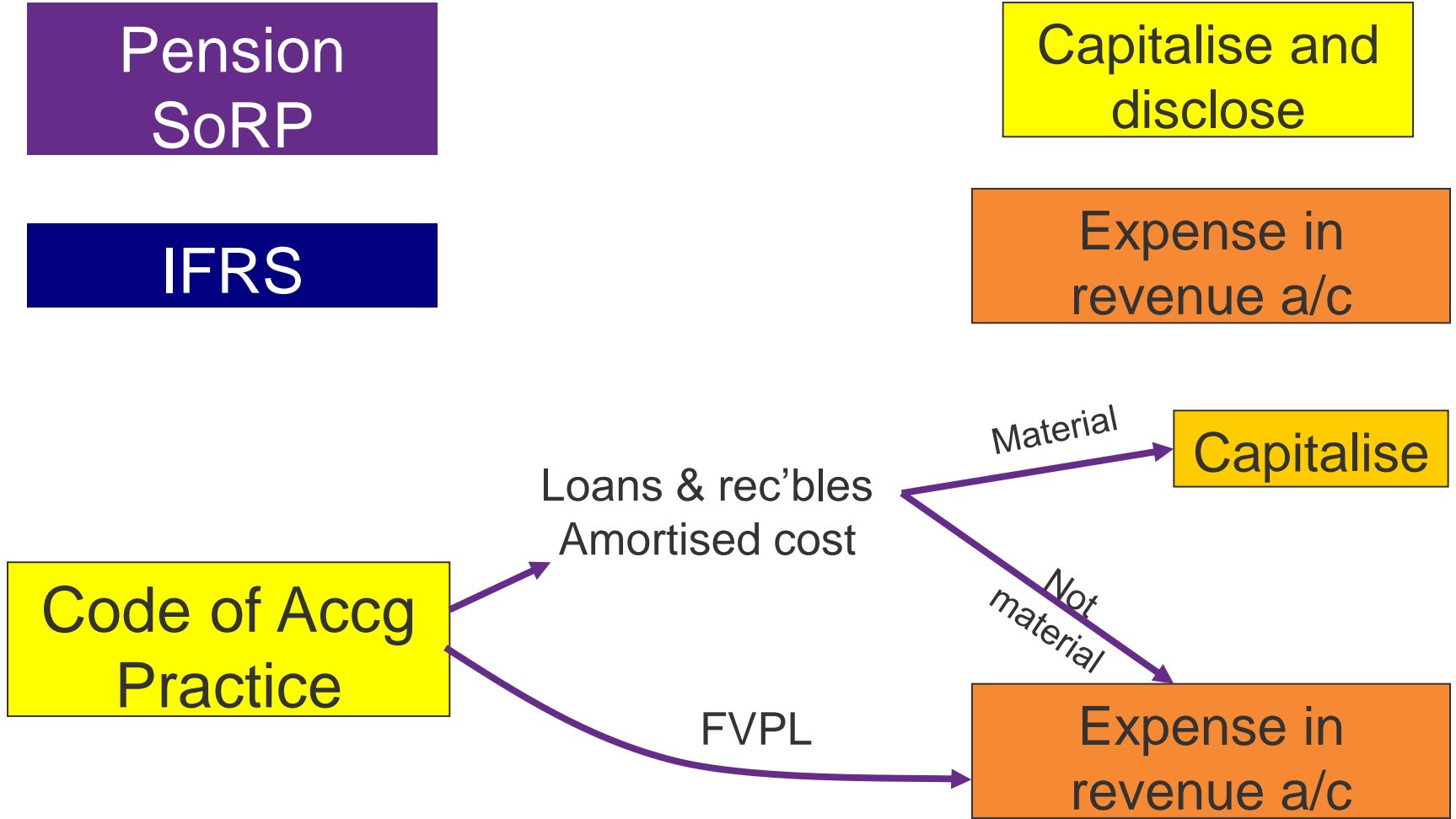
Source:
Custodian
CREST/Euroclear

Change in market value

- Not just 'the balancing figure'
- Reasonableness check
 - Use market indices
 - In line with Investment Strategy
- Agree movements to manager/custodian reports
- Investigate 'reconciling' items



Investment management expenses - principles



Investment managers expenses

Issues

- But where to disclose?
 - Code only has one line – Administrative expenses
 - Example accounts has extra line - Investment Management expenses

- Accruals basis
- Risk of understatement due to netting
- Challenges:
 - Market linked fees
 - Performance fees
 - Embedded fees
 - Private equity & opaque pricing
- Inconsistent reporting
 - lack of inter-fund comparability
 - impact for benchmarking

Area of close
external scrutiny

Investment management expenses - a way forward

What to do now

- Gross up fees and investment income
- Request information from fund managers, brokers etc
- Disclose either:
 - 1 line per the Code plus disclosure note(s)
 - 2 lines per example accounts plus disclosure note(s)

For the future – new CIPFA guidance

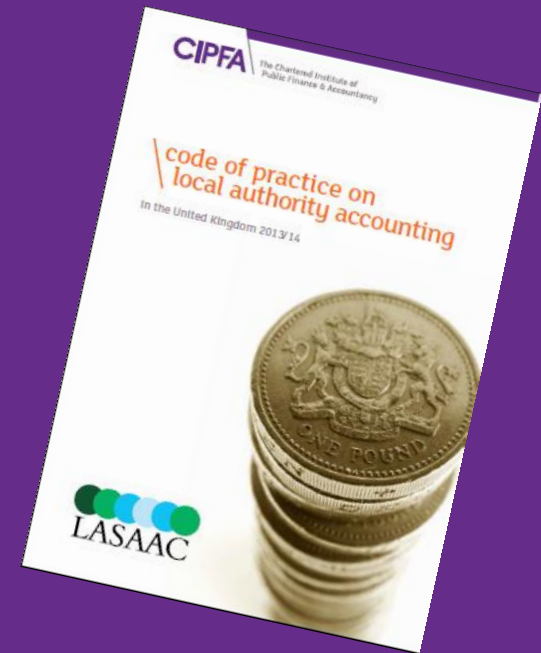
- 3 categories of expense
 - Pensions administration
 - Oversight and governance
 - Investment management expenses
- Expected summer 2014 for implementation 2014/15

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■ Net Assets Statement

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Investments
Property
Derivatives
Unquoted investments

