



The Highland Council Pension Fund
Annual Report & Statement of Accounts
Aithris Chunntasan

2013 - 2014

Pensions Regulator Scheme Number: 10051259

HIGHLAND COUNCIL PENSION FUND 2013/14

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Foreword by Director of Finance

It is my pleasure to present the Annual Report and Statement of Accounts of the Highland Council Pension Fund (“the Fund”) for 2013/14.

The Fund is a Local Government Pension Scheme (LGPS), established to provide retirement and death benefits to employees within the scheme. The Fund provides benefits for those employees of the Highland Council, Comhairle Nan Eilean Siar and of 34 other scheduled and admitted bodies that are active members of the Fund. During 2013/14, two bodies (Torvean Golf Club and Highlands and Islands Structural Partnership) ceased membership of the Fund.

The Fund has 11,850 Contributors, 7,665 Pensioners and 7,832 Deferred Pensioners.

Against a backdrop of continued uncertainty in the global economy, and volatility in the financial markets, the Fund had a positive year in terms of investment performance, with investment benchmarks exceeded overall, and the value of the Fund’s net investment assets increasing by 8% to £1,268m (2012/13 £1,173m).

More information on the economic and market environment during the year, and the Fund’s investment performance, is set out later in this report on page 11.

Total contributions income received from employers and employees totalled £50.578m for the year, a slight increase on the previous year’s £48.689m.

Total benefits paid to scheme beneficiaries, in the form of pensions or other benefits, totalled £43.101m, compared to £40.776m for the previous year.

The Fund remains in a positive cashflow position, with benefits payable and other outgoings more than covered by the inflow of income from members, employers and others involved in the scheme. There was a net £5.796m addition from dealing with scheme members (£6.783m previous year).

The Financial Statements for the Fund are prepared in accordance with International Financial Reporting Standards. The Fund is a separate entity from the Highland Council, and therefore its accounts are not included in the Council’s Core Financial Statements.

The Highland Council is the administering authority for the Fund.

The Statement of Accounts

The following key financial statements are included within the Statement of Accounts:

Pension Fund Account

The Pension Fund Account sets out all income and expenditure of the Pension Fund.

Net Assets Statement

The Net Assets Statement sets out the value, as at the Statement date, of all assets and liabilities of the Fund. The net assets of the Fund (assets less liabilities) represent the funds available to provide for pension benefits at the statement date.

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Accounting Policies and Notes to the Accounts

Explanations are provided for the basis of the figures included within the Accounts, and the accounting policies adopted, particularly where there is more than one acceptable basis. Notes are provided to set out further details of certain items included within the key financial statements.

Actuarial Valuations

Every three years, an independent actuary undertakes a valuation of the Pension Fund. The main purpose of the valuation is to review the financial position of the Fund and to determine the rate at which the employing bodies participating in the Fund should contribute in the future, to ensure that the existing assets and future contributions will be sufficient to meet future benefit payments from the Fund.

The most recent concluded triennial Valuation was as at 31 March 2011. This resulted in the funding level showing a slight decline since the 2008 valuation (97% compared to 98%) due to a number of factors, but primarily due to lower than assumed investment returns. However, this negative effect was mitigated by future pension increases being linked to CPI (rather than RPI), later retirement age plans and short term pay adjustment to reflect continued public sector pay restraint in the short-term. Details of that triennial Valuation are included in the Actuarial Position set out on page 17.

Work is ongoing on the current triennial valuation, which will be as at 31 March 2014. That exercise is expected to conclude late 2014/early 2015.

Looking Ahead

Looking ahead, there are a number of challenges facing Local Government Pension Schemes:

- Reform of the Local Government Pension Scheme in Scotland, based on a career average rather than final salary, will be implemented in April 2015. The move towards a career average salary is likely to have significant implications for the Fund in relation to the transition to and administration of a new scheme, as well as implications in relation to the Fund's assets, liabilities, and future funding requirements.
- Auto enrolment commenced for some of the Fund's larger employers from April 2013, resulting in eligible employees who had previously not been part of a workforce pension scheme, being automatically enrolled. The effect of auto-enrolment for The Highland Council was that 450 employees were taken into the Local Government Pension Scheme, 53 of who subsequently opted out within the 3 month opt out window. The Pension Administration team continues to work with employers to assist with the implementation of auto enrolment.
- The formation of the new Scottish Police & Fire Services from April 2013 has resulted in the transfer of the administration of the Police and Fire Pension Schemes to the Scottish Public Pension Agency by March 2015. The Highland Council Pension and Payroll teams are working with the SPPA and pension software providers to deliver the transfer on schedule.
- The on-going volatility and uncertainty in the global economy and investment markets, and linked to that the continuing regime of public sector austerity over the medium and quite possibly longer term. These issues have significant implications for the Fund and Fund employers.

