ISLINGTON

ISLINGTON COUNCIL PENSION FUND

STATEMENT OF INVESTMENT PRINCIPLES

LEGAL BACKGROUND

1 This Statement sets out the policy of the Council towards investment and management of the Pension Fund assets, as required by regulation 9A (1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 as amended. This Statement will be updated regularly and when material changes are made to the strategic asset allocation.

2 Regulation 12 of the LGPS (Management and Investment of Funds) Regulations 2009, as amended, requires the Council to publish a written Statement of Investment Principles governing its decisions about the investment of fund money. This will include the extent to which it complies with the six principles of investment practice (as revised by the Government in October 2008) in response to the recommendations of the Review of Institutional Investment in the UK undertaken by Paul Myners.

3 The Council is the administering authority for the London Borough of Islington Pension Fund, within the Local Government Pension Scheme (LGPS). It is managed within the legal framework set down in the Local Government Pension Scheme regulations 1997 (LGPS Regulations 1997), as amended. The body responsible for decision making in relation to the Pension Fund is the Pensions Sub-Committee of the Corporate Services Committee.

Supplementary Information available in other Published Statements

4 Details of **governance policy** for the Fund are contained in a statement required to be published by regulation 73A of the LGPS Regulations 1997. This covers, for example, policy on delegation within the Council's committee structure, frequency of meetings, terms of reference, and representation and voting rights of committee members. This statement is available on the Council's website.

5 The Council must publish a statement of policy concerning **communications with members and employing authorities** (including non-Scheme employers) under regulation 106B of the LGPS Regulations 1997. This covers, amongst other issues, the manner of publicising the Scheme to members, and employing authorities, and how the Scheme will be promoted to prospective members and their employing authorities. This statement is available on the Council's website.

6 Finally, under regulation 76A of the LGPS Regulations 1997 and guidance from the Chartered Institute of Public Finance and Accountancy Pensions Panel, the Council has had to publish a **Funding Strategy Statement** (FSS). The FSS recognises that benefits payable under the pension scheme are guaranteed by statute and that thereby the pensions promise is secure. The FSS, however, addresses the issue of managing the need to fund those benefits over the long term, whilst at the same time, facilitating scrutiny and accountability through improved transparency and disclosure. The FSS establishes a clear strategy identifying how employers' pension liabilities are best met going forward, taking into account the regulatory requirement to maintain as nearly constant employer contribution rates as possible, whilst taking a prudent longer-term view of funding the liabilities.

THE SCHEME

Pension Fund Liabilities

7 The LGPS is a defined benefit scheme based on the final salary of scheme members. Pension benefits are defined in the Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (as amended),and are linked to a formula involving years of service and pensionable pay (the formula being different for pensionable service accrued pre and post 1 April 2008). Scheme members building up their pension benefits are required to make contributions, between 5.5% and 7.5% of pensionable pay. The rate paid depends on which pay band is applicable. Pension benefits are not linked to the investment performance of the Pension Fund.

8 The Council appoints an independent actuary who values the liabilities of the Fund and determines the level of employer contributions which must be made by the Council and other employers admitted to the Fund, to ensure that the investment assets of the Fund achieve 100% of the value placed on the liabilities. Where there is a shortfall in the value of the assets, the Council must comply with contribution rates determined by the actuary to recover full funding, and in setting these rates (expressed in a rates and adjustments certificate), section 36 of the The Local Government Pension Scheme) (Administration) Regulations 2008 (as amended states:

"(6) The actuary must have regard-

(a) to the existing and prospective liabilities of the fund arising from circumstances common to all those bodies, and

(b) to the desirability of maintaining as nearly constant a rate as possible.

(c) the current version of the administering authority's Funding Strategy Statement as mentioned in Regulation 35.. "

9 As referred to above, further detail on policy towards funding the liabilities is now contained in the Funding Strategy Statement dated 31st March 2010.

