

Scottish Borders Council
Pension Fund

annual report and financial statements

for the year to 31 March 2016



Contents

	Page
Introduction by Chairman of Pension Fund Committee	2
Management Commentary	3
Management and Financial Performance	3
Investment Strategy	8
Review of Investment Performance	9
Funding Position	12
Pensions Administration Update	13
Governance	17
Annual Governance Statement 2015/16	17
Governance Compliance Statement 2015/16	19
Risk Management Statement	24
Statement of Responsibilities for the Statement of Accounts	25
Statement of Accounts 2015/16	26
Fund Account 2015/16	26
Net Assets Statement as at 31 March 2016	27
Notes to the Statement of Accounts	28
Independent Auditor's Opinion	48
Annex 1 Statement of Investment Principles	50
Annex 2 Glossary of Terms	55
Additional Information	57

REPORT BY CHAIRMAN OF PENSION FUND COMMITTEE

Introduction

Welcome to the Annual Report and Accounts for the Scottish Borders Council Pension Fund for the year ended 31 March 2016. This Annual Report has been produced to provide Elected Members, Scheme Members and Employers and other interested parties with information concerning the administration and performance of the Fund in financial year 2015/16.

Highlights for the Year

Pension Fund Committee/Pension Board

The Pension Fund Committee has worked hard during the year to support the delivery of the continually growing governance agenda and increasingly complex pension administration environment that the Fund operates within.

The Committee members have engaged with training events both locally and nationally to expand their knowledge and understanding. All members of the Pension Fund Committee have fully met the training and attendance requirements.

The introduction of a Pension Fund Board resulted in changes to the governance arrangements from 1st April 2015. Joint meetings of the Committee and Board commenced on 18 June 2015 and have been productive and informative due to the positive engagement of all members.

The introduction of the Investment and Performance sub-committee, under the new governance arrangement, has proved a success with all investment managers presenting twice yearly to the committee allowing full scrutiny to be undertaken of the funds managed.

Investment Assets

Following the strong market recovery and strong performance from key fund managers over the last couple of years, 2015 has provided a much more challenging time. The level of volatility across markets, especially

global equities has been unprecedented. Despite this unstable time the fund has managed to remain broadly at the 31/03/2015 level with only a small decrease of £2.6m.

The overall performance of the Fund was 7.1% based on a 3 year rolling average basis, outperforming the benchmark and the local authority weighted average return over the period.

Procurement Activity

Using the Norfolk Framework the successful procurement of the fund's Investment Advisor was completed. Members via the Procurement Sub-Group were fully engaged in this key procurement.

Cashflow Modelling

Work commenced in conjunction with the advisor to model the Fund's cashflow, using a number of scenarios. The models results will inform the Asset Allocation review, to be undertaken in 2016.

Pensions Administration

During the year the Pensions Administration Team have worked hard to embed new working practices and procedures, following the successful implementation of the new LGPS scheme, which came into force from 1st April 2015.

Acknowledgement

I would like to thank the Members of the Pension Fund Committee, Pension Fund Board, officers within the Council, our investment managers, AON Hewitt and Barnett Waddingham for their hard work during the year and their ongoing commitment to ensuring the Fund's continued success.

Councillor Bill White

**Chairman, Pension Fund Committee
Scottish Borders Council**

MANAGEMENT COMMENTARY

Management and Financial Performance

Scottish Borders Council Pension Fund

2015/16 in Numbers

- £543m Net Assets, a decrease of £2.6m on 2014/15
- 10,259 Members, an increase of 462 on previous year

- Implementation of the Pension Fund Board
- Good Engagement of Members in the Training Programme

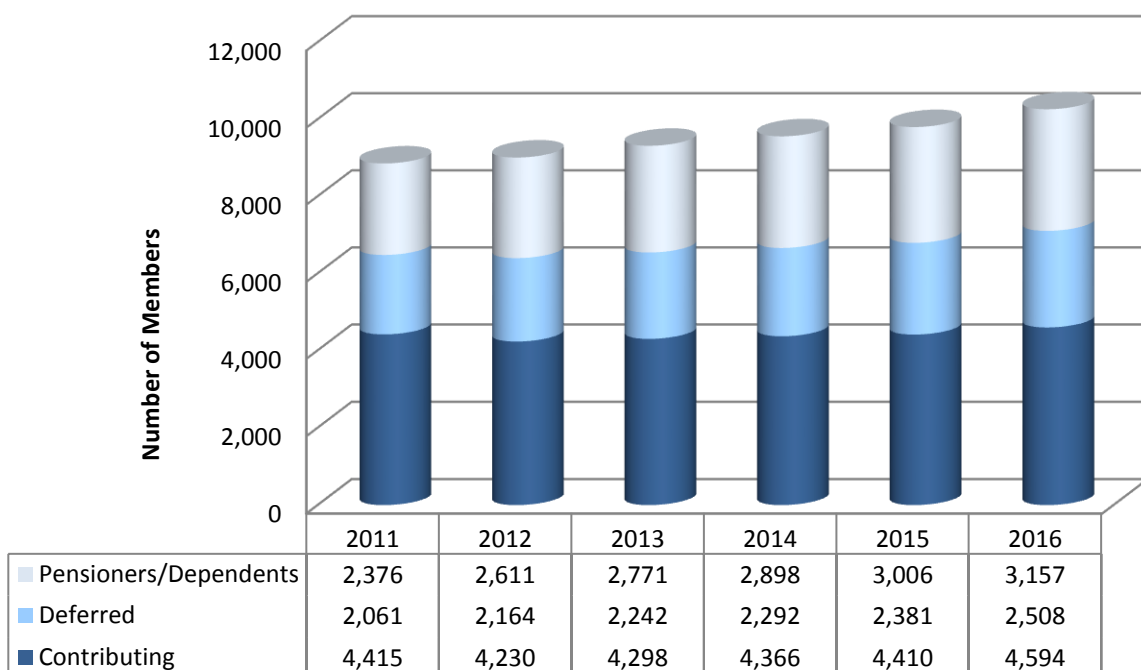
2015/16 Successes

The Scottish Borders Council Pension Fund (the Fund) as part of the Local Government Pension Scheme (LGPS) is administered by Scottish Borders Council (the Administering Authority). Note 1 to the Annual Accounts, page 28 provides a description of the Fund.

The Note sets out information in relation to the Fund's regulatory environment, funding, benefits and membership.

Overview of Fund Membership

Current membership of the Fund is 10,259 of which 4,594 are actively contributing and 3,157 are in receipt of pension benefits. The following chart summarises the trends in membership:



The chart on the previous page demonstrates that although there has been a relatively static position in relation to active contributing membership, there has been a continuing rise in the number of pensioners. Since 2011 the total membership has increased by 1,407 members (a 16% increase overall). During this period the number of pensioners and their dependants has increased by 28%, and the number of active contributing members has increased by 4%. This presents a challenge to the Fund to ensure that it manages its future cash flows effectively and will be included as part of the considerations when undertaking a full investment review.

A full reconciliation of the movement in membership during 2015/16 is included in Note 19 to the Accounts, page 44.

Financial Performance

The Financial Statements for the Fund are set out from page 25.

Key Figures from these are set out below:

	2014/15 £'000	2015/16 £'000
Net (Withdrawals) from Dealings with Members	(9,72)	(1,971)
Net Return on Investments	62,860	2,688
Net Increase/(decrease) in the Fund during the Year	59,030	(2,555)
Closing Net Assets of the Scheme	545,125	542,570

These highlight two key messages in relation to the Financial Position of the Fund:

- ***Reduction in Net Assets due to volatile nature of the current markets***
- ***A Net Withdrawal Position in relation to Dealing with the Fund's Members.***

The strong asset position, along with the 2014 Triennial Valuation of funding levels, demonstrates that the Fund is well placed to meet its future pension and other benefit liabilities.

The slightly increasing net withdrawal position supports the trend that is seen in the membership chart as outlined on page 3.

The changes in the legislation around what pensioners are able to do with their pension benefit entitlements are increasing individual freedom to withdraw from the Fund and trigger significant transfer movements. As this legislation has only just come into force this is an area that will require detailed monitoring to understand the impact and how it will affect the funding and investment strategy for the Fund.

Governance and Decision Making

Following the significant changes required in the governance arrangements which came into force on 1 April 2015 the Pension Fund Board was established. Joint meetings of the Pension Fund Committee and Pension Fund Board have been held during 2015/16.

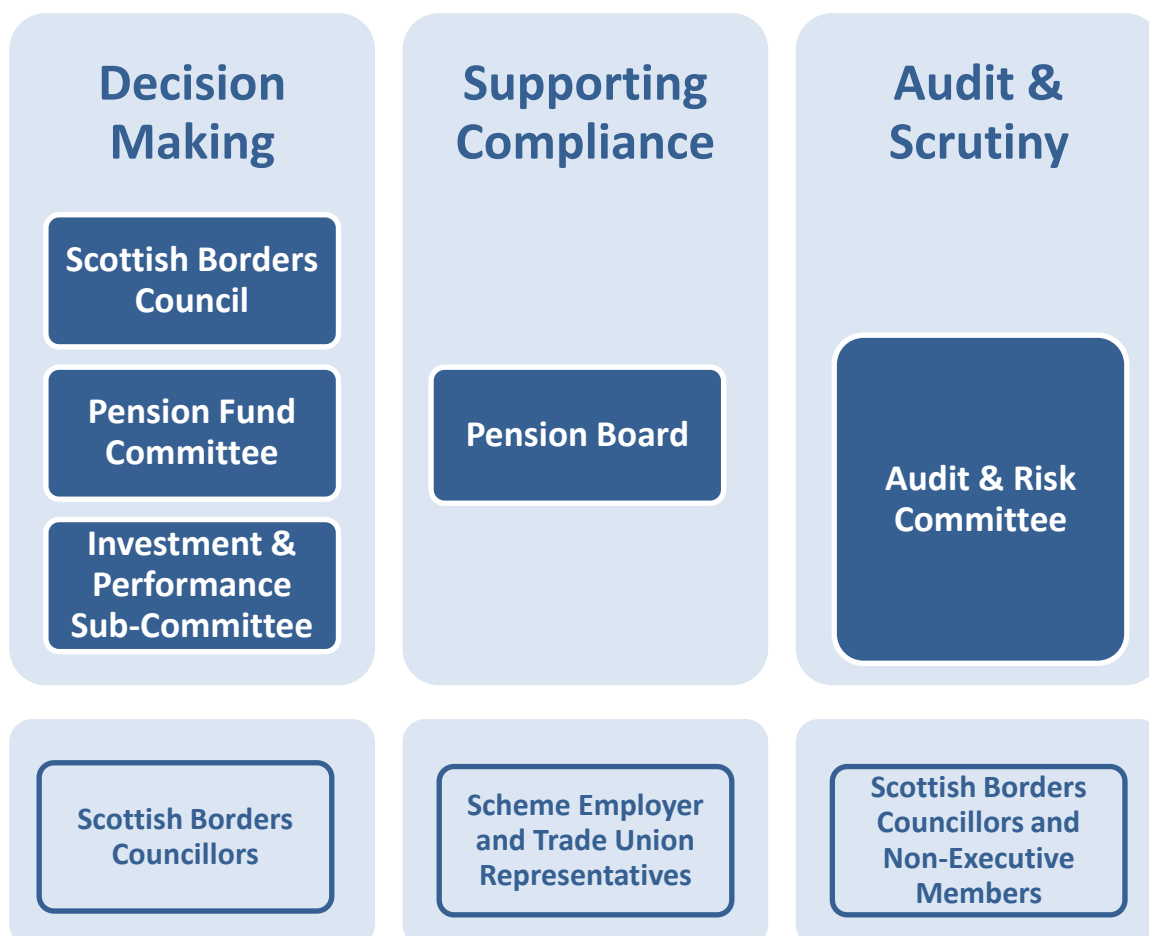
The remit of the Pension Fund Board is to assist the Council (as administering authority) in relation to:

- a) securing compliance with the regulations and other legislation relating to the governance and administration of the Scheme and any statutory pension scheme that is connected with it;
- b) securing compliance with requirements imposed in relation to the Scheme and any connected scheme by the Pensions Regulator; and
- c) such other matters as the regulations may specify.