Investments - generally

- Include at market value at date of net assets statement
- Adequate accounting policy disclosure
- Fair value measurement:
 - Level 1 – quoted prices in active markets
 - Level 2 – inputs observable directly or indirectly
 - Level 3 – inputs not based on observable market data

Securities and pooled investment vehicles

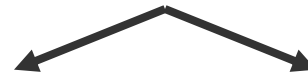
<ul style="list-style-type: none">▪ Quoted securities<ul style="list-style-type: none">▪ At closing price▪ Ex-dividend▪ 'Clean' fixed interest valuations	Level 1
<ul style="list-style-type: none">▪ Unquoted securities<ul style="list-style-type: none">▪ Estimated fair value▪ Disclose basis	Levels 2 or 3
<ul style="list-style-type: none">▪ Pooled investment vehicles (unit trusts, managed funds etc)<ul style="list-style-type: none">▪ closing bid price	Level 1 or 2

Property

Directly held

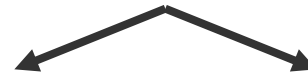
Open market value
Even if occupied by
administering authority or
other admitted body

Either



Pooled investment
vehicles

Valued at



Closing bid price
If available

- External/independent valuation periodically
 - Depending on significance to investment portfolio
- Disclose basis used

Investment property

- Only applies to property held directly
- Disclosure requirements (Code section 4.4.4):
 - rental income in Fund A/c
 - direct operating expenses in Fund A/c
- Also where not separately disclosed:
 - any restrictions in disposal
 - contractual obligations
 - include in investment reconciliation
- Meet “held for sale” criteria
 - Disclose in current assets as “Investment property held for sale”
 - Disclose effects of disposal



Miscellaneous

- Insurance policies
 - Rare in LGPS
- Other
 - Works of art
 - Cash
 - Loans

Valuation? Auction house

Separate bank a/c?
Risk of co-mingling
Balance per Investment Strategy

Limited to:

- Change of fund manager
- Cashflow shortfalls
- 90 days maximum

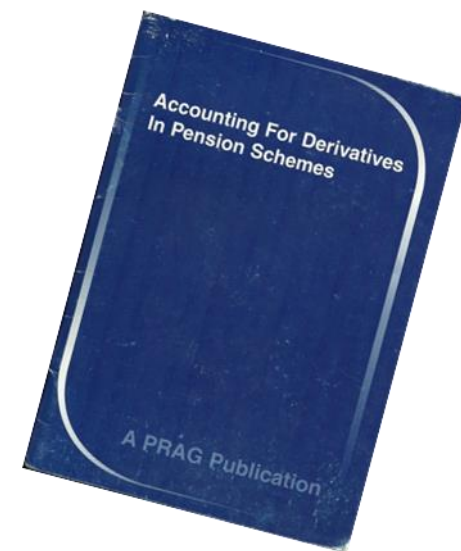
- What are they?
 - Financial contract between two parties that derive its value from the price of an underlying item
 - No/minimal initial investment required
 - Settled in the future
- Part of portfolio management
 - Matching long or short positions to underlying investment sectors
- Hedging against risk

Underlying	Exchange traded derivative (ETD)	Over the counter (OTC)
Exchange rate		Forward foreign exchange
Interest rate		Swaps
Equity price	Futures	
Security price	Options	Options

Increasingly difficult to measure

Accounting framework

- Derivatives stated at fair value
 - Total exposure to the stock market of the contract
 - Quoted market price of the contract, averaged by reference to all other contracts, weighted by lot size
 - Increase/decrease whether long (buy) or short (sell)
- Cash backing open futures positions
- Should be reported gross
- Separate asset classes in net asset statement – no offset of assets and liabilities
- Comprehensive description of derivative terms in notes to the accounts
- Include in investment risk disclosures and pricing hierarchy analysis (levels 1, 2 and 3)



Forward Foreign Exchange

Two parties agree to **exchange currencies** on a **specific future date** at an **agreed rate of exchange**

Characteristics:

- OTC contract – each is potentially unique
- No commission payable – normally
- No margin receipts/payments
- Settled on a gross basis on settlement date
- No collateral
- Value calculated using published market information on forward foreign exchange rates

Forward Foreign Exchange – worked example

Trade date	Sell currency	Sell Nominal	Buy currency	Buy nominal	opening rate	settlement date	revaluation rate	currency sold (in buy currency)	Unrealised profit/(loss) (in buy currency)	Unrealised profit/(loss)
16/03/0X	GBP	18,220,318	EUR	29,132,000	0.62544	09/04/0X	0.62184	29,300,653	(168,653)	(104,875)
05/03/0X	EUR	117,251,000	GBP	74,209,353	1.580003	09/04/0X	1.60813	72,911,394	1,297,959	1,297,959
15/03/0X	GBP	15,047,400	EUR	23,999,809	0.62698	10/04/0X	0.62184	24,198,186	(198,377)	(123,359)
29/03/0X	EUR	24,000,000	GBP	14,739,208	1.62831	10/04/0X	1.60813	14,924,167	(184,958)	(184,958)
										884,766

What is reported?

Forward Foreign Exchange – worked example

Investment manager report

Trade date	Sell currency	Sell Nominal	Buy currency	Buy nominal	opening rate	settlement date	revaluation rate	currency sold (in buy currency)	Unrealised profit/(loss) (in buy currency)	Unrealised profit/(loss)
16/03/0X	GBP	18,220,318	EUR	29,132,000	0.62544	09/04/0X	0.62184	29,300,653	(168,653)	(104,875)
05/03/0X	EUR	117,251,000	GBP	74,209,353	1.580003	09/04/0X	1.60813	72,911,394	1,297,959	1,297,959
15/03/0X	GBP	15,047,400	EUR	23,999,809	0.62698	10/04/0X	0.62184	24,198,186	(198,377)	(123,359)
29/03/0X	EUR	24,000,000	GBP	14,739,208	1.62831	10/04/0X	1.60813	14,924,167	(184,958)	(184,958)
										884,766

Fund A/c

Change in market value £ **884,766**

Net assets statement

Financial assets	
Forward foreign exchange	1,297,959
Financial liabilities	
Forward foreign exchange	(308,317)
Cash	(104,875)
	989,641

First contract closed

Investment reconciliation table

	b/f	Payments	Receipts	Change in market value	c/f
Forward foreign exchange	0	18,220,318	(18,115,443)	884,766	989,641

Forward foreign exchange

	Opening market value £000	Purchases / derivative payments £000	Sales / derivative receipts £000	Change in market value £000	Closing market value £000
Fixed interest	620,234	451,466	(495,134)	30,536	607,102
Equities	267,345	45,234	(34,245)	104,256	382,590
Derivatives:					
Foreign exchange forwards	3,049	1,751,345	(1,752,312)	2,100	4,182
Interest rate swaps		350,000	(350,000)	15,234	15,234
Futures	51,234	341,000	(332,095)	-	60,139
	941,862	2,939,045	(2,963,786)	152,126	1,069,247
Cash	(52,347)			2,434	(58,299)
Total	889,515			154,560	1,010,948

Is it likely that a pension scheme with £1 billion of assets has had cash outflows of £1.7 billion of foreign exchange?