Investment Policy / Attitude to Risk

10 The Pensions Sub-Committee has adopted policies with the objective of achieving maximum growth of Pension Fund investments, to reduce the burden of employer contributions on the General Fund. This is, however, tempered by the objective of reducing extreme variations of employer contribution that could occur at any triennial revaluation of the Fund by the Fund actuary.

11 At the last triennial valuation as at 31st March 2010, the funding level or ratio of asset value to the discounted value of the liabilities was 72%. An interim review at 31 March 2011 is being undertaken, the preliminary results indicate a funding level of 73% as at 31 March 2011, and 61% as at 30 September 2011. The funding level is monitored during the intervaluation period on a quarterly basis outside of the interim review exercises..

12 The Council has agreed a strategy with the Fund actuary to return the funding level from the 31 March 2010 level of 72%, to 100% through making additional employer contributions over a period of 25 years from 31 March 2010. The balance between major asset classes in the strategic asset allocation, and particularly the weighting to equities, is expected to contribute significantly, over the longer term, to the achievement of this objective. Further detail may be found in the Funding Strategy Statement.

13 The risk profile adopted by the Pensions Sub-Committee has been established following detailed asset/liability studies of the Fund and this was most recently reviewed in 2010. These studies examined the balance of active contributing scheme members to pensioner members and deferred members (no longer employed by the Council but not yet drawing benefits), and

related this "scheme maturity" to asset allocation strategies for Fund investment. The risk of significant variation in future employer contribution outcomes could then be modelled on a variety of economic and market assumptions.

14 A strategy of limiting risk by matching to a degree the types of assets invested in, to the obligations or liabilities of the Fund has been adopted. The balance between investing for growth and investing in assets with the best fit or match to liabilities is a judgement requiring regular reappraisal.

15 Policy is determined in compliance with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998, as amended. As required by these Regulations the suitability of various types of investments has been considered, as also has the need to diversify investments to reduce the risk of being invested in too narrow a range of assets. In addition, this process has benefited from the provision of independent, professional investment advice.

16 The most significant asset allocation strategy decision for the Pension Fund has been to split assets as follows:

- 60% company shares or equities, (private and publicly quoted)
- 25% corporate bonds
- 15% property

The full asset allocation is set out in Appendix A, showing the various asset classes, the target for each asset class at the level of the total Fund, and the permitted ranges within which this may vary due to the relative movements in asset values over time.

17 Appendix B shows how this is reflected across individual portfolios, the current managers of those portfolios, and the benchmarks against which the individual manager's performance is measured. These portfolios have been established to ensure diversification, and take into account the suitability of the type of investment for the Fund, and are managed as follows:

18 **Equities**

- The Fund has made allocations to UK and overseas equities, both publicly and privately quoted, with the regional split broadly 50% UK and 50% overseas. The intention is for the allocation to UK equities to be reduced from 50% to 30% over time.

- The equity portfolio is split between a core index-tracking allocation and actively managed portfolios that target returns in excess of the relevant market index.

- **UK Equity Index Fund.** Aims to track the FTSE All Share Index which currently comprises c.98-99% of the total UK equity market capitalisation and is an aggregation of the FTSE 100, FTSE 250 and FTSE Small Cap Indices. This portfolio is passively managed to track the index within a variation of plus or minus 0.5% p.a.. This portfolio is the only portfolio managed in-house. External managers manage the other specialist portfolios.

- **Overseas equities.** Legal and General Investment Management (LGIM) manage an index-tracking overseas equity portfolio with allocations to North America, Europe (ex UK), Japan, Asia-Pacific (ex Japan) and Emerging Markets. LGIM's mandate requires them to maintain the Fund's overall allocations to each region within specific tolerance bands around a central asset allocation. Performance will be assessed for each of the regional allocations against the relevant FTSE regional index as detailed in Appendix B.

- **Global equities.** Newton and RCM manage global equity portfolios benchmarked against the FTSE All World index. The managers' targets are to achieve at least 2.0% p.a. and 3.0% p.a. outperformance respectively over their benchmarks measured on rolling three year periods net of fees.