This body is made up of four scheme employer representatives and four trade union representatives. The first joint meeting of the Pension Fund Committee and Pension Board was on 18 June 2015.

The changes also amended the membership of the Pension Fund Committee which now only has elected members from the administering authority, Scottish Borders Council.

The governance of the Fund is as follows:



The Annual Governance Statement and Governance Compliance Statement 2016 can be found on pages 17 to 23.

Knowledge and Skills

The Training Policy for the Fund was updated and agreed on 18 June 2015 to reflect the changes in the governance arrangements set out on page 5.

Following the annual training needs assessment, the 2015/16 training programme was developed. It was delivered to all members of both the Pension Fund Committee and the Pension Fund Board and covered the following areas:

- Performance Reporting
- Investments and new Investment Managers
- Governance
- Employees Benefits

The Training Policy sets out a target for all members of the Pension Fund Committee and Pension Fund Board in relation to attendance at Committee meetings and training events. The 2015/16 performance is set out below.

<i>Pension Fund Committee</i>	Number of Members Attending	
% Attendance	Committee (Target – 2 meetings)	Training (Target – 2 sessions)
100% (4 sessions or more)	4	0
75% (3 sessions)	2	3
50% (2 sessions)	1	4
≤ 25% (1 or no sessions)	0	0

<i>Pension Fund Board</i>	Number of Members Attending	
% Attendance	Committee (Target – 2 meetings)	Training (Target – 2 sessions)
100% (4 sessions or more)	1	2
75% (3 sessions)	4	2
50% (2 sessions)	2	1
≤ 25% (1 or no sessions)	1	3

All Members of the Pension Fund Committee have fully met the attendance and training targets set in the Training Policy. The Policy also requires members of the Pension Fund Board to attend two meetings per year and two training events. Due to changes in the year to membership, seven of the eight members have met the attendance requirement and five have met the training requirement.

The Fund is able to demonstrate full compliance with the relevant best practice standards and this is set out in the Governance Compliance Statement from page 19.

Fund's Aims and Objectives

Primary Aim of the Fund

- To provide for members' pension and lump sum benefits on their retirement or for their dependants' benefits on death before or after retirement, on a defined benefits basis.

Funding Objectives

- Set levels of employer contribution that will **build up a fund of assets that will be sufficient to meet all future benefit payments** from the Fund.
- Build up the required assets in such a way that ensure levels of **employer contribution that are stable**

Pensions Administration

- Deliver a **High Quality Pension Service to Members.**

Governance

- Ensure that Scottish Borders Pension Fund is **managed effectively, transparently and remains compliant.**

The Fund approved a Business Plan for the period covering 2015/16 – 2017/18 on 18 June 2015 and this presented the action plan associated with supporting the delivery of these aims and objectives. The key following actions were completed during 2015/16 supporting these objectives

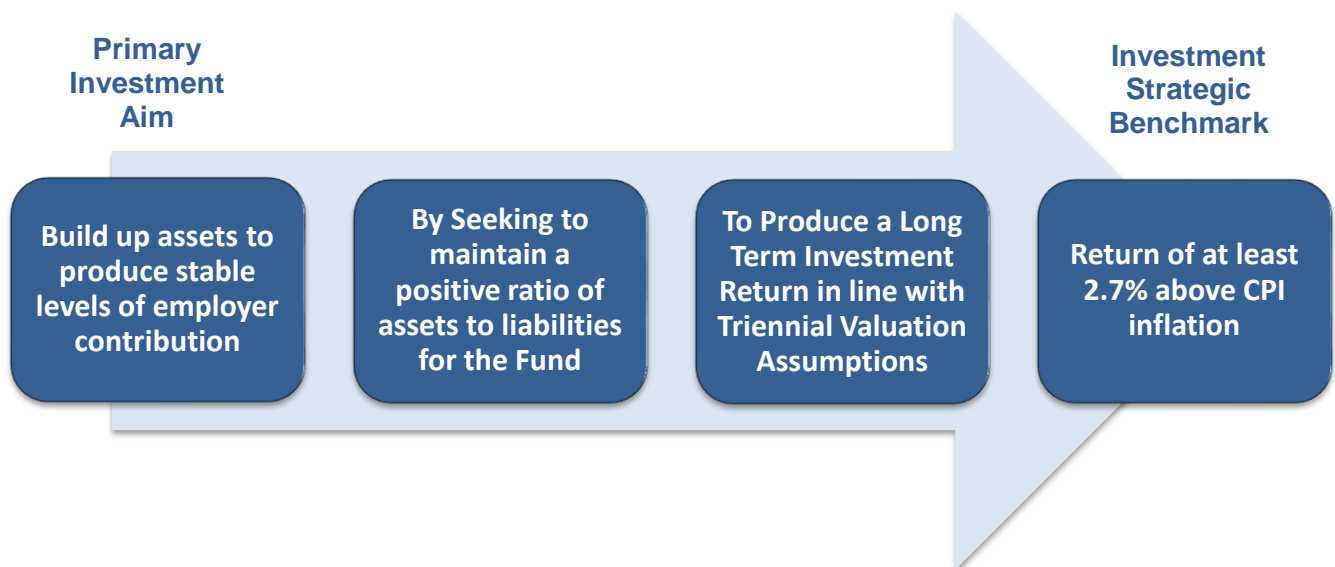
- **Implemented new governance structure, resulting in establishment of Pension Fund Board**
- **Implemented new pension administration system**
- **Procurement completed for Investment Manager**
- **Annual Report and Financial Statements produced within prescribed timescale with no audit qualifications.**

A full copy of the Business Plan can be found at www.scotborders.gov.uk/pensions.

MANAGEMENT COMMENTARY

Investment Strategy

The Statement of Investment Principles (SIP) approved on the 18 June 2015 sets out the Fund's current Investment Strategy and a copy of this document can be found at: www.scotborders.gov.uk/pensions. An extract of the key elements of the SIP are included in Annex 1 and the Investment Strategy that it sets out is summarised below:



The following table indicates the 31 March 2016 position in relation to asset allocation versus the revised benchmark which was agreed as part of the Investment Strategy:

Asset Class	Asset Allocation at 31/3/15 %	Asset Allocation at 31/3/16 %	Strategic Benchmark %
UK Equity	22.1	18.8	19.0
Global Equity	43.5	46.8	46.0
Bonds	10.7	10.8	13.0
Multi Asset Fund	17.2	17.0	17.0
Property	5.3	6.1	5.0
Cash	1.2	0.5	0.0
Total	100.0	100.0	100.0

As can be seen from the table on the above there has not been any major changes in the position of the allocation of assets between 2014/15 and 2015/16. The Fund has taken a deliberate decision to run underweight in the Bonds allocation due to the current market conditions.

The strategic benchmark represents the asset allocation split as approved within the Statement of Investment Principles.

MANAGEMENT COMMENTARY

Review of Investment Performance

2015/16 in Numbers

- **Strong 3 year annualised investment performance of 7.1%, 0.3% above benchmark**

- **Strong 3 year performance** to March 2016 with investment returns of 7.1% on a rolling 3 year annualised basis compared to a benchmark of 6.8%

Key Successes 2015/16

Investment Markets

During 2015/16 there was an unprecedented level of volatility across a number of markets. Over the 1 year rolling period a negative return was experienced in Equities both UK and Global. The 3 year rolling period however remains positive in all market areas. The factors affecting the markets were:

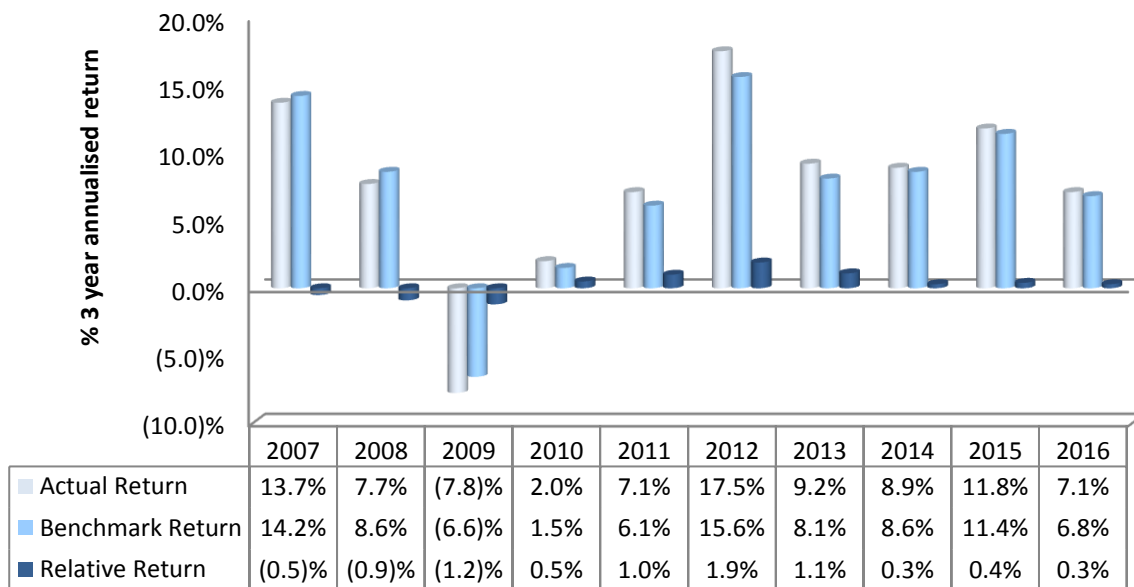
- Fears around the impact of Greek exit from Eurozone and slowing Chinese economic growth resulted in volatility across the global equity market.
- Demand for Property due to improving economic data resulted in Property being the top assets class performer.
- Interest rate increases in US resulted in volatility in both Bond and Equity markets. This also increased the fluctuations in exchange rates and resulting impact of currency hedging.

The Fund's investment performance has mirrored these strong investment returns during 2015/16.

Investment Performance

The Fund's performance against benchmark over the past 10 years is highlighted in the chart below. This chart demonstrates that the rolling 3 year annualised relative return (i.e. Fund's return achieved compared with the benchmark) since 2010 has been positive, and that over the 10 year period there has only been one year of negative returns overall for the Fund and that was during the financial crisis.

3 Year Annualised Returns ending 31 March



Including the impact of the passive currency hedge, the overall fund return over 3 years was 7.1% p.a. versus the benchmark of 6.7% p.a., and the Fund return over 1 year was -0.1% p.a. compared to a benchmark of -0.4% p.a. Excluding the impact of the currency hedge, the fund return over 3 years was 7.1% p.a. versus the benchmark of 6.8% p.a. and the fund return over 1 year was 0.9% p.a. versus the benchmark of 0.6% p.a.

The Fund achieved these favourable returns in 2015/16 despite the volatile period in the markets during the year. The fluctuations in currency and the resulting currency hedge payments pulled the overall performance of the fund down by 0.9% during the year but over the 3 year period the currency hedge has had no material impact on the overall performance.

Each quarter the Investment Consultants, AON Hewitt, reported on the Fund's quarterly performance by individual investment manager and mandate to the Joint Pension Fund Committee, and Pension Board. The Investment and Performance Sub Committee also met each Manager twice during the year giving members an opportunity to gain a deeper understanding of the investments, the decision making process and their performance.

The following table provides an analysis of how the Fund's investments performed against the UK Local Authority Weighted Average and the Fund Benchmark.

Return on Investment	1 Year rolling return			3 year rolling return		
	Fund %	Bench ¹ %	LA ² %	Fund %	Bench ¹ %	LA ² %
Total Fund including Currency Hedging	(0.1)	(0.4)	0.2	7.1	6.7	6.4
Total Fund excluding Currency Hedging	0.9	0.6		7.1	6.8	
Global Equities including UK	2.9	(0.4)	(1.6)	9.7	8.9	8.1
UK Equities	(3.7)	(3.9)	(3.8)	4.1	3.7	4.4
UK Government Bonds	3.3	3.2	2.9	8.2	7.0	4.9
UK Corporate Bonds	(0.4)	0.4	(0.9)	4.1	4.9	4.5
Pooled Bonds	(0.4)	0.5	(0.2)	n/a	n/a	2.6
Property	10.3	10.6	10.5	13.2	13.0	12.4
Alternatives	(1.6)	4.6	8.7	4.4	4.6	8.3
Cash	0.4	0.3	2.2	1.4	0.3	1.8

Key:

¹ **Bench:** Benchmark Return which reflects the overall performance of the individual markets available to the manager within the mandate given to them.