Forward foreign exchange

What is the custodian/fund manager doing?

- There is no cost to enter into a foreign exchange contract
- But to record the contract on the valuation system, both legs of the contract are entered
- This allows the fund manager/custodian to value the contract
- Most custodians/fund managers account for forward foreign exchange contracts in this way and most 'Pension SoRP' reports provided have this grossing up issue
- The custodians will usually provide a report to 'correct' the accounting entries that have been made

Derivative accounting - futures

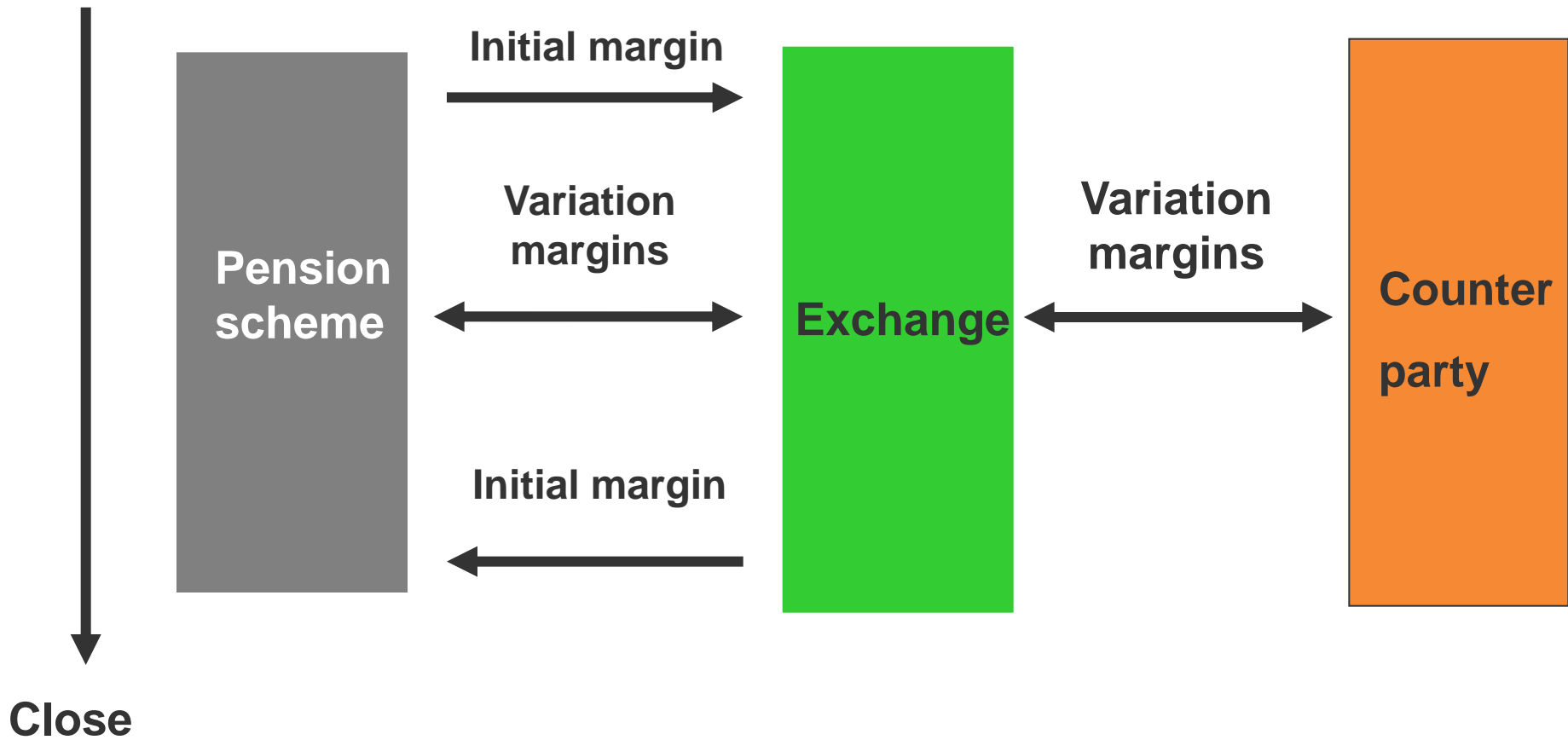
Two parties agree to buy/sell a standard specified nominal amount of an asset at a specified price in the future at a price specified today

Characteristics

- ETD contracts
- no initial consideration so no purchase cost
- initial and variation margin cash movements are transfers between cash/amounts due to/from brokers
- unrealised gains/losses = typically variation margin cash movements over life of contract
- gains and losses are unrealised until the contract is closed out
- no sale proceeds
- economic exposure in notes to accounts