- **Global Private Equity investments.** An allocation of up to 10% of the Pension Fund may be invested in such arrangements. The benchmark is currently a composite derived from the FTSE

US and FTSE Europe (including UK) indices. However, the weighting in the overall customised benchmark set for the whole fund is adjusted quarter by quarter to reflect the amounts actually invested in private equity. This reflects the long term nature of the investment process in this asset class. Assets notionally allocated to private equity but not yet invested will be held in the in-house UK Equity Index Fund.

19 **Bonds**

- Standard Life has been appointed to manage a corporate bond portfolio for the Fund. The benchmark for the bond portfolio is the Merrill Lynch Sterling Non Gilt All Stocks Index. The performance target is set at 0.8% p.a. outperformance of the benchmark, measured over rolling three year periods gross of fees.

- A pooled bond fund has been selected as the most appropriate investment vehicle for the Fund's investment in this asset class. Constraints apply to the types of bonds the assets can be invested in; however the Fund does not have control over these constraints.

20 **Property**

- A strategic allocation to property assets has been made of up to 15% of the total Fund value. This allocation is split between three mandates.

- 5% is invested in a defensive pooled property fund managed by Aviva Investors with a "high lease to value" approach. To reflect the low-risk characteristics of this fund, a tailored benchmark has been applied based on government bond indices. The benchmark is a composite of 50% FTSE Over 15 Year Gilts Index and 50% FTSE 5-15 Year Gilts Index.

- 6% is invested in a conventional (or "core") pooled property fund managed by Threadneedle which invests in UK offices, industrial and retail properties. The fund aims to outperform the CAPS UK Pooled Property benchmark by 1.0% (net of fees) over rolling three year periods.

- Up to 4% is committed to be invested in a closed ended Private Equity Real Estate fund of funds managed by Franklin Templeton and which will be invested in equity or debt-related real estate investments around the globe. The fund's investment objective is to achieve an internal rate of return of 15% over the term of the fund (net of all management fees and carried interest).

21 **Other Investments**

- The risk exposure from currency fluctuations associated with the overseas equity portfolios is managed through a passive hedging programme, targeted on the major currencies. The passive hedging is implemented by BNY Mellon at a level of 50% of the overseas developed market currency exposure arising from equity holdings outside the UK.

22 Managers are currently remunerated through fee scales based on percentage rates applied to the market value of funds under management. In most cases the rate reduces for funds under management above threshold values. Performance-related fee structures have been taken into account on retendering of fund manager contracts.

Exercise Of Shareholder Rights (Including Voting Rights)

23 The Pensions Sub-Committee takes its responsibilities as a company shareholder seriously and exercises its votes at company AGMs/EGMs wherever practically possible. The Panel has decided to use the Corporate Governance Service provided by Pension Investments Research Consultants (PIRC), and votes cast at UK, European and North American company AGMs will follow PIRC recommendations unless specifically agreed otherwise.

24 The Pensions Sub-Committee has also agreed a policy to extend voting to include its share holdings in the FTSE All Share and FTSE All World indices and currently uses the PIRC global research service to achieve this.

Social, Environmental or Ethical Considerations

25 The Pensions Sub-Committee takes the view that well-managed companies that evaluate and assess their social and environmental risks are likely to add shareholder value in the long term more successfully than companies that do not manage these risks. The Council continues to monitor its policies on socially responsible investment issues and will increase the use of its position as shareholder to actively engage with companies by appropriate means collectively or directly, to ensure best practice in the management of these risks and in line with the Council's 'Fairer Islington' corporate policy, and in particular the key policy objectives of promoting sustainability and regeneration.