² **LA:** Local Authority Weighted Average Return based on WM Company's League Tables for period to 31 March 2016

The performance of the Fund overall has exceeded the rolling 1 year and 3 year benchmark. The rolling 1 year performance was aided by strong performance from Morgan Stanley in global equities, off-setting an under performance from Harris Associates in global equities, M&G in bonds and LGT in alternative portfolios.

Top 20 Direct Equity Holdings at 31 March 2016

Company	Market Value of Holding £ m	Company	Market Value of Holding £ m
Prudential	4.9	Anthem	2.5
Amazon	4.2	Ryanair Holdings	2.5
Royal Caribbean Cruises	4.0	BNP Paribas	2.4
Naspers	3.5	Moody's	2.4
SAP	3.1	First Republic Bank San Francisco	2.3
Taiwan Semicon.SPN.ADR.1:5	3.1	LafargeHolcim	2.2
CRH (LON)	3.1	Daimler	2.2
Alphabet 'C'	2.9	Credit Suisse Group	2.1
Glencore	2.6	MS&AD Insurance Group Holdings	2.1
Markel	2.5	TD Ameritrade Holding	2.0

MANAGEMENT COMMENTARY

Funding Position

2014 Valuation

- **101 % Funding Level for the Fund**
- **Stable Common Employer Contribution Rates at 18%**

Triennial Valuation 2014

The Triennial Funding Valuation as at the March 2014 was undertaken during 2014/15 and the final certified report was presented to the joint meeting of the Pension Fund Committee and Pension Board on 18 June 2015. A copy of the report is available via the Council's committee papers website <http://scottishborders.moderngov.co.uk/>.

The outcome of the 2014 Valuation was a funding level of 101% and a Fund which is no longer in a funding deficit position. As a result there was no change in the overall Fund common employer contribution rate, although some individual employer rates did change for specific circumstances.

Valuation Date as at 31 March	Past Service Funding Position – Scottish Borders Council Pension Fund		
	2008 £m	2011 £m	2014 £m
Value of the Scheme Liabilities	(310.1)	(402.2)	(487.6)
Smoothed Asset Value	299.2	384.8	490.5
Surplus/ (Deficit)	(10.9)	(17.4)	2.9
Funding Level	96%	96%	101%

Note 20 to the Statement of Accounts on page 44, contains details of the outcome and assumptions used in the 2014 Valuation and the impact that it had on employer contribution rates.

This is the first valuation that has taken into account the move to an LGPS based on career average earnings rather than final salary which came into effect on 1 April 2015.

A major contributing factor to the improvement in the funding level has been the strong investment performance that the Fund has achieved over the past 3 years.

Valuation for Statutory Accounts at 31 March 2016

Note 21 to the Statement of Accounts on page 47, contains the actuarial present value valuation for the Fund as required by the International Accounting Standard (IAS) 26. This shows a net liability for the Fund of £154.2m. However the liabilities for this figure are calculated on an IAS 19 basis and therefore will differ from the results of the 2014 Triennial Funding Valuation because IAS 19 stipulates a discount rate rather than a rate that reflects the market rate for investment returns on the Fund's assets. It is therefore not appropriate to use this as a measure for setting employer contribution rates or assessing its overall long term funding health.

MANAGEMENT COMMENTARY

Pensions Administration Update

2015/16 in Numbers

- 17 Scheme Employers
- £20.4m of Pension and Other Benefits paid during year
- £18.6m of Contributions Received from 4,594 Active Members and their Employers
- 6,446 Benefits Statements issued

- Pension Administration Strategy updated and approved September 2015
- Implementation of the new LGPS Scheme April 2015
- Successful admission of additional Bodies to the Fund

Key Successes 2015/16

Scheme Employer Liaison

The Scheme Employer Liaison meeting was held during 2015/16 and covered the new requirements for the year end returns, which were updated as a consequence of the new scheme rules. The opportunity was also taken to reinforce the scheme changes and the impact of these for the Fund and employers.

The good relationship with the main Scheme Employers also has resulted in the continued involvement of 4 employers as representatives in the new Pension Board.

MEMBERSHIP

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

Teachers are not included as they come within other national pension schemes. There are 17 employer organisations within the Fund including the Council itself and membership by employer are analysed over the page.

Membership Details as at 31 March 2015	Number of Contributors	Pensioners	Deferred Pensioners	Total
Scheduled Bodies:				
Scottish Borders Council	3,543	2,952	2,281	8,776
Borders College	162	62	85	309
Visit Scotland (Scottish Borders)	1	6	9	16
	3,706	3,020	2,375	9,101
Active Admitted Bodies:				
Scottish Borders Housing Association	121	73	59	253
Borders Sport and Leisure Trust	59	12	22	93
SBCares	693	23	33	749
Jedburgh Leisure Facilities Trust	2	-	2	4
L&B Community Justice Authority	5	1	3	9
Amey Community Limited	8	2	4	14
	888	111	123	1,122
Admitted Bodies with No Active Contributing Members:				
Gala Youth Project	-	1	1	2
Scottish Borders Careers	-	1	3	4
Others	-	24	6	30
	-	26	10	36
Total	4,594	3,157	2,508	10,259

Member Engagement

This has been identified as an area for development within the Pension Fund Business Plan 2015/16 – 2017/18. The development of a Communication Policy and associated action plan is included as an action for delivery within the next three year period. This will include exploiting the use of the web to engage with members via self-service interaction with the new pension administration system and improved information being available on the website.

Trade Unions as member representatives have also shown good engagement through their attendance at the Pension Fund Committee and also by securing 4 representatives for the Pension Board and identifying several substitutes.

Pensions Administration Strategy

The Fund's Pensions Administration Strategy was approved in September 2015. This sets out scheme employer and administering authority roles and responsibilities and defines the service performance standards.

How have we done?

A comprehensive report on Pensions Administration performance for 2015/16 was presented to the joint meeting of the Pension Fund Committee and Pension Board on 16 June 2016 and a copy of the report is available via the Council's committee papers website <http://scottishborders.moderngov.co.uk/>.

Administering Authority Performance Measures

Many of the performance standards have been met in 2015/16 and show improvements on 2014/15 performance. During 2015/16 the target performance days was reduced from 10 to 5 days for query responses and 100% of queries were replied to within this new target.

Service Standard - Estimates

Standard	Volume of Requests	Target Response	2015/16 % on Target
Estimates – Transfer In	54	20 days	22.2%
Estimates – Transfer Out	65	20 days	35.4%
Estimate – All Other	887	10 days	84.2%
Total Estimates	1,006		

Service Standard – Query Response Turnaround

Standard	2014/15		2015/16	
	Volume of Queries	% on Target	Volume of Queries	% on Target
Query responses – within 5 working days	480	100%	1,075	100%
Benefit Statement queries – within 20 working days	20	100%	55	100%
Total	500	100%	1,130	100%

Service Standard - Other

Area	Measure	Completed
Employer Liaison Meetings	1 per annum	Yes
Benefit Statements	by end of August	Yes

Employer Performance Measures

Service Standard – Employer Notifications

Standard	Volume of Notifications	Target %	% Achieved
New starts notification - within 20 working days	691	90%	100%
Changes notified – within 20 working days	485	90%	100%
Retirement info – at least 20 working days before	191	90%	100%
Early leaver notification – within 20 working days	410	90%	100%
Death in service notification – within 10 working days	6	90%	100%

Service Standard – Pension Contribution Payments

The following tables compare the date contribution payments are received against the target date for each of the Scheduled and Active Admitted Bodies.

Employer Body	Number of Monthly Payments Received		
	By Target Date (19 th of Month)	Late	% On Time
Scottish Borders Council	12	-	100%
Visit Scotland	12	-	100%
Borders College	12	-	100%
Scottish Borders Housing Association	11	1	92%
Jedburgh Leisure Facilities Trust	12	-	100%
Borders Sport and Leisure Trust	12	-	100%
AMEY Community Limited	12	-	100%
SBCares	12	-	100%

There has been a significant improvement in the number of payments being received on time during 2015/16, with only 1 payment being made after the target date, compared with 6 late payments in the previous year. The payments dates continue to be monitored on a monthly basis.

Councillor Bill White
Chairman
Pension Fund Committee

Tracey Logan
Chief Executive
Scottish Borders Council

David Robertson
Chief Financial Officer
Scottish Borders Council

29 September 2016

GOVERNANCE

Annual Governance Statement 2015/16

Introduction

The Local Government Pension Scheme (Scotland) Regulations 2014 require Administering Authorities to measure their governance arrangements set out against standards set by Scottish Ministers. These standards are established via a number of best practice principles.

The key document summarising the governance arrangements for the Pension Fund is the Governance Policy and Compliance Statement (as amended on 18 June 2015) which is available on the website www.scotborders.gov.uk/pensions.

The Governance Framework

The key elements of the Pension Fund's governance arrangements include:

- a) Scottish Borders Council is the Administering Authority for the Local Government Pension Scheme set up for the Scottish Borders geographic area.
- b) The Council has delegated its responsibilities as Scheme Manager to the Pension Fund Committee. The members of the Committee act as quasi-trustees and oversee the management of the Scottish Borders Council Pension Fund.
- c) The introduction of the Pensions Board, which meets jointly with the Committee, formalises the involvement of the employers and trade unions representing the membership. All members of the Committee and Board are covered equally by the Training Policy to give them full opportunity to contribute effectively.
- d) The approval the first Pension Fund Business Plan covering the period 2015/16 – 2017/18 to improve planning and monitoring of the performance of the Fund and to demonstrate the “Myners Principle” relating to effective decision making. The business plan supports the delivery of the objectives of the Fund which are to deliver a high quality pension service to members that was managed effectively, transparently and was compliant.
- e) The Pension Fund appoints professional advisers and external service providers.
- f) The system of internal financial control operates within a financial strategy and is based on a framework of delegation and accountability for officers and elected members embodied in procedural standing orders, financial regulations, scheme of delegation, scheme of administration, supported by a framework of administrative procedures including the segregation of duties, and regular financial management information. In particular, the system includes comprehensive accounting systems that record income and expenditure for both member and investment activities, regular reviews of investment reports that measure investment returns against agreed benchmarks, regular reviews of investment manager reports that measure performance against agreed targets, and independent performance reviews of the Fund by the Fund's investment consultant and performance monitoring services provider.
- g) The Pension Fund follows the Council's approach to risk management and assesses risk using a scoring methodology and subjects the risk register to regular review.
- h) The Chief Financial Officer (Section 95 officer) for the Council is responsible for ensuring the proper administration of the financial affairs of the Pension Fund. This includes ensuring appropriate professional advice is sought and is given to the Pension Fund on all financial matters, keeping proper financial records and accounts, and maintaining an effective system of internal financial control.

- i) The Chief Officer HR for the Council is responsible for the pension benefit policy oversight and day-to-day administration of member benefits in accordance with statutory legislation and the approved pensions' administration strategy.
- j) The Chief Officer Audit & Risk (Head of Internal Audit) provides an independent and objective annual opinion on the effectiveness of internal control, risk management and governance based on the delivery of an approved plan of systematic and continuous internal audit review in conformance with the Public Sector Internal Audit Standards.
- k) The Pension Fund responds to findings and recommendations of external audit and internal audit, as appropriate. The Audit and Risk Committee is integral to overseeing independent and objective assurance and monitoring improvements in internal control and governance.

Review of Framework

The Council as Administering Authority of the Pension Fund conducts an annual review of the effectiveness of its overall governance framework which is presented to the Audit and Risk Committee whose role includes high level oversight of the Pension Fund's governance, risk management, and internal control arrangements.

The review is informed by the work of an officer assessment of the Fund's compliance with the best practice principles and the detail of this is set out in the Governance Compliance Statement 2015/16, Annex 1 (pages 19 – 23).

The review of the effectiveness of the system of internal financial control is informed by the work of professional accountancy staff within the Council, the assurances from the Chief Officer Audit & Risk's annual internal audit opinion and report on the work internal audit, and by the external auditors' reports.

The review cycle for the risk register is undertaken in line with agreed practice and the current status is summarised in the Risk Management Statement.