Futures – focus on cash flows

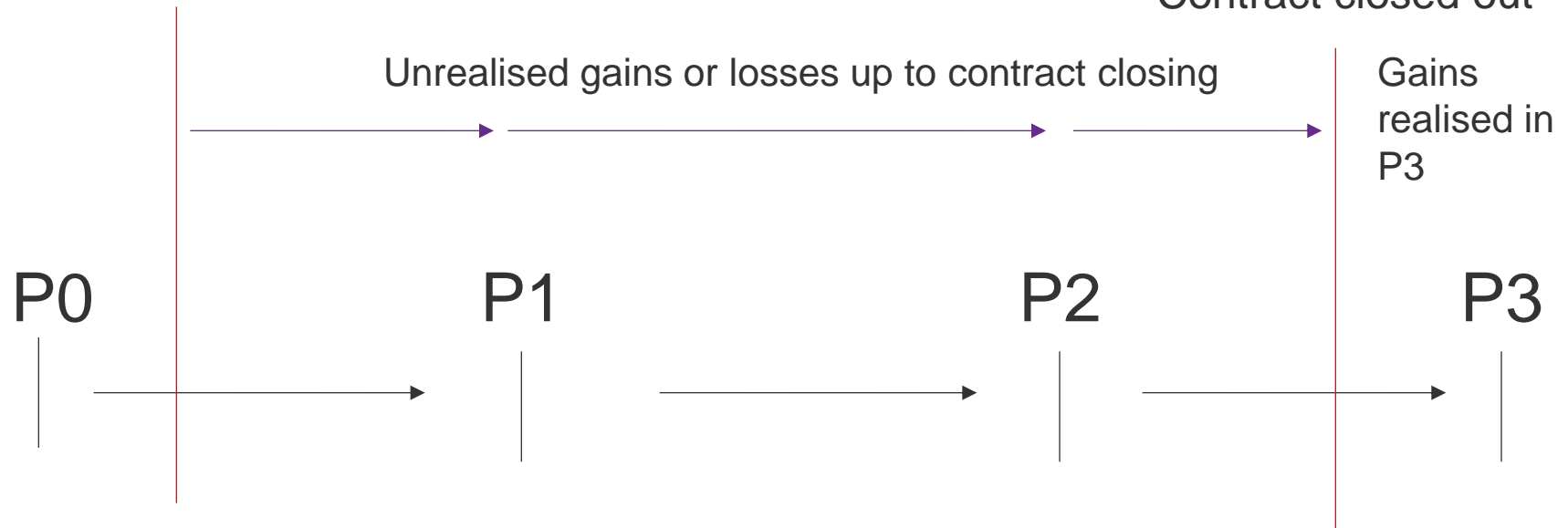
Inception



Variation margins, gains and losses

Contract entered

Contract closed out



Cash flows

Initial margin on inception of contract paid to exchange

Variation margin at end of P1 (to)/from exchange

Variation margin at end of P2 (to)/from exchange

Final variation margin to/from exchange and return of initial margin

	Opening market value £000	Purchases / derivative payments £000	Sales / derivative receipts £000	Change in market value £000	Closing market value £000
Fixed interest	620,234	451,466	(495,134)	30,536	607,102
Equities	267,345	45,234	(34,245)	104,256	382,590
Derivatives:					
Foreign exchange forwards	3,049	1,751,345	(1,752,312)	2,100	4,182
Interest rate swaps	-	350,000	(350,000)	-	60,139
Futures	51,234	341,000	(332,095)	-	60,139
	941,862	2,939,045	(2,963,786)	152,126	1,069,247
Cash	(52,347)			2,434	(58,299)
Total	889,515			154,560	1,010,948

- There are two problems here which are very much linked – a large market value for the futures and a large negative cash balance or investment creditor.
- Another issue you may also see is futures with a £Zero market value.
- What is going on?

Derivatives – Risks

- Grossing up of legs of derivative contracts
- 'Simplified' futures accounting
- Economic exposure reporting of derivatives by investment managers/global custodians
- Lack of information on collateral positions/valuations
- Collateral re-hypothecation accounting implications
- Opaque/hard to understand reporting by investment managers/global custodians
- New types of derivative products – eg longevity swaps
- Lack of understanding of derivative products by investment accounting service providers

Unquoted investments – what are they?

“dealt in the market but are not subject to any listing requirements and are given no official status”

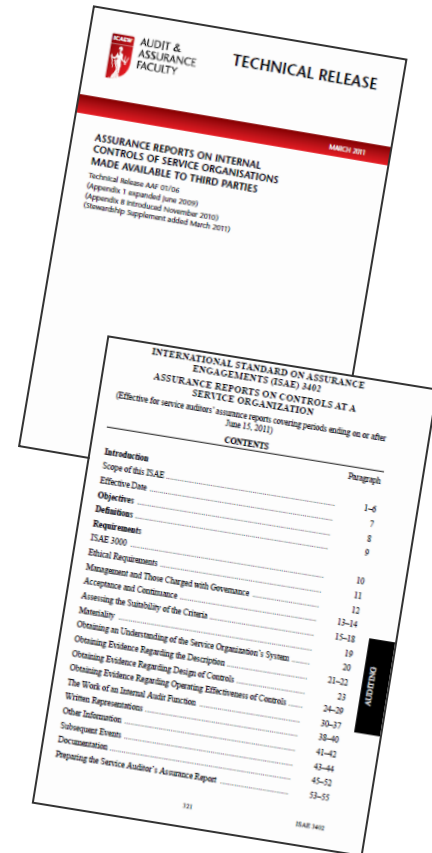
- Derivatives
- Venture capital
- Private equity
- Hedge funds
- Funds of funds
- Emerging market investments



The internal controls report

What to do with it?

- Internal controls reports for different jurisdictions
 - AAF 01/06
 - SAS 70
- Being replaced by ISAE 3402
- Work required:
 - Nature and content of report
 - Scope of work done
 - Usefulness and appropriateness incl period covered
 - Review exceptions raised
 - Do exceptions warrant reporting:
 - Pensions Panel
 - Governance Compliance Statement?
 - Additional work required?



What we're going to cover today

- Setting the scene
- Financial Reporting framework
- The Pension Fund Accounts
- Fund Account
- Net Assets Statement

▪ Disclosures

▪ Annual Report



Debtors
Related parties
Financial instruments



Debtors and creditors

Don't forget investment transaction balances

Code requires specified analysis:

Analysis	Who?
Central government bodies	Probation boards/trusts, tax authorities
Other local authorities	Local authorities, police, fire, schools
NHS bodies	PCTs, NHS and foundation trusts
Public corporations and trading funds	PTEs
Bodies external to general government	Fund managers, colleges, ALMOs, LA companies etc

Deferred debtors/creditors (eg phased augmentation conts, magistrates courts)