26 The Pensions Sub-Committee has also decided to join with other local authorities to use its shareholder rights in a responsible manner to influence company behaviour, through membership of the Local Authority Pension Fund Forum (LAPFF), and supports the mission statement of the LAPFF:

27 "The LAPFF exists to promote the investment interests of local authority pension funds, and to maximise their influence as shareholders to promote corporate social responsibility and high standards of corporate governance amongst the companies in which they invest, commensurate with statutory regulations"

28 The Pension Sub-Committee is a member of the Institutional Investors Group on Climate Change (IIGCC). The IIGCC seeks to promote better understanding of the implications of climate change amongst its members and other institutional investors. It also aims to promote a lower carbon economy by encouraging the companies and markets in which IIGCC members invest to address their approach to climate change issues.

November 2011

Myners Investment Principles - Compliance Statement

In accordance with regulation 9A(3A) of the LGPS (Management and Investment of Funds) Regulations 1998, as amended the Council is required to state the extent to which the administering authority comply with the ten principles of investment practice set out in the document published in April 2002 by CIPFA, the Chartered Institute of Public Finance and Accountancy, and called "CIPFA Pensions Panel Principles for Investment Decision Making in the Local Government Pension Scheme in the United Kingdom (Guidance note issue No. 5)"; and give the reasons for not complying where they do not do so. This CIPFA publication is based on ten principles proposed by the Myners review of Institutional Investment in the United Kingdom, and adopted by the Government as a model for best practice in 2001.

The Myners Principles were reviewed by the NAPF during 2008 and a revised set of six principles were issued in October 2008. CIPFA expect to issue a new publication based on the revised six principles in the near future.

Principle 1 - Effective decision-making

- Trustees should ensure that decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to take them effectively and monitor their implementation.
- Trustees should have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.

Comment

The Fund is generally compliant with the requirements of this Principle. The Pensions Sub-Committee requires new members serving on the Sub-Committee to source appropriate training within six months of joining the Sub-Committee. The three-day course run by the Local Government Pensions Committee of the Employers Organisation is recognised as particularly relevant training for new Members, but other routes and courses, and requisite experience are also recognised as appropriate. Where several new Members are appointed together, tailor-made training will be considered.

Principle 2 - Clear Objectives

- Trustees should set out an overall investment objective(s) for the Fund that takes account of the scheme's liabilities, the strength of the sponsor covenant and the attitude to risk of both the trustees and the sponsor, and clearly communicate these to advisers and investment managers.

Comment

The Council seeks to undertake regular reviews of investment strategy, most recently in 2007, which take into account the scheme's liabilities, the strength of the employer covenant and the attitude to risk of both the trustees and the sponsor.

Principle 3 - Risk and Liabilities

- In setting and reviewing their investment strategy, trustees should take account of the form and structure of liabilities.
- These include the strength of the sponsor covenant, the risk of sponsor default and longevity risk.

Comment

In setting the investment strategy, the Trustees have considered the form and structure of liabilities, along with the strength of the sponsor covenant, risk of sponsor default and longevity risk, taking advice from independent professional advisors where appropriate.

Principle 4 - Performance Assessment

- Trustees should arrange for the formal measurement of the performance of the investments, investment managers and advisers.
- Trustees should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.

Comment

Overall Fund performance and detailed portfolio performance is measured quarterly, annually and over longer periods by external independent measurement specialists (WM Company). Performance is also monitored against the local authority peer group of pension funds, also based on WM Company data (for the local authority universe), although in line with the Myners Principles the peer group is no longer considered the benchmark for overall fund performance. The overall benchmark is specific and customised to the Fund's objectives based on the outcome of the successive asset/liability studies.

Performance of the Fund is also subject to annual review by external auditors (the District Audit service) and by internal audit through regular audits programmed into the Audit Plan.

Pension benefits administration performance is reported regularly to Pensions Sub-Committee.

Principle 5 - Responsible Ownership

- Trustees should adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee Statement of Principles on the responsibilities of shareholders and agents.
- A statement of the scheme's policy on responsible ownership should be included in the Statement of Investment Principles.
- Trustees should report periodically to members on the discharge of such responsibilities.

Comment

The Fund uses the proxy voting service, PIRC, to vote for the shares held within FTSE All Share and FTSE World indices.