The conclusion from the review activity outlined above is that in 2015/16 the Pension Fund continued to demonstrate that the governance arrangements and framework within which it operates are sound and effective.

Improvement Areas of Governance

The review has identified some areas where further improvements can be made to enhance the existing governance arrangements:

- a) Development of a communications plan to improve awareness and understanding of stakeholders and encourage maximum membership of the Fund.
- b) Work to fully evaluate the implications of new national policy on freedom of choice of pension sums.

Certification

It is my opinion that reasonable assurance can be placed upon the adequacy and effectiveness of Scottish Borders Council Pension Fund's systems of internal control and governance. Although areas for further improvement have been identified the annual review demonstrates sufficient evidence that the Pension Fund's Governance Policy is operating effectively and that the Pension Fund fully complies with the best practice principles as demonstrated in the Governance Compliance Statement, Annex 1 (pages 19 – 23).

Councillor Bill White
Chairman
Pension Fund Committee
29 September 2016

Tracey Logan
Chief Executive
Scottish Borders Council

GOVERNANCE

Governance Compliance Statement 2015/16

The Local Government Pension Scheme (Scotland) Regulations 2014 require Administering Authorities to measure their governance arrangements set out against standards set by Scottish Ministers. These standards are established via number of best practice principles. The following table contains an assessment of the Fund's compliance with these principles and reflects the changes following the introduction of the Pension Board.

Principle		Full Compliance	Comments
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.	Yes	<p>Scottish Borders Council acts as administering authority for the Pension Fund and delegates its responsibilities as Scheme Manager to the Pension Fund Committee (the Committee).</p> <p>The Committee comprises of 7 elected members.</p> <p>The Council's Scheme of Administration sets out the Committee's remit.</p>
B	Representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee	Yes	<p>Introduction of the Pensions Board (the Board) has formalised the involvement of the employers and trade unions representing the membership.</p> <p>The Fund's Board has 8 members, 4 employer representatives and 4 trade union representatives covering all pension fund members.</p> <p>The Board constitution was developed in line with the regulations, a copy of which is included in the Fund's Governance Policy and Compliance Statement.</p> <p>The Board meet jointly with the Committee and the Board Constitution and the Scheme of Administration set out how disputes between the two bodies should be resolved.</p> <p>The Investment and Performance Sub-Committee (the Sub-Committee) was established under the Committee and its remit is set out in the Scheme of Administration. The Membership of the Sub-Committee is comprised of the 7 elected members from the Committee and 2 (non-voting) members from the Board.</p>

Principle		Full Compliance	Comments
C	Where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	Yes	Minutes of the Sub-Committee and any other Sub-Groups are submitted to Committee for approval. 2 members from the Board and all members of the Committee are part of the Sub-Committee which has a remit to monitor investment performance.
D	Where a secondary committee or panel has been established, at least one seat of the main committee is allocated for a member from the secondary committee or panel.	Yes	The Scheme of Administration states that any Sub-Group established will have member(s) of the Committee as part of its membership.
Committee Membership and Representation			
A	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) (ii) scheme members (including deferred and pensioner scheme members), (iii) where appropriate, independent professional observers, and (iv) expert advisors (on an ad-hoc basis)	Yes	The Board and Committee meet jointly ensuring employer and member (trade union) representation at meetings. The Investment Sub-Committee has two non-voting members from the Board. The Independent Investment Consultant and key Finance and HR Officers also attend in an advisory capacity.
B	Where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.	Yes	All members of the Committee and Board are covered equally by the Training Policy (as amended annually in June). The Board was established by Council on 2 April 2015. Scheme of Administration for the Committee and Board Constitution provide for the joint meetings with equal rights to receive papers and access meetings in the same way.

Principle		Full Compliance	Comments
Selection and role of lay 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.	Yes	For elected members this is part of Council's Code of Governance along with Member induction programme. In addition the Fund's Training Policy provides for an annual training needs assessment, and an annual programme of training to be made available to all members of the Committee and Board.
B	At the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.	Yes	Part of Council's Code of Governance requires the declaration of members' interests as a standard agenda item on all committees.
Voting			
A	The policy of individual administering authorities on voting rights is clear and transparent, including justification for not extending voting rights to each body or group represented on main LGPS committees.	Yes	This is set out in the Council's Scheme of Administration and the Board's Constitution.
Training/Facility time/Expenses			
A	In relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process.	Yes	The Members Expenses are managed under the Council's policies. The Training Policy also covers the reimbursement of Training Related Expenses.
B	Where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	Yes	Training policy for all members of Pension Fund Board and Committee approved by Board and Committee annually in June.

Principle		Full Compliance	Comments
C	The Administering Authority considers the adoption of annual training plans for committee members and maintains a log of all such training undertaken.	Yes	Annual Training Plan produced and logs of training are being maintained.
Meetings (frequency/quorum)			
A	An administering authority's main committee or committees meet at least quarterly.	Yes	The joint meetings of the Committee and Board are quarterly.
B	An administering authority's secondary committee or panel meet at least twice a year and is synchronised with dates when the main committee sits.	Yes	Investment Sub-Committee meets every six months in between main joint Committee/Board meetings.
C	An administering authority that does not include lay members in their formal governance arrangements must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	Not applicable	Pension Board formally provides for the stakeholders engagement.
Access			
A	Subject to any rules in the Council's constitution, all members of main and secondary committees or panels have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	Yes	Papers sent to all Committee/Board members detailed in Scheme of Administration.

Principle		Full Compliance	Comments
Scope			
A	Administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Yes	The Scheme of Administration sets out that the Committee as having a remit which covers all matters relating the Council's role as the Administering Authority for the Scottish Borders Council Pension Fund, within the terms of all relevant Local Government Pension Scheme legislation and the requirements of the Pension Regulator.
Publicity			
A	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.	Yes	Minutes and Public papers available via Council website, as are various governance and scheme policy documents.

GOVERNANCE

Risk Management Statement

The Fund is committed to a strong control environment to ensure that risks are identified, understood, managed and monitored appropriately.

The Risk Register for the Pension Fund has been developed in line with the Council's approach to risk management and assesses risk using a scoring methodology based on likelihood and impact.

A full risk review was undertaken in June 2015 and subsequent reviews have followed the Council's cycle, as shown below was followed:

Level of risk (Inherent risk score)	Reporting and Review Cycle
RED -Very High (15-25)	3 monthly reviews of action progress throughout the year
AMBER – High (6-12)	6 monthly review
GREEN – Low (1-5)	Annual review

The headings under which the Council consider risk are set out below and the analysis of the level and number of risks are set out below:

Risk Category	Risk Assessment					
	Before Controls			After Controls		
	Red	Amber	Green	Red	Amber	Green
Asset & Investment	5	5	-	-	8	2
Employer	-	4	-	-	3	1
Resource & Skill	-	5	-	-	3	2
Liquidity	2	4	-	1	5	-
Administrative	1	8	-	-	4	5
Regulatory & Compliance	1	1	1	1	-	2
Reputation	1	4	-	-	2	3
Total Number of Risks	10	31	1	2	25	15

The two risks that remain at red assessment i.e. high risk as at 31 March 2016 are:

- ***Change in the composition of the Pension Fund Membership between active/deferred/pensioners***
- ***Legislation Changes impacting on the Fund***

STATEMENT OF RESPONSIBILITIES FOR THE STATEMENT OF ACCOUNTS

The Council's responsibilities

The Council is required to:

- Make arrangements for the proper administration of the financial affairs of the Scottish Borders Council Pension Fund (the Fund) and to secure that one of its officers has the responsibility for the administration of those affairs. In this Council, that officer is the Chief Financial Officer.
- Manage the affairs of the Fund to secure economic, efficient and effective use of resources and safeguard its assets
- Approve the Statement of Accounts of the Fund (in Scotland, the audited accounts must be laid before a meeting of the Authority within two months of receipt of the audit certificate)

The Chief Financial Officer's responsibilities

The Chief Financial Officer is responsible for the preparation of the Statement of Accounts in accordance with the Local Government Pension Scheme (Administration) (Scotland) Regulations 2014, as updated by the Local Government Pension Scheme Amendment (Scotland) Regulations 2010 (SSI 2010/234) and supporting guidance issued by the Scottish Government.

In preparing this Statement of Accounts, the Chief Financial Officer has:

- Selected suitable accounting policies and then applied them consistently
- Made judgements and estimates that were reasonable and prudent
- Complied with the Code of Practice on Local Authority Accounting

The Chief Financial Officer has also:

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

Statement of Accounts

The Statement of Accounts presents a true and fair view of the financial position of the Scottish Borders Council Pension Fund as at 31 March 2016, and of its income and expenditure for the year ended 31 March 2016.

Councillor Bill White
Chairman
Pension Fund Committee

David Robertson (CPFA)
Chief Financial Officer
Scottish Borders Council

29 September 2016

STATEMENT OF ACCOUNTS 2015/16 FUND ACCOUNT

2014/15 Restated £'000		2015/16 £'000	Notes
	Dealings with members, employers and others directly involved in the scheme:		
18,217	Contributions	18,642	6,9
703	Transfers in from other pension funds	411	7
18,920		19,053	
(19,106)	Benefits	(20,357)	8
(786)	Payments To And On Account Of Leavers	(667)	10
(19,892)		(21,024)	
(972)	Net Additions/(Withdrawals) from Dealings with Members	(1,971)	
(2,858)	Management expenses	(3,272)	11
	Return on Investments:		
4,605	Investment Income	6,359	12
58,422	Profits and (Losses) on Disposal of Investments and Changes in the Market Value of Investments	(3,519)	13
(167)	Taxes on Income	(150)	
62,860	Net Return on Investments	2,688	
59,030	Net Increase/(Decrease) in the Fund during the Year	(2,555)	
486,095	Opening Net Assets of the Scheme	545,125	
545,125	Closing Net Assets of the Scheme	542,570	

NET ASSETS STATEMENT as at 31 March 2016

2015 £'000		2016 £'000	Notes
	Investment Assets		
216,527	Equities	203,952	15
	Managed Funds:		
28,652	Property	32,546	
76,217	Global Equities	82,947	
65,308	UK Equities- Passive	62,415	
18,374	Bonds	18,643	
39,967	Diversified Fixed Income	39,913	
93,815	Alternatives	92,526	
1,665	Open Ended Investment Contracts	1,674	
(2,515)	Derivatives – Forward Foreign Exchange	1,447	
6,450	Cash Deposits	5,715	
544,460	Total Investment Assets	541,778	
748	Other Investment Balances	926	
	Current Assets & Liabilities		
1,138	Cash Balances	1,365	
91	Contributions due from Employers	210	
56	Other Current Assets	387	
(1,368)	Other Current Liabilities	(2,096)	
665		792	
545,125	Net Assets	542,570	

The Fund Account and Net Assets Statement do not show any liability to pay pensions or other benefits in the future. The liability to pay pensions is detailed in the Actuarial Statement in Note 21.

The unaudited accounts were issued on 28 June 2016 and the audited accounts were authorised for issue on 29 September 2016.

David Robertson CPFA
Chief Financial Officer
29 September 2016

NOTES TO THE STATEMENT OF ACCOUNTS

1 DESCRIPTION OF THE FUND

A) GENERAL

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

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

- The Local Government Pension Scheme (Scotland) Regulations 2014 (as amended)
- The Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014
- The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010
- The Local Government Pension Scheme (Governance)(Scotland) Regulations 2015

It is a contributory defined benefit pension scheme administered by Scottish Borders Council to provide pensions and other benefits for pensionable employees of Scottish Borders Council and a range of other scheduled and admitted bodies within the Scottish Borders area.

Organisations participating in the Fund include:

- Scheduled Bodies – which are local authorities and similar bodies whose staff are automatically entitled to be members of the Fund
- Admitted Bodies – which are other organisations that participate in the Fund under an admission agreement between the Fund and the relevant organisation.

B) FUNDING

Pensions and other benefits are funded by contributions from employees, employers and investment earnings.

The Pension Fund is subject to a triennial valuation by an independent, qualified Actuary, whose report indicates the required future employer's contributions, which for 2015/16 were based on the valuation undertaken as at the 31 March 2014 as amended by specific changes agreed by the Committee relating to an individual employer. The overall contribution rate was 18% for the Fund as a whole; however employer contribution rates during 2015/16 ranged from 15.5% to 18.5%.