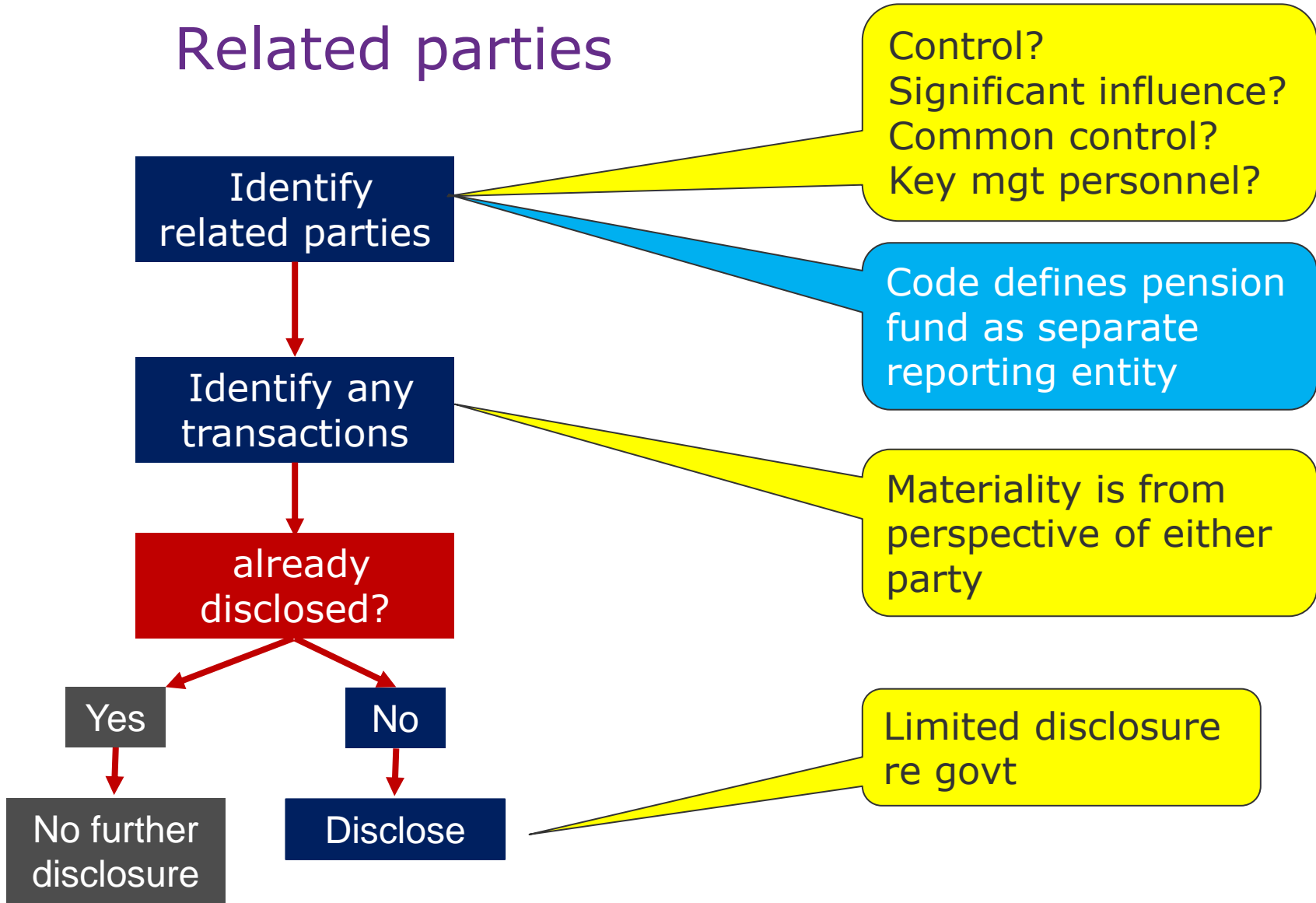
- Maturity analysis
- Discount over life of deferral

Related party transactions

- Disclosures as per Code
- But also key management personnel compensation
 - Short-term employee benefits
 - Post employment benefits
 - Other long-term benefits
 - Termination benefits
 - Share-based payments
- Pension fund examples – 2.162-2.185 Pension SoRP

“Those with authority or responsibility for planning, directing or controlling...”

Related parties



Control?
Significant influence?
Common control?
Key mgt personnel?

Code defines pension fund as separate reporting entity

Materiality is from perspective of either party

Limited disclosure re govt

Should key management personnel compensation be disclosed?

- Requirements of IAS 24 met by senior officer remuneration and members allowances disclosures

- Code requirements stem from:
 - senior officers- Accounts & Audit Regulations 2011 Reg7(2)-(4)
 - Members - Local Authorities (Members' Allowances) (England) Regulations 2003

Key management personnel compensation

Does the Code exemption apply to pension funds?

- Unclear
- Reg 7(2) applies to single entity authority accounts
- Pension fund accounts are separate standalone a/cs
-Reg 7(1)(d)
- Pension fund a/cs in Annual Report should be
“freestanding”

Key management personnel compensation – who and what

Who?

- “chief officers, elected members....having authority and responsibility for planning, directing and controlling the activities....” [Code 3.9.2.2]

What?

- Compensation includes:
 - a) Short-term employee benefits eg pay, NI, annual leave
 - b) Post-employment benefits eg pension
 - c) Other long-term post-employment benefits
 - d) Termination benefits
 - e) Share-based payments
- Disclose in total and for each category
 - No names required

Key management compensation – in practice

Element	Officers	Members	Measurement
S/t benefits	Pay etc	N/A	IAS 19
Post-employment	Pensions	Pensions?	IAS 19
Other I/t benefits	Unlikely	N/A	IAS 19
Termination benefits	Potentially	N/A	IAS 19
Share-based pay'ts	Unlikely	N/A	IFRS 2

IAS 19 Employee benefits

IFRS 2 Share-based payments

Financial instruments

- Background
- What are financial instruments?
- Disclosures about significance
- Nature and extent of risks



Background

IFRS 7

Code requires extensive disclosures:

- Significance of financial instruments to
 - Financial position
 - Financial performance
- Nature and extent of risks arising from financial instruments to which the fund is exposed
- How the fund is managing those risks

Financial instruments – what are they?

Any **contract** giving rise to a **financial asset** in one entity and a **financial liability** or **equity instrument** of another entity



Financial instruments – what are they?

Financial assets are:

- Cash
- Equity instrument of another entity e.g. shares
- Contractual right to:
 - receive cash or another financial asset from another entity e.g. trade debtor
 - exchange financial assets or financial liabilities under potentially favourable conditions e.g. derivatives

Financial instruments – what are they?

Financial liabilities are contractual obligations to:

- Deliver cash or another financial asset
- Exchange financial assets or financial liabilities under potentially unfavourable conditions - e.g. derivatives

Equity is:

- A residual interest in the net assets and also where there is no contractual obligation to make payments -e.g. non-puttable ordinary shares, preference shares (some)

Financial instruments - examples

Which of these are financial instruments?

Cash

Equity/debt instruments

Forward transactions

Guarantees

Leases

Overdrafts

Promised future retirement benefits

Property fund

Property

Subsidiaries, associates & JVs

Tax owed

Trade creditors

Classify into financial asset or liability.
If neither, which accounting standard applies?