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In Conclusion

My thanks and appreciation is extended to all Councillors and Officers for their continued input to the strong governance and management arrangements of the Fund.

Derek Yule B.Com. CPFA. IRRV (Hons)
Director of Finance
29 September 2014

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About the Fund

The Fund is constituted under legislation governing the Local Government Superannuation Scheme, the primary Act of governance is the Superannuation Act 1972. Detailed regulations for the Scheme are contained in the Local Government Pension Scheme (Scotland) Regulations 1998 and the Local Government Pension Scheme (Management & Investment of Funds) Regulations 2010.

The Fund is built up by contributions from both employees and employing bodies, together with interest and dividends from investments, out of which defined pensions and other benefits are paid.

The Fund's assets are managed by appointed Investment Fund Managers. Once the cost of current benefits is met all surplus cash income is invested to meet future liabilities to employees within the Fund and deferred pension benefits.

Employees' contributions to the Fund are fixed by statute and contributions payable by employing bodies are fixed every three years following a report by an independent actuary who determines the level of contribution necessary to ensure that the Fund will be able to meet future benefits. A common contribution rate of 17.3% of payroll contributions was set by the Actuary for the period 1 April 2012 to 31 March 2015 in the Triennial Actuarial Valuation report 2011.

A Funding Strategy Statement, which summaries the Fund's approach to funding liabilities, has been prepared and describes the strategy of the Highland Council acting in its capacity of Administering Authority for the funding of the Highland Council Pension Fund.

<http://www.highlandpensionfund.org/themes/highland/scheme%20documents/Funding%20Strategy%20Statement.pdf>

A Statement of Investment Principles (SIP) details the policy governing the Fund's investments. A summary of the SIP is set out on page 14. The Fund's Governance Policy Statement is set out later within this document (page 57).

The Highland Council has delegated authority to a Pensions Committee to take decisions on behalf of the Pension Fund. The Investment Sub Committee is responsible for overseeing the management of the investments of the Fund and scrutinises the performance of the Fund's six investment managers. Both Committees meet quarterly, and on an ad hoc basis as required. The Investment Sub Committee also makes decisions in relation to the appointment/termination of managers and any other issues relating to the management of investments.

The Highland Council Pension Fund qualifies as an HMRC 'exempt approved scheme'.

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Members & Advisors

Pensions Committee Membership as at 31 March 2014

Cllr Dave Fallows (Chair)
Cllr David Alston
Cllr Kenneth MacLeod
Cllr Helen Carmichael
Cllr Norrie Donald
Cllr John Ford
Cllr Richard Laird
Cllr Colin Macaulay
Cllr Alister MacKinnon
Cllr Thomas MacLennan
Cllr Carolyn Wilson

Non-Voting members

Cllr Angus Campbell (Comhairle nan Eilean Siar)
Ms Elaine Ward (representative for the other Employers)
Mr Ewen Macniven (scheme member representative)
Ms Liz MacKay (scheme member representative)

Investment Sub Committee Membership as at 31 March 2014

Cllr Colin Macaulay (Chair)
Cllr Helen Carmichael
Cllr John Ford
Cllr Richard Laird
Cllr Alister MacKinnon
Cllr Ken MacLeod
Cllr Carolyn Wilson

Non-Voting members

Cllr A Campbell (Comhairle nan Eilean Siar)
Ms E Ward (representative for the other Employers)

Fund Custodian

The Northern Trust Company

Fund Actuary

Hymans Robertson

Fund Bankers

Clydesdale Bank plc

Investment Advisers

AON Hewitt

Fund Investment Managers

Baillie Gifford & Co
Fidelity International
Legal & General Investment Management
Partners Group
Pyrford International
Schroder Property Investment Management Limited

AVC Provider

Prudential

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Admitted & Scheduled Bodies

Administering Authority

Highland Council (also Scheduled Body)

Scheduled Bodies

Comhairle Nan Eilean Siar
Highland and Western Isles Valuation
Joint Board
Scottish Fire & Rescue
Highlands of Scotland Tourist Board
Western Isles Tourist Board
HITRANS

Inverness College
Lews Castle College
Scottish Police Authority
Scottish Police Service Authority
The Highland Council
The North Highland College

Admitted Bodies

Bord Na Gaidhlig
Inverness Leisure
An Comunn Gaidhealach
Cromarty Firth Port Authority
Eden Court Theatre
Fujitsu Ltd
Forth & Oban Limited
Hebridean Housing Partnership
Highland Blindcraft
Highland & Islands Enterprise (HIE)
Highlands and Islands (Scotland)
Structural Funds Partnership – last
active member 30/06/12
Highland Opportunity Ltd