Contributions from active members of the Fund are paid on a tiered basis, the contribution rate being determined by the amount of salary falling into each earnings tie. These rates are made in accordance with the 2008 Regulations and ranged from 5.5% to 12.0% of pensionable pay for the financial year ending 31 March 2016. *From 1 April 2015 these contributions will be based on the LGPS Regulations 2014 in line with the updated LGPS Scheme.*

C) BENEFITS

Prior to 1 April 2015, pension benefits under the LGPS have been based on final pensionable pay and length of pensionable service as summarised below:

	Service before 1 April 2009	Service after 31 March 2009 until 31 March 2016
Pension	Each year worked is worth 1/80 th x final pensionable salary	Each year worked is worth 1/60 th x final pensionable salary
Lump Sum	Automatic lump sum of 3 x salary. In addition, part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up.	No automatic lump sum. Part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up.

From the 1 April 2015, the scheme will become a career average scheme, whereby members accrue benefits based on their pensionable pay in that year at an accrual rate of 1/49th. Accrued pension is uprated annually in line with the Consumer Price Index.

There are a range of other benefits provided under the scheme including early retirement, disability pensions and death benefits.

2 BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS

The financial statements summarise the Fund's transactions for the 2015/16 financial year and its position as at the 31 March 2016. The accounts have been prepared in accordance with the *Code of Practice on Local Authority Accounting in the United Kingdom 2015/16* (the Code) which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector. In addition, consideration has been given to the *Local Government Pension Scheme Fund Accounts 2015/16 - example accounts and disclosure checklist* published by the Chartered Institute of Public Finance Accountants (CIPFA).

The financial statements also present the net assets available to pay pension benefits. These do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. Local authorities responsible for administering a pension fund that forms part of the LGPS are required by The Local Government Pension Scheme (Scotland) Regulations 2014 to publish a pension fund annual report, which is required to include a Fund Account and Net Assets Statement prepared in accordance with proper accounting practices.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fund Account

Accruals Basis

In accordance with the Code, the Fund's Financial Statements are generally prepared on an accruals basis. The Net Assets Statement does not include liabilities to pay pensions and benefits after the end of the Fund year and the accruals concept is applied accordingly. Receipts and payments in respect of the transfer of benefits from and to other schemes are treated on a cash basis.

Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the fund during the financial year and are calculated in accordance with the LGPS Regulations. Individual transfers in/out are accounted for when the member liability is accepted or discharged.

Investment Income

i) Interest income

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

ii) Dividend income

Dividend income is recognised on the date the shares are quoted ex-dividend. Any income not received by the end of the reporting period is disclosed in the net assets statement as a current financial asset.

iii) Distributions from pooled funds

Distributions from pooled funds are recognised at the date of issue.

iv) Movement in the net market value of investments

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

Benefits Payable

Pensions and lump-sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the Net Assets Statement as current liabilities.

Taxation

The Fund is a registered public service scheme under section 1(1) of Sch 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax is accounted for as a Fund expense as it arises.

Administration Expenses

All administration expenses are accounted for on an accruals basis. Central Support Costs from Scottish Borders Council have been recharged to the Fund on the basis of time spent by staff on the service.

Investment Management Expenses

Fees of the external investment managers and custodian are agreed in the respective mandates or subscription agreements governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.

Net Assets Statement

Valuation of Investments

The values of investments as shown in the net assets statement have been determined as follows:

- Market-quoted investments – Investments listed on recognised Stock Exchanges are valued at the bid price on the closing business day.
- Unquoted investments – Directly held investments include investments in limited partnerships, shares in unlisted companies, trusts and bonds. Other unquoted securities typically include pooled investments in property, infrastructure, debt securities and private equity. The valuation of these pools or directly held securities is undertaken by the investment manager or responsible entity and advised as a unit or security price. The

valuation standards followed in these valuations adhere to industry guidelines or to standards set by the constituent documents of the pool or the management agreement

- Pooled investment vehicles – are valued at bid price on the closing business day

The processes of the fund managers, who are listed in Note 15, page 38 are subject to external audit and verification and this is reported in their respective assurance reports on internal controls (in accordance with Technical Release AAF 01/06).

Foreign Currency Transactions

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

Derivatives

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

Derivative contract assets are fair valued at bid prices and liabilities are fair valued at offer prices. Changes in the fair value of the derivative contracts are included in the change in market value.

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

Cash and Cash Equivalents

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

Actuarial Present Value of Promised Retirement Benefits

The actuarial present value of promised retirement benefits is assessed on a triennial basis by the scheme actuary in accordance with the requirements of IAS 26, calculated in line with IAS 19 and relevant actuarial standards.

The financial statements summarise the transactions of the Fund during the year and its net assets at the year end. They do not take account of the obligations to pay pensions and benefits which fall due after the end of the year. As permitted under the Code, the Fund has opted to disclose the actuarial present value of promised retirement benefits by way of a note to the Net Assets Statement (Note 21, page 47).

Additional Voluntary Contributions (AVCs)

Additional Voluntary Contributions are invested separately from the main Fund, securing additional benefits on a money purchase basis for those members that have elected to contribute. All AVCs are managed by Standard Life and the value at 31 March 2016 was £0.846m (2014/15 £0.833m). During the year contributions totalled £0.006m, while payments out of the AVC fund totalled £0.01m. In accordance with regulation 4(2) (b) of the Government Pension Scheme (Management and Investment of Funds)(Scotland) Regulations 2009 (SI 2009/3093), AVCs are not included in the Pension Fund accounts.

4 CRITICAL JUDGEMENTS IN APPLYING ACCOUNTING POLICES

Unquoted private equity investments

It is important to recognise the highly subjective nature of determining the fair value of private equity investments. They are inherently based on forward-looking estimates and judgements involving many factors. Unquoted private equities are valued by the investment managers using guidelines set out by the British Venture Capital Association. The value of unquoted private equities at 31 March 2016 was £19.79m.

Pension Fund Liability

The pension fund liability is calculated every three years by the appointed actuary (currently Barnett Waddingham), with annual updates in the intervening years. The methodology used is in line with the accepted guidelines and in accordance with IAS 19. Assumptions underpinning the valuations are agreed with the actuary and are summarised in Note 21, page 47. This estimate is subject to significant variances based on changes to the underlying assumptions.

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

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

The items in the financial statements at 31 March 2016 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial Present Value of Promised Retirement Benefits (Note 21)	Estimation of the net liability to pay pensions in the future depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets. Barnett Waddingham is engaged to provide the Fund with expert advice about the assumptions to be applied.	<p>The effects on the net pension liability of changes in individual assumptions can be measured.</p> <ul style="list-style-type: none"> - A 0.5% increase in the discount rate assumption would result in a decrease in the pension liability of £44m - A 0.5% increase in the Consumer Price Index assumption for inflation would increase the value of the liabilities by £27m - A 0.5% increase in the long-term rate of salary increase would increase value of the liabilities by £6m, and - A 1.25% increase in assumed life expectancy would increase the deficit by £5m <p><i>Source – Triennial Valuation 2014</i></p>
Portfolio of alternative assets held in a fund of funds	The alternative assets fund of funds is valued at the sum of the fair values provided by the administrators of the underlying funds plus adjustments that the fund of funds directors or independent administrators judge necessary. The fund of funds is not publically listed and as such there is a degree of estimation involved in the valuation.	The total portfolio of alternative assets held in a fund of funds is valued in the Financial Statements at £92.34m. There is a risk that this investment may be under- or overstated in the accounts.

6 CONTRIBUTIONS RECEIVABLE

2014/15				2015/16		
Employers £'000	Members £'000	Total £'000		Employers £'000	Members £'000	Total £'000
13,039	4,400	17,439	Normal	13,373	4,401	17,774
743	-	743	Special/Pension Fund Strain	772	-	772
-	35	35	Additional Voluntary	-	96	96
13,782	4,435	18,217	Total	14,145	4,497	18,642

7 TRANSFERS IN

There were no group transfers in to the scheme during 2015/16 or 2014/15 and the total of £0.411m (2014/15: 0.703m) represents the total of transfer values in respect of individual members joining the scheme.

8 BENEFITS PAYABLE

2014/15 £'000		2015/16 £'000
14,657	Pension Payments	15,234
4,449	Lump Sums/Death Benefits	5,123
19,106		20,357

9 ANALYSIS OF CONTRIBUTIONS AND BENEFITS

2014/15			2015/16	
Benefits Payable £'000	Contributions Receivable £'000		Benefits Payable £'000	Contributions Receivable £'000
18,255	16,511	Scottish Borders Council	19,340	14,811
245	585	Scheduled Bodies	261	594
606	1,121	Admitted Bodies	756	3,237
19,106	18,217	Total	20,357	18,642

10 PAYMENTS TO AND ON ACCOUNT OF LEAVERS

2014/15 £'000		2015/16 £'000
73	Contributions Returned	68
713	Individual Transfers to Other schemes	599
786		667

11 MANAGEMENT EXPENSES

2014/15 £'000		2015/16 £'000
362	Administrative costs	301
2,165	Investment management expenses	2,754
331	Oversight and governance costs	217
2,858	Total	3,272

12 INVESTMENT INCOME

2014/15 £'000		2015/16 £'000
(103)	Income from Fixed Interest Securities	0
(3,767)	Dividends from equities	(5,569)
(676)	Income from Pooled Investment Vehicles	(771)
(59)	Interest on Cash Deposits	(19)
(4,605)		(6,359)

13 (PROFITS) AND LOSSES ON DISPOSAL OF INVESTMENTS AND REALISED CURRENCY PROFITS AND LOSSES

2014/15 £'000		2015/16 £'000
(21,150)	Realised	1,025
(37,272)	Unrealised	2,494
(58,422)		3,519

14 AUDITOR'S REMUNERATION

In 2015/16 the agreed audit fee for the year was £23,000. There were also fees, of £5,950, incurred during 2015/16 in respect of specialist taxation services provided by KPMG LLP, the Pension Fund's auditor.

15 ANALYSIS OF NET INVESTMENT ASSETS

Market Value at 31 March 2015				Market Value at 31 March 2016		
UK £'000	Overseas £'000	Total £'000		UK £'000	Overseas £'000	Total £'000
			Investment Assets			
53,569	162,958	216,527	Equities	46,438	157,515	203,953
			Managed Funds:			
28,652	-	28,652	Property	32,546	-	32,546
-	76,217	76,217	Global Equities	-	82,947	82,947
65,308	-	65,308	Passive UK Equities	62,415	-	62,415
18,374	-	18,374	Bonds	18,643	-	18,643
-	39,967	39,967	Diversified Fixed Income	-	39,913	39,913
-	93,815	93,815	Alternatives	-	92,526	92,526
1,665	-	1,665	Other Open Ended Investment contracts	1,674	-	1,674
5,056	1,394	6,450	Cash Deposits	3,936	1,778	5,714
172,624	374,351	546,975	Total Investment Assets	165,652	374,679	540,331
			Investment Liabilities			
(2,515)	-	(2,515)	Derivative - Passive Currency Hedge	1,447	-	1,447
170,109	374,351	544,460	Net Investment Assets	167,099	374,679	541,778

As at 31 March 2016 assets valued at £442.09m were quoted on the Stock Exchange (31 March 2015: £446.78m). The investments in the alternatives portfolio, managed by LGT Capital Partners (£92.53m at 31 March 2016), are not quoted on a stock exchange.

During 2015/16, sales of investments totalled £55.7m and purchases totalled £63.7m. These levels were reduced from 2014/15 as no transition activities were undertaken during 2015/16.

The Fund has in place a passive currency hedging programme, using forward foreign exchange contracts, which hedges 50% of exposure on specific overseas currencies on its overseas equity investments. All contracts are traded on an over the counter basis. The forward currency contracts outstanding at 31 March 2016 were hedging a foreign currency exposure value of £108.9m and had a market value of a gain of £1.452m. These contracts had a settlement date of 11 June 2016.

Alternative asset portfolio at 31 March 2016

The investment in the alternative asset portfolio, managed by LGT Capital Partners and valued at £92.526m at 31 March 2016, is allocated to the following asset classes at 31 March 2016: Convertible Bonds, Emerging Markets Debt, High Yield (Bonds), Commodities, Insurance-Linked Securities, Property, GTAA/Global Macro, Event Oriented, Market Neutral, Thematic Opportunities, Infrastructure and Private Equity.