Carrying value by asset category:

	FVPL	Loans and receivables	Financial liabilities at amortised cost
	£000s	£000s	£000s
Financial Assets			
Fixed interest securities	416,672		
Equities etc	1,183,056		
Etc		100,877	
Cash		16,151	
Debtors			
Total	4,403,074	117,028	0
Financial liabilities			
Other investment balances etc	(2,656)		
Creditors			(11,506)
Total	(11,487)	0	(11,506)

Note: No available for sale category

Do figures agree to NAS?

Significance of financial instruments

Net assets statement

- Reclassification between categories
 - Code defines and restricts classification
 - Disclose when change valuation: cost \longleftrightarrow fair value
- Derecognition
 - Transfer of assets
- Collateral
- Defaults and breaches

Significance of financial instruments Fund account

Income, expense, gains or losses

- Net gains & losses by instrument category
- For instruments NOT at FVPL:
 - Total interest income/expense
 - Fee income/expense
- Interest on impaired financial assets
- Impairment losses by class of financial asset

Significance of financial instruments

Hedge accounting

- Hedges are derivatives used to offset changes in fair value of designated hedged item
- Option to **designate** instruments as hedging instruments
- Disclosures:
 - Description of each hedge
 - Description of each hedged instrument
 - Risks being hedged
 - Cashflows
 - Ineffectiveness

Significance of financial instruments Fund account

Fair value

- Balances analysed by class versus carrying value
- Grouping ONLY where offset permitted
- Valuation techniques & underlying assumptions
- Fair values analysed by hierarchy of valuation approach
 - Level 1 – quoted prices
 - Level 2 – other than quoted prices eg observable/derived data
 - Level 3 – unobservable inputs eg valuation models
- Disclosure not required where
 - Carrying value approximates to fair value
 - Fair value cannot be measured reliably

Nature and extent of risks Disclosures - overall

For each type of risk (credit, liquidity, market):

Qualitative	Quantitative
<p>Extent of risk exposure and how they arise</p> <p>How the risk is managed</p> <ul style="list-style-type: none"> Objectives Policies Processes <p>Any changes from previous period</p>	<p>Summary quantitative data about exposure to risk</p> <p>Based on information provide to key management</p> <p>Any concentrations of risk</p>

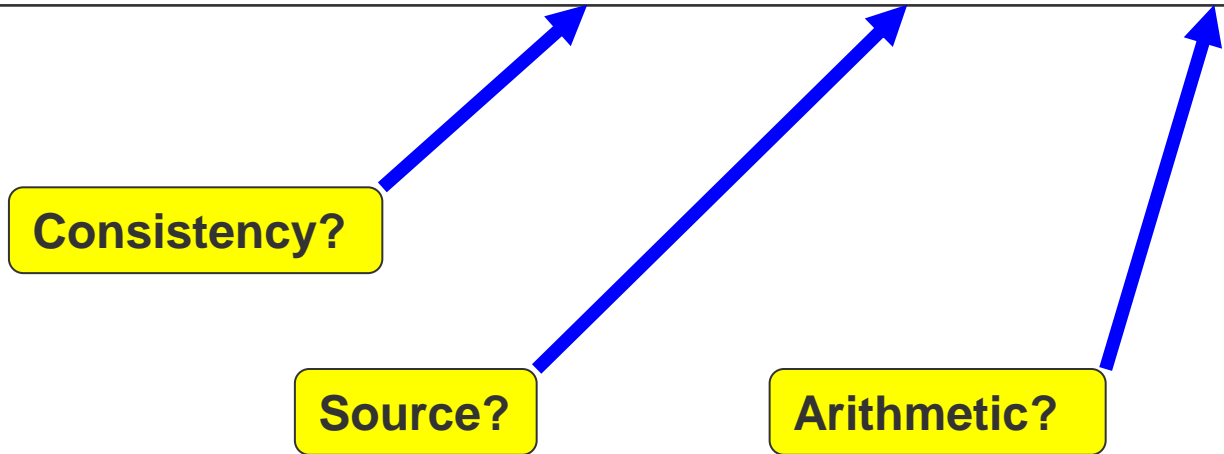
Links to:
Risk register?
Investment policy?
SIP?

Nature and extent of risks Disclosures - specific

Credit risk	<p>Maximum exposure</p> <p>Collateral held</p> <p>Credit quality of past due/impaired assets</p>
Past due/impaired assets	<p>Age analysis of past due assets</p> <p>Analysis of impaired assets</p>
Collateral	<p>Nature and carrying amount of assets</p> <p>If not convertible, policy for disposal</p>
Liquidity risk	<p>Maturity analysis</p> <p>Arrangements for managing liquidity risk</p>
Market risk	<p>Sensitivity analysis for each market risk</p> <p>Methods and assumptions used</p> <p>Any changes and reasons</p>

Example sensitivity analysis

Asset Type	Value at 31/3/12	%age change	Value on increase	Value on decrease
	£000	%	£000	£000
Cash & equivalents	12,850	0.0	12,850	12,850
Investment portfolio assets:				
UK bonds	72,514	3.6	75,125	69,903
Overseas bonds	344,158	2.9	354,139	334,177
etc				



Do the accounts hang together?

Your chance to spot the errors!

Annual Report

- What is required?
- Compliance
- Summary reports
- Management & financial performance
- Administrative management performance
- Risk management



Compliance

What is required?

“An administering authority **must**.....prepare...the pension fund annual report which **contains**:.....
.....must **publish** on or before 1 December....
.....must **have regard** to guidance....” [Reg 34]

- must - not discretionary
- contains – have or hold within
- publish
 - not defined in LGPS Regs
 - A&A Regs: “.....must include publication on the body’s website....”
- have regard
 - need good reason for not following