RCM, who manage a global equity mandate, use the proxy voting service Shareholder Services (ISS) to vote on all other shares held on behalf of the Fund.

Newton, who manage a global equity mandate, vote in all other indices at their discretion.

The Fund encourages each active investment manager to take account of social, environmental and ethical considerations insofar as the manager believes such considerations will benefit performance and/or reduce risk.

For those assets of the Scheme managed in pooled funds, the Trustee accepts that the assets are subject to the investment manager's own policy on socially responsible investment. The Trustee is satisfied that this corresponds with its responsibilities to the beneficiaries.

The Fund's attitude to and policies regarding responsible ownership are set out within the body of the Fund's Statement of Investment Principles.

The Trustees issue member newsletters in which this discharge of responsibilities is noted.

Mercer has adopted the Institutional Shareholders' Committee Statement of Practice relating to investment consultants.

Principle 6 - Transparency and Reporting

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

Comment

The Council's SIP is currently published and available to scheme members on the Council website. Summaries of performance and monitoring of managers are reported in the Pension Fund Annual Report and distributed to employees each year with payslips. Further performance reporting is provided to contributors and pensioners at the AGM. The full Pension Fund Report and Accounts are published as part of the Council's overall Annual Report and Accounts and available to all members of the public.

Overall communication and publicity strategy for the Fund is set out in the Communications Policy Statement which is available on the Council's website.

APPENDIX A

From November 2011

STRATEGIC ASSET ALLOCATION	Target	i.e Permitted Range +/- %
UK Equities	25.0%	3.0%
Overseas Equities (50% currency hedged)	25.0%	3.0%
Global Private Equity	10.0%	2.0%
Total Equity	60.0%	6.0%
Corporate Bonds	25.0%	2.5%
Property	15.0%	2.0%
Cash	0.0%	0.0%
Total bonds/property/cash	40.0%	4.0%
Total	100.0%	

NB i) Both the private equity and property allocations are target allocations and are expected to be reached once committed assets are called and invested by the relevant investment managers. In the interim, the assets will be held in the UK Equity Index Fund.

ii) Over time the listed equity allocation will be adjusted from 25% UK and 25% overseas to 15% UK and 35% overseas.

APPENDIX B

Portfolio	Manager(s)	Sector/Market	Target Weight within portfolio at 11/2011	Permitted Range	Index
UK Index Fund	In-house	UK Equity	100%		FTSE All Share
Overseas Equity	LGIM	Regional overseas equity *:			
		i) North America	40%	+/- 4.0	FTSE AW Developed North America
		ii) Europe (ex UK)	16%	+/- 1.5	FTSE AW Developed Europe (ex UK)
		iii) Japan	7%	+/- 1.0	FTSE AW Japan
		iv) Asia Pacific (ex Japan)	7%	+/- 1.0	FTSE AW Developed Asia Pacific (ex Japan)
		v) Emerging Markets	30%	+/- 3.0	FTSE AW All Emerging
Global Equity	i) RCM	Global	40%	+/- 10.0	FTSE All World Index
	ii) Newton	Global	60%	+/- 10.0	
Global Private Equity	i) Standard Life (private Equity) Ltd	Europe	50%	+/- 10.0	FTSE US
	ii) Pantheon	US	50%	+/- 10.0	FTSE Europe inc UK
Bond Portfolio	Standard Life	UK Non-Government	100%		Merrill Lynch Sterling Non Gilt All Stocks
Property Portfolio	i) Aviva Investors	HLV Property (Lime Property Fund)	33%		Composite Gilt index: 50% FTSE Over 15 yr Gilts 50% FTSE 5-15 yr Gilts
	ii) Threadneedle	Core UK Property	40%		CAPS Pooled Property
	iii) Franklin Templeton	Global real estate fund of funds	27%		n/a

* LGIM manage their own regional allocations so as to maintain the overall Fund allocation to be in line with the stated target weights. In order to do this they take into account the value of RCM and Newton's portfolios and the regional allocations of the FTSE All World index.