(**GTAA** – *Global Tactical Asset Allocation*)

Investment Movement Reconciliation

	Opening Market Value £'000	Purchases & Derivative Payments £'000	Sales & Derivative Receipts £'000	Other Movements £'000	Closing Market Value £'000
Investment Assets					
Equities	216,527	46,179	(48,708)	(10,046)	203,952
Managed Funds:					
Property	28,652	5,941	(4,408)	2,361	32,546
Global Equities	76,217	114	(2,600)	9,216	82,947
Passive UK Equities	65,308	-	-	(2,893)	62,415
Bonds	18,374	-	-	269	18,643
Diversified Fixed Income	39,967	771	-	(825)	39,913
Alternatives	93,815			(1,289)	92,526
Other Open Ended Investment Contracts	1,665	-	(10)	19	1,674
Derivative Contracts:					
Passive Currency Hedge	(2,515)	10,738		(6776)	1,447
Net Investments exc. Cash Deposits	538,010	63,743	(55,726)	(9,964)	536,063

Significant Transactions during the year:

The requirement to fund currency hedge payments required £9m disinvestment to be made from the Global Equity portfolio.

Investments representing more than 5% of Net Assets

The value of the following investments exceeds 5% of the total value of the net assets of the Pension Fund at 31 March 2016. Each of the investments comprises units in a managed fund.

Value as at 31 March 2015	£'000
M&G Alpha Opportunities Fund	39,913
Morgan Stanley Global Brands Fund	82,947
LGT Crown SBC Segregated Portfolio	92,526
UBS UK Passive Equities	62,415

Investment Analysed by Fund Manager

Investment Management was undertaken on behalf of the Fund during the financial year by six firms of investment managers: UBS Global Asset Management, Baillie Gifford & Co, Morgan Stanley, Harris Associates and M&G and LGT Capital Partners. The Fund's passive currency hedging programme was provided by State Street Global Advisors. As at 31 March 2016 the market value of the assets under management, broken down by manager and mandate (including cash held within each mandate) was:

31-Mar-15				31-Mar-16	
£'000	%			£'000	%
65,308	12.00	UBS	UK Equities - Passive	62,415	11.49
40,783	7.49	Baillie Gifford	UK Equities	39,111	7.20
123,788	22.74	Baillie Gifford	Global Equities	120,370	22.16
57,214	10.51	Harris	Global Equities	50,278	9.26
76,216	14.00	Morgan Stanley	Managed Fund - Global Equities	82,947	15.27
39,967	7.34	M&G	Managed Fund - Diversified Income	39,913	7.35
18,374	3.37	M&G	Managed Fund - Bonds	18,643	3.43
29,428	5.40	UBS	Property	32,812	6.04
93,815	17.23	LGT	Managed Fund - Alternatives	92,337	17.00
(2,515)	(0.46)	State Street	Derivatives - Passive Currency Hedge	1,447	0.27
2,081	0.38	Internal	Internally Managed Cash & Investments	2,871	0.53
544,459	100.00			543,144	100.00

The benchmarks and performance targets for each manager as at the 31 March 2016 are contained in Annex 1, Section 4.3, page 51 for information.

Fund Performance

The total Fund return for the year was (0.1)% including the currency hedging. The hedging arrangements had a negative impact, decreasing the return by 0.9%. Excluding the currency hedging, the return on the Fund was 0.9% with a relative return over benchmark of 0.3%.

Over three years the Fund has generated an annualised return of 7.1% per annum, including the currency hedging, with a relative return over benchmark of 0.3% per annum. Further information on this is contained in the Management Commentary – Review of Investment Performance, page 9.

16 STOCK LENDING

As at 31 March 2016 no stock had been released to a third party under a stock lending arrangement.

17 NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS

RISK AND RISK MANAGEMENT

The Fund's primary long-term risk is that the Fund's assets will fall short of its liabilities (i.e. promised benefits payable to members). Therefore the aim of investment risk management is to minimise the risk of an overall reduction in the value of the Fund and to maximise the opportunity for gains across the whole Fund portfolio. The Fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) and credit risk to an acceptable level. In addition, the Fund manages its liquidity risk to ensure there is sufficient liquidity to meet the Fund's forecast cash flows.

Responsibility for managing the Fund's risk rests with the Pension Fund Committee. A risk register for the Fund has been established to identify and analyse the risks that the Fund faces and the key messages from this process are covered in the Risk Management Statement on page 24. The Market Risk and Credit Risk aspects below come under the risk category of Assets and Investment in the Risk Register, whilst Liquidity Risk is a separate category of risk.

In addition, the Funding Strategy Statement and Statement of Investment Principles address risk management considerations as they apply to the particular objectives of each document.

A) MARKET RISK

Market risk is the risk of loss from fluctuations in equity and commodity prices, interest and foreign exchange rates and credit spreads. The Fund is exposed to market risk from its investment activities, particularly through its equity holdings. The level of risk exposure depends on market conditions, expectations of future price and yield movements and the asset mix. The objective of the Fund's risk management strategy is to identify, manage and control market risk exposure within acceptable parameters, whilst optimising the return on risk.

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

(i) Other Price Risk

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

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

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

Other Price Risk – Sensitivity Analysis

In consultation with the Fund's independent provider of performance and analytical data (WM), it has been determined that the following movements in market price risk are reasonably possible for this reporting period.

Asset Type	Potential Market Movement +/- (% p.a.)
UK Equities	10.76
Global Pooled Equities	10.72
UK Bonds	6.84
Cash	0.01
Property	1.88
Alternatives	1.97

Potential price changes are determined based on the observed historical volatility of asset class returns. The potential volatilities are consistent with a one standard deviation movement in the change in value of the assets over the latest three years. Had the market price of the Fund investments increased/decreased in line with the above, the change in the net assets available to pay benefits in the market price could have been as follows:

Asset Type	Value as at 31 Mar 16 £'000	+/- % Change*	Value on Increase £'000	Value on Decrease £'000
UK Equities	101,526	10.76	112,450	90,602
Global Equities	253,594	10.72	280,779	226,409
Total Bonds	58,556	6.84	62,561	54,551
Cash	2,871	0.01	2,871	2,871
Property	32,812	1.88	33,429	32,195
Alternatives	92,337	1.97	94,156	90,518
Total Assets Exc. Currency Hedge	541,696	7.83	586,246	497,146

*The percentage change for total assets includes the impact of correlation across asset classes.

(ii) Interest Rate Risk

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

The Fund's interest rate risk is routinely monitored by the Council and its Investment Consultants, including monitoring the exposure to interest rates and assessment of actual interest rates against the relevant benchmarks.

The Fund's direct exposure to interest rate movements as at 31 March 2015 and 31 March 2016 is set out below and includes investment and operational cash balances. These disclosures present interest rate risk based on the underlying financial assets at fair value:

Asset Type	At 31 March 2015 £'000	At 31 March 2016 £'000
Cash and Cash Equivalents	7,588	7,080
Fixed Interest Securities	58,341	58,556
	65,929	65,636

Interest rate risk sensitivity analysis

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

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

Asset Type	Value as at 31 Mar 16 £'000	Effect on Asset Values	
		Favourable Rate Move + 100 BPS £'000	Unfavourable Rate Move -100 BPS £'000
Cash and Cash Equivalents	7,080	71	(71)
Fixed Interest Securities	58,556	586	(586)
	65,636	657	(657)

(iii) Currency Risk

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Fund (£UK). The Fund is invested in equities overseas that are denominated in currencies other than £UK. To help manage this risk, the Fund hedges 50% of its exposure to equities denominated in certain major foreign currencies through the operation of a passive currency overlay programme, operated by State Street.

The following table summarises the Fund's currency exposure at 31 March 2016:

Currency exposure by asset type	As 31 March 2015 £'000	As 31 March 2016 £'000
Overseas Equities	239,175	243,370
Diversified Bonds	39,967	39,913
Alternatives	93,815	92,526
Cash - Foreign Currency	1,394	1,778
Total	374,351	377,587

Currency Risk – Sensitivity Analysis

Following analysis of historical data in consultation with WM, the likely volatility associated with foreign exchange movements on an individual currency basis is shown on the table on the following page. The weight of each currency in relation to the total currency basket is multiplied by the change in its exchange rate (relative to GBP) to create the aggregate potential currency change of the 'basket'.

Currency	Value as at 31 Mar 16 £'000	+/- % Change	Value on Increase £'000	Value on Decrease £'000
Australian Dollar	1,219	8.26%	1,320	1,118
Brazilian Real	669	13.89%	762	576
Canadian Dollar	1,442	7.89%	1,556	1,329
Danish Krone	2,274	6.83%	2,429	2,119
EURO *	20,767	3.39%	21,471	20,063
Hong Kong Dollar	2,847	7.67%	3,066	2,629
Japanese Yen *	11,072	5.84%	11,719	10,426
Norwegian Krone	1,309	9.40%	1,432	1,186
South African Rand	3,878	10.31%	4,277	3,478
South Korean Won	1,836	7.22%	1,969	1,704
Swedish Krona	4,177	7.65%	4,496	3,857
Swiss Franc	11,668	9.95%	12,829	10,507
US Dollar *	91,095	3.89%	94,639	87,551
Total Currency **	154,253		161,965	146,543

* denotes 50% GBP hedge

** The % change for Total Currency includes the impact of correlation across the underlying currencies.

B) CREDIT RISK

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the Fund's financial assets and liabilities. The selection of high quality counterparties, brokers and financial institutions minimises credit risk that may occur through the failure to settle a transaction in a timely manner.

The Fund is separately mentioned within the Council's Annual Treasury Strategy and this document sets out the Fund's approach to credit risk for internally managed funds. Deposits are not made with banks and financial institutions unless they are rated independently and meet the Council's credit criteria. The Fund has also set limits as to the maximum percentage of the deposits placed with any one class of financial institution.

The Fund believes it has managed its exposure to credit risk, and the Fund has had no experience of default or uncollectable deposits over the past five financial years. The Fund's cash holding under its internal treasury management arrangements at 31 March 2016, including current account cash, was £2.78m (31 March 2015: £3.14m). This was held with the following institutions:

	Rating	Balance at 31 March 2015 £'000	Balance at 31 March 2016 £'000
Money Market Accounts			
Ignis	AAA	500	355
Scottish Widows	AAA	500	355
Blackrock	AAA	500	355
Prime Rate	AAA	500	355
Bank Current Accounts			
Bank of Scotland	A	1,138	1,365
Total		3,138	2,785

C) LIQUIDITY RISK

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

The Council has immediate access to its internally managed Pension Fund cash holdings through use of instant access accounts or money market funds.

The Fund defines liquid assets as assets that can be converted to cash within three months. Illiquid assets are those assets which will take longer than three months to convert in to cash. As at 31 March 2016, the Fund's only illiquid assets under this definition are some of the Property fund of funds holdings which are only tradable in the secondary market.

18 RELATED PARTY TRANSACTIONS

During the year, the Pension Fund had an average balance of £1.797m (2015: £6.603m) of cash administered by Scottish Borders Council within separate external banking arrangements, which earned interest of £0.010m (2015: £0.022m). The Council charged the Pension Fund £0.339m in respect of expenses incurred in administering the Fund. There are no additional related party transactions that require to be disclosed. The Pension Fund balance due from Scottish Borders Council to the Pension Fund at the balance sheet date and disclosed in the net assets statement was as follows:

As at 31 March	2015 £'000	2016 £'000
Due to Scottish Borders Council	(136)	(671)

19 MEMBERSHIP RECONCILIATION 2015/16

	Membership Reconciliation – Number of Members			
	Contributing Members	Pensioners	Deferred Pensioners	Total
Number at 31 March 2015	4,410	3,006	2,381	9,797
Adjustments (late notifications etc.)	4	8	(4)	8
New Members	691		2	693
Transfers to Other Schemes	(40)		(10)	(50)
Refunds of Contributions	(132)			(132)
Retirement of Contributing Members	(122)	122		0
Transfer to Deferred Pensioners	(228)		228	0
Re-employed Deferred Pensioners	17		(17)	0
Retirement of Deferred Pensioners		69	(69)	0
Dependants' Pensions		37		37
Deaths	(6)	(80)	(3)	(89)
Commutation (trivial pensions)		(5)		(5)
Ill Health Grant				0
End of Entitlement				0
Number at 31 March 2016	4,594	3,157	2,508	10,259

20 FUNDING ARRANGEMENTS

In line with the Local Government Pension Scheme Regulations 2014, the Fund's actuary undertakes a funding valuation every three years for the purpose of setting employer contribution rates for the forthcoming triennial period.