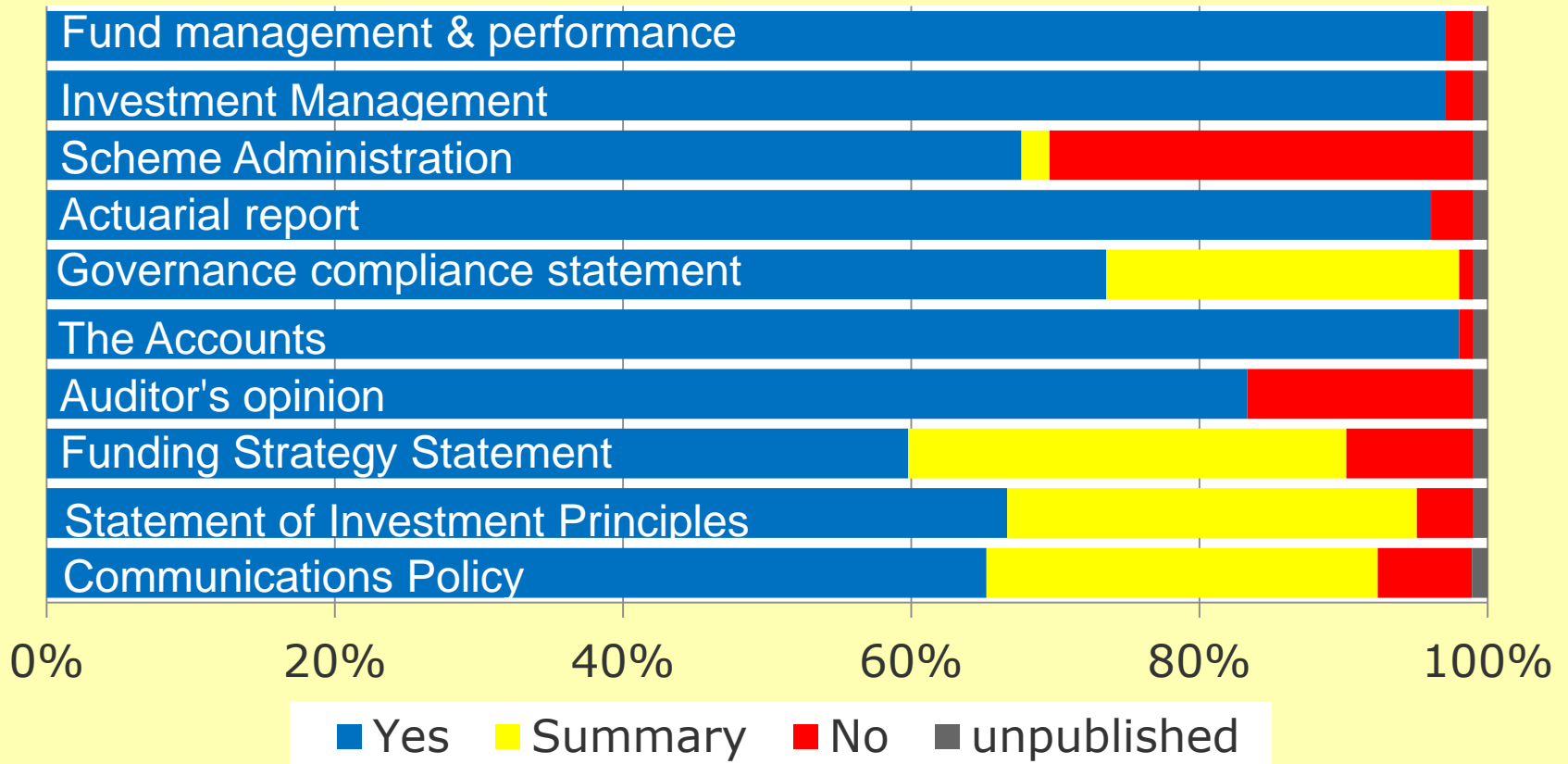


Must contain....

Management & financial performance	
Investment policy & performance	
Scheme Administration	
Outstanding borrowings	Scotland only
Actuarial report	
Governance compliance statement	
The Accounts including notes	
Pensions Administration Strategy performance	Discretionary
Funding Strategy Statement	
Statement of Investment Principles	
Communications Policy	England & Wales only

Not everything was included....

Annual Report content 2012/13



Publication

- Audit opinions given by 30 September
- 24 day delay between opinion and publication

Good practice:

- ✓ Project plan production
- ✓ Identify what you want, from whom and when
- ✓ Use CIPFA Guidance
- ✓ Populate with sections which are “givens”
 - ✓ Governance compliance statement
 - ✓ Funding Strategy Statement
 - ✓ Statement of Investment Principles
 - ✓ Communications Policy
- ✓ Arrange for Member approval



Accessibility – how easy to find

Quicker to find in 2012/13 – 2 pages to find annual report
BUT fewer accessed from Fund homepage – 28 (34 in 2011/12)

Good practice:

- ✓ List reports under **Reports and Documents** not **Investments**
- ✓ Websites with internal search engines more accessible
- ✓ Check the report is searchable!
- ✓ Standardise naming of documents
- ✓ List most recent documents at the top of webpages
- ✓ Remove superceded versions
- ✓ Include newsletters under the “News” page

Annual Report - content

- CIPFA guidance
 - Revisit
 - Compare how your report follows
- Some content is a given
 - Actuary's report
 - The Accounts
- Focus on sections where there is wide variety of practice
 - Management and Financial Performance Report
 - Investment Policy and Performance Report
 - Scheme Administration Report