The Actuarial Valuation assesses the health of the fund and provides a check that the funding strategy and assumptions used are appropriate.

The Funding Strategy Statement

The latest Funding Strategy Statement (FSS) was approved by the Pension Fund Committee on 18 June 2015 and a copy of this document can be found at: www.scotborders.gov.uk/pensions. Key elements of the FSS are the Funding Objectives and Funding Strategy for the Pension Fund and these have been extracted and included below:

Funding Objectives (Section 1, page 2 of FSS)

To:

- set levels of employer contribution that will build up a fund of assets that will be sufficient to meet all future benefit payments from the Fund;
- build up the required assets in such a way that produces levels of employer contribution that are as stable as possible;
- ensure effective and efficient management of employer's liabilities; and
- allow the return from investments to be maximised within reasonable risk parameters.

Funding Strategy (Section 3, page 4 of FSS)

The funding strategy seeks to achieve (via employee and employer contributions and investment income) two key objectives:

- A funding level of 100%, as assessed by the Fund's appointed actuary, triennially, in accordance with the Regulations; and
- As stable an employer contribution rate as is practical

2014 Actuarial Valuation

The 2014 Actuarial Valuation was undertaken for the Fund as at 31 March 2014 and was completed during the financial year 2014/15 by the Fund's actuaries, Barnett Waddingham. It has been undertaken in accordance with Regulation 32 of the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008.

The funding level of the Fund as at the 31 March 2014 was 101%, above the valuation as at 31 March 2011 and this corresponded to a surplus of £2.9m. The following table summarises the funding position.

Past Service Funding Position – Scottish Borders Council Pension Fund		
Valuation Date as at 31 March	2011 £m	2014 £m
Value of the Scheme Liabilities	(402.2)	(487.6)
Smoothed Asset Value	384.8	490.5
Surplus/ (Deficit)	(17.4)	2.9
Funding Level	96%	101%

The value of the scheme liabilities is an estimate of the assets required to pay pensions over the coming years. The smoothed asset value is the contributions received from employers and members as well as investment returns. The surplus or deficit on the Fund is the difference between the two.

The next detailed actuarial valuation will be carried out for the Fund as at 31st March 2017.

New LGPS Benefits Impact on Benefits Projections

The Actuarial Valuation Report identified the estimated additional pension and lump sum benefits projected to come into the payments of benefits in each year during the period 1 April 2015 to 31 March 2018 as a result of the changes to the LGPS benefits. These are set out as follows:

Financial year	Additional Retirement Benefits	<i>Increase versus 2014/15 Base</i>
2014/15 Base (per Note 8)		19.1
2015/16	3.4	17.8%
2016/17	5.2	27.2%
2017/18	5.4	28.3%

Valuation Assumptions

The valuation of the Fund has been undertaken using the projected unit method under which the salary increase for each member is assumed to increase until they leave active service by death, retirement or withdrawal from service.

Financial Assumptions

The principal assumptions used in the last triennial valuation (to March 2014) were:

	2011 Valuation		2014 Valuation	
	% p.a.	Real % p.a.	% p.a.	Real % p.a.
Investment Return				
Equities/absolute return funds	6.9	3.4	5.9	2.6
Gilts	4.3	0.8	3.6	-
Bonds	5.5	2.0	4.1	0.5
Property	5.5	2.0	5.5	1.9
Multi Asset Fund	-	-	5.9	2.3
Expense Allowance				
Retail Price Inflation (RPI)	3.5	-	3.6	-
Pay Increases – Long Term	5.0	1.5	4.6	2.0
Pension Increases	3.0	(0.5)	2.8	(0.8)
Discount Rate	6.4	2.9	5.5	1.9

Mortality assumptions

The mortality assumptions used and applied to all members are those underlying the S1PA mortality tables allowing for Continuous Mortality Investigation (CMI) 2013 projections, with a long term rate of improvement 1.5%.

Commutation Assumption

It is assumed that future retirees will commute pension to provide a lump sum of 50% of the maximum allowed under HMRC rules.

Employer Contribution Rates

As part of the 2014 Actuarial Valuation, the actuary certified the common rate of contribution as 18% of payroll for the next three years.

Individual and pooled employers' rates vary from the common contribution rate (18.0%) depending on the demographic and actuarial factors particular to each employer. The table below highlights the key employer contribution rates (i.e. the rate which employers in the Fund pay):

Employers Contribution Grouping	Employers Contribution Rate	
	2015/16	2015/16 to 2017/18
Scottish Borders Council Common Pool	18.0%	18.0%
Leisure Trusts Common Pool *	15.5%	15.5%
Scottish Borders Housing Association – Individual	-	19.0%

* During the inter-valuation period the Pension Fund Committee agreed, in consultation with the actuary, to reduce the rate for Borders Sport and Leisure Trust in order that they would undertake work to open up the LGPS scheme to their employees again. This was set at 15.5% until the outcome of the 2014 Actuarial Valuation.

21 ACTUARIAL PRESENT VALUE OF PROMISED RETIREMENT BENEFITS

In addition to the Triennial Funding Valuation, the Fund's actuary also undertakes a valuation of pension fund liabilities (actuarial present value of promised retirement benefits) at the accounting date as required by International Accounting Standard (IAS) 26, and calculated in line with IAS 19 assumptions.

This uses the same base data as the Triennial Funding Valuation rolled forward to the current financial year, taking account of changes in membership numbers and updating assumptions to the current year. This valuation is not carried out on the same basis as that used for setting Fund employer contribution rates and the Fund Account does not take account of liabilities to pay pensions and other benefits in the future.

The actuarial present values, calculated in line with IAS 19, are set out in the table below.

	Net Pension Asset as at:		
	31 March 2014 £m	31 March 2015 £m	31 March 2016 £m
Present value of the defined benefit obligations	(713.9)	(716.6)	(696.9)
Fair Value of Fund Assets* (bid value)	475.9	537.4	542.7
Net Asset/(Liability)	(238.0)	(179.2)	(154.2)

This figure is used for statutory accounting purposes by the Fund and complies with the requirements of IAS 26. The assumptions underlying the figure are detailed below:

	At 31 March 2014		At 31 March 2015		At 31 March 2016	
	% p.a.	% p.a.	% p.a.	Real % p.a.	% p.a.	Real % p.a.
Discount Rate	4.5	0.8	3.3	0.1	3.7	0.4
Retail Price Inflation (RPI)	3.7	-	3.2	-	3.3	-
Pay Increases – Long Term	5.1	1.4	4.2	1.0	4.2	0.9
Pension Increases	2.9	(0.8)	2.4	(0.8)	2.4	(0.9)

As noted above, the liabilities above are calculated on an IAS 19 basis and therefore will differ from the results of the 2014 Triennial Funding Valuation (see Note 20) because IAS 19 stipulates a discount rate rather than a rate that reflects the market rate for investment returns on the Fund's assets.

22 CONTINGENT ASSETS

One of the admitted body employers in the Pension Fund holds an insurance bond to guard against the possibility of being unable to meet their pension obligations. These bonds are drawn in favour of the Pension Fund and payment will only be triggered in the event of employer default.

23 POST BALANCE SHEET EVENTS

On 23 June 2016, the result of the Referendum on membership of the European Union (EU) was a majority vote to leave. This resulted in initial increase volatility in some markets. The longer term effect on the investments held and inflation on the liabilities is currently unknown and the Pension Fund's longer term investment strategy, which is currently under review, will evolve as the implications of these changes emerge.

INDEPENDENT AUDITOR'S REPORT

Independent auditor's report to the members of Scottish Borders Council as administering body for Scottish Borders Council Pension Fund and the Accounts Commission for Scotland

We certify that we have audited the financial statements of Scottish Borders Council Pension Fund ("the Fund") for the year ended 31 March 2016 under Part VII of the Local Government (Scotland) Act 1973. The 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 International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 (the 2015/16 Code).

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 125 of the Code of Audit Practice approved by the Accounts Commission for Scotland, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Respective responsibilities of the Chief Finance Officer of Scottish Borders Council and auditor

As explained more fully in the Statement of Responsibilities, the Chief Finance Officer is responsible for the preparation of financial statements and for being satisfied that they give a true and fair view. Our 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) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. Those standards require us 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 Chief Finance Officer; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report and accounts to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view in accordance with applicable law and the 2015/16 Code of the financial transactions of the fund during the year ended 31 March 2016, and of the amount and disposition at that date of its assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2015/16 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Independent auditor's report to the members of Scottish Borders Council as administering body for Scottish Borders Council Pension Fund and the Accounts Commission for Scotland
(continued)

Opinion on other prescribed matter

In our opinion the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We are required to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit; or
- the Annual Governance Statement 2015/16 has not been prepared in accordance with Delivering Good Governance in Local Government; or
- the Governance Compliance Statement 2015/16 does not comply with guidance from the Scottish Ministers.

We have nothing to report in respect of these matters.

Hugh Harvie
for and on behalf of KPMG LLP
Chartered Accountants
Saltire Court, 20 Castle Terrace, Edinburgh, EH1 2EG
29 September 2016

STATEMENT OF INVESTMENT PRINCIPLES

The key aspects of the Statement of Investment Principles (SIP) for the Scottish Borders Council Pension Fund are set out below. The full SIP was approved by the Pension Fund Committee on 18 June 2015 and a copy of this document can be found at: www.scotborders.gov.uk/pensions

1. The Fund's Objectives (Section 3, page 4 of SIP)

Primary Aim

1.1 The primary aim of the Fund is:

“To provide for members’ pension and lump sum benefits on their retirement or for their dependants’ benefits on death before or after retirement, on a defined benefits basis.”

In order that this primary objective can be achieved, the following funding and investment objectives have been agreed.

Funding Objectives

1.2 The funding objectives are set out in the Funding Strategy Statement (the FSS) and are as follows:

- i To set levels of employer contribution that will build up a Fund of assets that will be sufficient to meet all future benefit payments from the Fund.
- ii To build up the required assets in a way that produces employer contributions, which are as stable as possible.

1.3 The funding objectives must complement the Fund's investment strategy so that the appropriate amount of risk is adopted in the pursuit of investment returns.

2. Investment Policy (Section 4, page 6 of SIP)

Investment Strategy

2.1 The Investment Strategy's primary aim is to deliver the funding objective in 1.2 ii) above which is to build up the required assets in a way that produces stable employer contributions to the Fund.

2.2 The Committee in pursuing this primary aim will, as far as is practicable and as an aid to long-term stability, seek to maintain a positive ratio of assets to liabilities at each actuarial valuation.

2.3 The Funding Strategy Statement (FSS) states that the discount rate that is adopted in the actuarial valuation of the Fund's liabilities is derived by considering the expected return from the underlying investment strategy but makes no allowance for additional returns from active management. The strategic benchmark that is established for the Fund's investment strategy is therefore expected to produce a return over the long term in excess of the investment return assumed in the triennial Actuarial Valuations.

2.4 The Fund's current **total target is to generate a return of at least 2.7% above CPI inflation** assumed as the real discount rate at the actuarial valuation as at 31 March 2014.