Management and financial performance

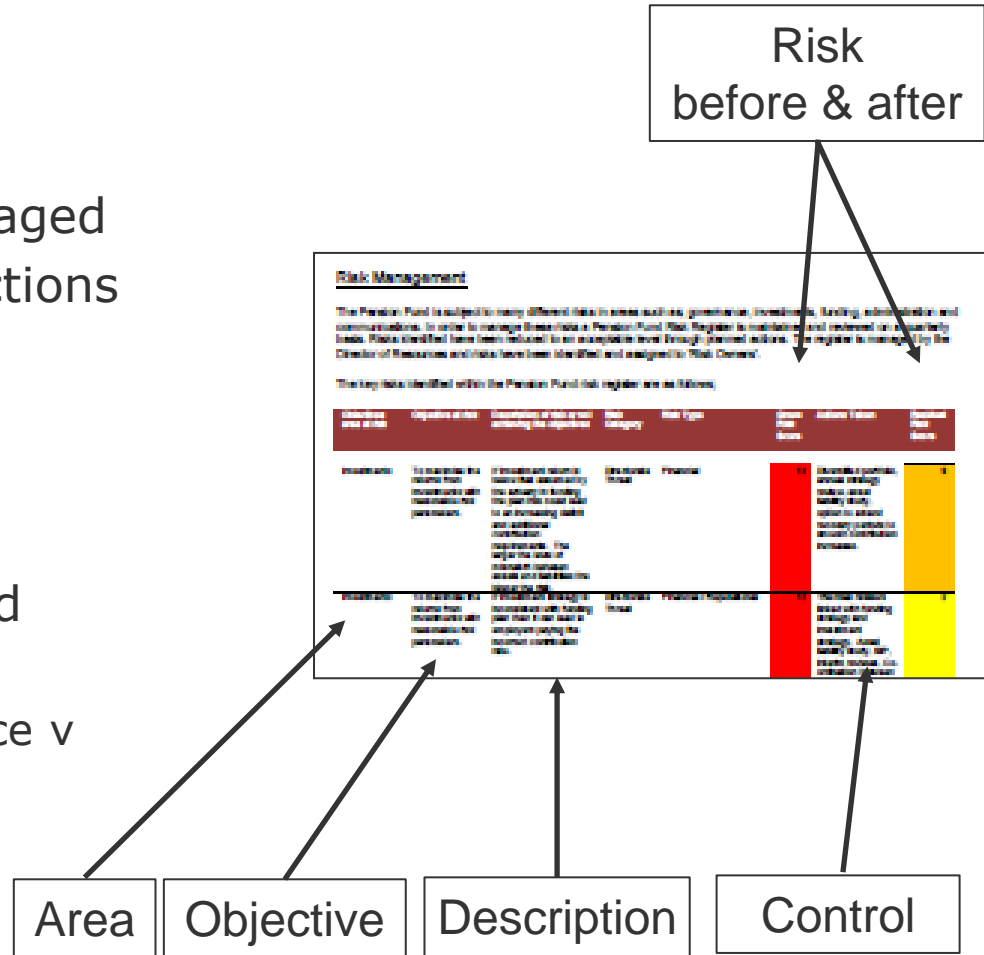
Area of annual reports with greatest variation in practice

Compliance	
Scheme management & advisors	97%
Risk management	44%
Financial performance	22%
Administrative management performance	65%

Risk Management

- Fit within fund governance
- How risks identified and managed
- SUMMARY of key risks and actions to mitigate
- Approach to third party risk
 - Late contributions
 - Outsourced operations
- How investment risk managed
 - Advice
 - Regular review of performance v strategy

Does section link to financial risk disclosures?



Financial performance

- Annual and 3 year forecast of major cashflows
- More detailed analysis of “controllable” expenditure
 - Administration expenses
 - Investment management expenses
- Variances explained
- Brief commentary on movements in assets and liabilities
- Amounts due from employers
 - Timeliness of receipt
 - Exercise of penalties



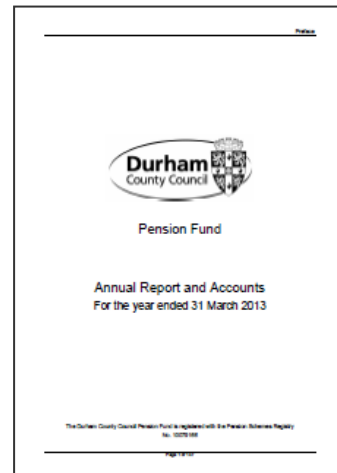
Administrative management performance

- Overlap with Scheme Administration Report
- Section focus is on performance of administration service
 - Key admin PIs - dealings with members, customer satisfaction
 - Unit costs & benchmarking data
 - Staffing KPIs
 - Service development
 - Staff training
- 5 yearly analysis of membership **WITH** commentary

Scheme Administration Report

Review of administrative arrangements for the fund

- Focus on who does what **NOT** performance
- IT arrangements, self-service
- Scheme administration
 - Internal or outsourced
 - Assurance arrangements
- Internal Dispute Resolution Procedure
 - Explanation
 - Analysis of activity



Investment policy and performance

Purpose - demonstrate how investment strategy performed in year
how thinks links to SIP

- Asset allocation
 - ✓ Actual v planned
 - ✓ Variances explained

 - Investment performance
 - By asset class
 - By fund manager
- Compare against benchmarks
-
- UK Stewardship Code
 - Compliance with Myners Principles
- Tabular layout?
-
- Investment administration and custody
 - Who does what
 - How managed

 - Implementation of funding strategy
 - Managing contributions
 - Managing admitted bodies
 - Bonds

- ✓ Simple and clear messages
- ✓ Selective use of graphs

The Accounts

Ongoing issues:	
Accounting policies for estimation and critical judgments	➤ There should be some
Accounting for derivatives	➤ Over-valuing risk
Disclosure of related party transactions	➤ Identification ➤ Only disclose if not already disclosed elsewhere ➤ Quantify

Summary reporting

- Increasing number of funds publishing summary reports 15 (11 in 2011/12)

Good practice:

- ✓ Simple naming of document (eg summary report, newsletter)
- ✓ No more than 4 pages
- ✓ Access from same page as full annual report
- ✓ Short clear messages



Bedfordshire Pension Fund
Summary Report and Accounts 2012 / 2013

MARKETS

Devon County Council
Pension Fund Annual Report & Accounts

2012/13

Government

	2012/13	2011/12
Employer contributions	19,912	20,265
Employee contributions	68,161	69,823
Transfer from reserves	8,863	7,217
Investment income	72,288	18,846
Other income	5,185	1,158
Total income	164,399	117,309
Pensions & other benefits	73,480	72,803
Finance charges paid	3,231	4,832
Investment management expenses	4,075	4,118
Other expenses	1,053	1,024
Total expenditure	81,839	82,837
Surplus for investment	78,788	24,817
Investment of funds	1,318,798	1,278,685
Operating net assets	23,798	24,817
Surplus for investment	23,798	24,817
Change in value of assets	128,669	12,464
Closing net assets	1,371,265	1,316,166

Contact

If you have any questions, please contact the following:

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geoff.reader@bedford.gov.uk

Benefits and contributions
Clare Bennett
Pensions Administration Manager
01224 220873
pensions@bedford.gov.uk

Website
www.bedpensionfund.org

If you would like a copy of the report and accounts, the "Guide to Local Government Pension Scheme", the Fund's Statement of Investment Principles or any other information, please contact either of the above, or visit our website.

In summary

- ✓ Statutory prescribed content
 - ✓ so must be included
 - ✓ draft skeleton Annual Report now
 - ✓ compare against CIPFA guidance
- ✓ Think about audience
 - ✓ Less is more
 - ✓ Simple and clear messages
- ✓ Timing
 - ✓ plan now for what you want, from whom and when
 - ✓ project plan throughout the year
- ✓ Publication
 - ✓ link on Fund homepage
 - ✓ include auditor's report OR state it is unaudited
 - ✓ consider summary report as well



LGPS fund accounting – 2012-13

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