3. Types of Investment (Section 5, page 9 of SIP)

3.1 The Fund has approval from the Committee to use the following different types of investment and income generating mechanisms to achieve the overall investment objectives:

- Equities (UK, Overseas and Global mandates including direct holdings, Managed Funds, Unit trusts, Investment Trusts, Open Ended Investment Companies)
- Bonds
- UK Property
- Currency
- Alternative assets such as commodities, hedge funds, infrastructure, emerging market debt, private equity, high yield debt and convertible bonds.
- Cash (including Treasury Bills and Money Market Funds)
- Derivatives and other Managed transactions

3.2 Stock Lending is not currently authorised by the Committee for the directly held investments under the custody of its custodian

4. Investment Management Arrangements (Section 4, page 6 of SIP)

4.1 The agreed Strategic Asset Allocation for the Fund is currently as follows (Appendix 3, page 13 of SIP):

Asset Class	Manager	Strategic Benchmark %
UK Equity	UBS	12.6%
	Baillie Gifford	6.4%
Global Equity	Sub Total	19.0%
	Harris Associates	9.9%
	Baillie Gifford	21.7%
	Morgan Stanley	14.4%
	Sub Total	46.0%
Total Equity		65.0%
Bonds		
Alpha Opportunities	M&G	10.5%
Govt. Fixed Interests Bonds	M&G	2.25%
Corporate Fixed Interest Bonds	M&G	2.25%
	Total	15.0%
Alternatives		
Multi-Asset Alternatives Fund	LGT Partners	15.0%
Property	UBS	5.0%
	Total	20.0%
Cash		0.0%
Total		100.0%

- 4.2 The investment managers are responsible for the selection of individual holdings within each type of investment category within the parameters set out in their agreement which includes the need to achieve targets which are measured.
- 4.3 The current investment management arrangements are set out below (Appendix 4, page 14 of SIP)

Asset Class	Manager	Performance Objective (all net of fees) relative to Benchmark Return	Benchmark Indices Used	
UK Equity	UBS	+0.0%	FTSE All-Share Index	
	Baillie Gifford	+1.0%	FTSE All-Share Index	
Global Equity	Harris Associates	+2.5%	MSCI AC World Total Return Index	
	Baillie Gifford	+2.5%	MSCI AC World Total Return Index	
	Morgan Stanley	Not Defined	MSCI World Total Return Index	
Bonds	Alpha Opportunities	M&G	+3.5% - 5%%	1 Month LIBOR
	Govt Fixed Interest Bonds	M&G	+0.75%	FTSE Actuaries UK Conventional Gilts All Stock Index
	Corporate Fixed Interest Bonds	M&G	+0.8%	iBoxx Sterling Non-Gilts Index
Multi-Asset Alternatives Fund	LGT Partners	+4.0%	1 Month LIBOR	
Property	UBS	+0.75%	IPD UK PPFI All Balanced Funds Index	

5. Risk Measurement and Management (Section 4, page 6 of SIP)

5.1 Asset Allocation (Section 4.19 of SIP)

The asset allocation risks are assessed triennially, typically using asset liability modelling techniques following the actuarial valuation of the Fund, after which the Committee take advice on the continued appropriateness of the existing investment strategy.

5.2 Investment Managers (Section 4.20 of SIP)

To reduce the risk that the Fund significantly underperforms, performance and risk targets and controls are set for each manager relative to their benchmark.

The investment managers are required to provide data monthly and report quarterly on portfolio management issues. This information is reported to the Committee on a quarterly

basis. The monitoring includes assessing their achievement of performance that meets or outperforms their individual targets.

5.3 Proper Advice (Section 4.21 of SIP)

The Committee is required to secure proper advice to ensure that their decision making processes are appropriately informed. The current advisers to the Fund are:

Investment Consultant: AON Hewitt Ltd to March 2016, KPMG from April 2016

Actuaries: Barnett Waddingham

5.4 Concentration Risk and Diversification (Section 4.22 of SIP)

Concentration risk arises from the failure of any investments which constituted a significant proportion of the Fund's assets. In order to reduce this risk a spread of assets is held.

Diversification is used to manage the risk involved in pursuing an active management approach to a substantial part of the fund. This is achieved through diversification of investment over various types of asset, by the use of at least two managers with different styles or specialism, and by requiring a wide range of individual stocks and shares to be held.

5.5 Transition Management Arrangements (Section 4.23 of SIP)

The use of a specialist transition manager, currently State Street Global Markets, is intended to reduce the cost of transition to the Fund and minimise the overall impact on the Fund value at the point of transition.

5.6 Currency Risk (Section 4.24 of SIP)

A Passive Currency Hedging mandate to hedge 50% of the currency exposure is in place within the overseas equity portfolios. The key purpose of this is to reduce the short term volatility in the Fund's asset valuations which results from currency movements.

5.7 Safe Keeping of Assets (Section 4.25 of SIP)

The services of a global custodian, currently J.P. Morgan, are employed to ensure the safeguarding of the Fund's assets and ensure that all associated income is collected.

5.8 Cashflow Risk and Realisation of Investments/Liquidity (Section 4.26 of SIP)

The overall liquidity of the Fund is considered in the light of potential demands for cash. The Fund will hold sufficient cash to meet the likely benefit payments. Additionally, the Fund will hold sufficient assets in liquid or readily realisable form to meet any unexpected cashflow requirements so that the realisation of assets will not disrupt the Fund's overall policy.

6. Environmental, Social and Corporate Governance Issues (Section 6, page 9 of SIP)

- 6.1 The Committee believes that environmental, social and governance issues can affect the financial performance of companies and that it has a responsibility to take these issues seriously and where appropriate, to act upon them.
- 6.2 The Committee considers engagement with companies in which the Fund invests to be the most effective means of understanding and influencing the social, environmental and business policies of those companies. The investment managers for the Fund are therefore encouraged to constructively engage with companies on issues which are consistent with the Fund's fiduciary responsibilities.

- 6.3 The Committee recognises its responsibility to exercise voting rights to ensure transparency and accountability in corporate governance.
- 6.4 The Fund's investment managers maintain close contact with the management of companies in which investments are held or contemplated and subject their affairs to considerable analysis and skilled scrutiny. In recognition of this activity, the Sub-Committee delegates to its managers all its voting and other rights attaching to Fund investments.
- 6.5 The investment managers have delegated powers to exercise such rights in the best financial interests of the Fund and would, in particular, expect them to vote appropriately at company Annual General Meetings (AGMs) and Extraordinary General Meetings (EGMs).
- 6.6 The Committee has, however, drawn the attention of managers to its general concern that the remuneration practices of companies should be patently fair and reasonable. It has asked that managers reflect such concern when voting shares in companies in which the Fund is directly invested. The Committee is content to allow its managers discretion on the voting of in-house pooled fund shares subject to referring any matters relating to the remuneration of Fund managers to it for direction.
- 6.7 The key highlights in terms of voting actions taken by investment managers is included as part of the quarterly investment manager report to the Committee by AON Hewitt.

7. Compliance with the Myners principles (Section 8, page 10 of SIP)

- 7.1 The statement of compliance with the six principles is set out in Appendix 5, page 15 of the SIP. It demonstrates that the Fund is in full compliance with all the six principles of:
 - i Effective Decision Making
 - ii Clear Objectives
 - iii Risk and Liabilities
 - iv Performance Assessment
 - v Responsible Ownership
 - vi Transparency and Reporting

GLOSSARY OF TERMS

ACTIVE MANAGEMENT

An investment management style that seeks to outperform by way of self-selected decisions on stock choice, timing of market incursions, or asset allocation. Compare this with Passive Management.

ASSET ALLOCATION

The division of the Fund's assets between different classes of assets, for example, UK Equities, Japanese Equities, UK Bonds. In the long run the asset allocation choices should support the Fund's strategic financial objectives. In the short term tactical changes might be made to achieve short-term advantage.

ALTERNATIVE ASSETS

This is any non-traditional asset with potential economic value that would not be found in a standard investment portfolio. Due to the unconventional nature of alternative assets, valuation of some of these assets can be difficult.

BALANCED MANAGEMENT

An arrangement under which investments are spread over a range of asset classes at the manager's discretion. The manager controls investments over as many classes as are available under the Fund's overall strategy. Compare this with specialist management.

BENCHMARK RETURN

This is calculated against the Fund's chosen "benchmarking" group, which comprises a composite of different market indices. The indices in use cover all the markets in which the Fund is invested.

CONTRIBUTING MEMBER

This is someone who is currently employed by a scheduled or admitted body and is making contributions from pay to the Pension Scheme. Such a person is sometimes referred to as an "active" member.

DEFERRED MEMBER

This is someone who was once a contributing member and who has chosen to leave his or her accumulated contributions in the Fund to benefit from a pension in due course.

GROWTH MANAGER

An investment manager who fundamentally believes in picking stocks that he believes will achieve an above-average growth in profits. This is sometimes caricatured as buying stock irrespective of price because the price will rise. Compare this with value manager.

INVESTMENT MANAGER/FUND MANAGER

A person or organisation that makes investments in portfolios of securities on behalf of clients, in accordance with the investment objectives and parameters defined by these clients

MANDATE

An agreement between an investment manager and his client as to how investments are to be managed, specifying whatever targets and investment limitations are to apply.

PASSIVE MANAGEMENT

A style of investment management that seeks performance equal to market returns or to some appropriate index. Such investment entails a more mechanical approach to asset allocation and stock selection because such decisions are largely dictated by general market shifts rather than individual manager discretion. Compare this with active management.

PENSIONER/DEPENDENT MEMBER

This is someone who is receiving benefits from the Fund either as a former contributor or as a dependent of a former contributor who has deceased.

POOLED FUND

A fund in which a number of investors hold units rather than owning the underlying assets. This is a useful way for smaller funds to diversify investments without exposing them to undue risks. Unit Trusts are pooled funds as are Open-ended Investment Companies. Compare this with segregated fund.

REALISED GAIN OR LOSS

Only when an investment is sold does the Fund actually make a profit or loss.

Realised profits and losses are those that have actually arisen via sales throughout the year.

RETURN

The value of capital enhancement and income received by a fund in a year, expressed as a percentage of the opening value of the fund. If values fall "Return" would be negative.

RISK

The danger or chance that returns will vary against benchmarks or targets. If risks are high the expected return should be higher still (the risk premium).

SEGREGATED FUND

The management of a particular fund's assets independently of those of other funds managed by the same investment house. Compare this with a pooled fund.

SPECIALIST MANAGEMENT

The use of a number of managers, each specialising in a particular asset class. Such managers have no say in asset allocation, being only concerned with stock selection.

UNREALISED GAIN OR LOSS

The Statements of Accounts are based on the market value of investments at 31 March 2016. This means that these show what profit or loss would have made if the Fund had sold all its investments on that day. The result is a notional "unrealised" profit or loss.

VALUE MANAGER

A manager who selects stocks that he believes to have potential that is not reflected in the price. This is sometimes caricatured as buying stock because it is cheap. Compare this with growth manager.

VESTED/NON VESTED OBLIGATIONS

Vested obligations refer to employee benefits that are not conditional on future employment. Non vested obligations refer to employee benefits that are conditional on future employment.

PENSION FUND STRAIN

The cost to employers of the early release of pension benefits.

ADDITIONAL INFORMATION

Key Documents Online

You can find further information on our website, www.scotborders.gov.uk/pensions, including the following documents:

- Funding Strategy Statement
- Annual Report and Accounts
- Governance Policy and Compliance Statement
- Statement of Investment Principles
- Training Policy
- Business Plan 2015/16 to 2017/18
- Actuarial Valuation Statement 2014

Fund Advisers

Actuaries:	Barnett Waddingham
Auditors:	KPMG
Bankers:	Bank of Scotland
Investment Consultancy:	AON Hewitt to 31 March 2016, KPMG from 12 April 2016
Investment Custodians:	JP Morgan
Investment Managers:	Baillie Gifford, UBS, Morgan Stanley, LGT Partners, M&G and Harris Associates
Additional Voluntary Contributions (AVC) Managers:	Standard Life

Contact Details

For further information and advice on administration, benefits and scheme membership please contact

Graeme Wilson	Telephone 01835 – 824000	Ext 5341
	E-mail gwilson@scotborders.gov.uk	

Scheme members should have a copy of the “Employees’ Guide to the Local Government Pension Scheme Administered by the Scottish Borders Council”, and can obtain their own copy of an Annual Report on request.

or visit Scottish Borders Council Pension Fund website at: www.scotborders.gov.uk/pensions

For further information on the Fund’s investments, please contact

Lynn Mirley	Telephone 01835 – 825016
Corporate Finance Manager	E-mail lmirley@scotborders.gov.uk

You can get this document on audio CD, in large print, and various other formats by contacting us at the address below. In addition, contact the address below for information on language translations, additional copies, or to arrange for an officer to meet with you to explain any areas of the publication that you would like clarified.

Contact us at Lynn Mirley, Corporate Finance Manager, Corporate Finance, Council Headquarters, Newtown St Boswells Melrose TD6 0SA
Tel: 01835 825019 Fax: 01835 825011 or email: lmirley@scotborders.gov.uk