Highlife Highland
Inverness Harbour Trust
Morrison FM
NHS Highland
Richard Irvin & Sons
RS Occupational Health
Skills Development Scotland
Stornoway Port Authority
Torvean Golf Club- last active member
18/09/13
University of the Highlands & Islands
Vacman Limited
Sight Action

How to Contact Us

Website: www.highlandpensionfund.org

Enquiries regarding Pension Fund Investments:

Corporate Budgeting, Taxation and Treasury
The Highland Council
Council Buildings
Glenurquhart Road
Inverness
IV3 5NX

Tel: 01463 702432

E-mail: treasury.team@highland.gov.uk

Enquiries regarding Pensions Contributions & Benefits:

Pensions Section
The Highland Council
Council Buildings
Glenurquhart Road
Inverness
IV3 5NX

Tel: 01463 702441

E-mail: pensions.section@highland.gov.uk

Website: www.highlandpensionfund.org

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Administration Strategy and Performance

On 1 July 2012 the Fund implemented an Administration Strategy which can be found on the Fund's website.

<http://www.highlandpensionfund.org/themes/highland/scheme%20documents/Administration%20Policy.pdf>

The strategy sets out the roles and responsibilities of both the Administering Authority and scheme employers, and includes a number of key processes and tasks to be benchmarked against expected results. Service level standards for the administering authority performance are based on industry standard Performance Indicators and are detailed in the following tables.

Administering Authority Performance

Task	Target	Total 01/04/2013- 31/03/2014	Completed within target (%)	Previous year (%)
New Entrants	Issue Statutory Notice within 14 days of receipt of a new start notice	1,747	87%	88%
Early Leavers	Issue entitlement notice within 2 months of leaving employment	999	89%	86%
Retirements including deferred benefits coming into payment	To be paid by date of entitlement	513	82%	85%
Deaths in Service	Contact next of kin within 5 days of notification being received	17	100%	100%
Transfers in from outwith fund	Issue statutory notice within 14 days of receipt of payment	81	100%	100%
Transfers of pension rights outwith fund	Make payment within 14 days of receipt of election	61	100%	100%
Estimate of benefits	Issue within 10 days of receipt of request	652	100%	100%

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Scheme Employer Performance - Target performance 90%

Standard	Number from 01/04/13 to 31/03/14	% achieved	Previous year %
New Start Notification – within 30 days of joining (or 10 days from first deduction if later)	1747	91%	91%
Retirement information – to allow benefits to be paid on time	276	90%	89%
Early leaver notification-within 30 days of leaving (or 10 days after last deduction if later)	999	93%	85%
Death in Service notification – within 7 days of death	17	100%	100%
Year End Query responses – within 14 days	19 employers were issued with queries	100%	100%

Investment Performance Report

Economic and market background

Markets brushed aside concerns over a reduction in quantitative easing, and despite various economic and political difficulties, global equity returns were strong over the 12 months to 31 March 2014. Central Banks quantitative easing programmes and Eurozone issues were the dominant factors. The Federal Reserve continued its open-ended quantitative easing programme to support the US economy. However, investors became anxious in May as Federal Reserve Chairman Bernanke signalled a reduction in quantitative easing earlier than expected. The Federal Reserve actually initiated its withdrawal of quantitative easing in December. As the Federal Reserve continued to wind down its asset purchases, Bernanke's successor Janet Yellen emphasised her commitment to maintain accommodative monetary policy in order to support continuing economic growth. Both Janet Yellen and Bank of England Governor Mark Carney changed course on their respective forward guidance policies, playing down dependence on the unemployment rate, which had been falling faster than anticipated in both the US and UK.

Equities –a reduction in quantitative easing did not impact markets, and despite various economic and political difficulties, global equity returns performed well, and the MSCI All Country World Index returned 17.4% over the 12 months to 31 March 2014 in local currency terms. However, sterling strength over the year eroded the majority of these returns, and the sterling return on the index was 6.7%. Despite some encouraging economic data and having the fastest developed market GDP growth, UK equity market returns over the past 12 months were overshadowed by other developed markets. The UK equity market returned 8.8%.

Bonds - UK fixed interest gilts provided a negative return over the year as better economic data and rising US yields put upward pressure on UK bond yields. Fixed interest gilt yields increased substantially across all maturities over the year, with the

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majority of rises occurring in the first six months. A similar trend was also seen in index-linked gilt yields.

Property - The UK commercial property market had an exceptionally strong year as it was up by 14.0% over the 12 months to 31 March 2014, giving the highest 12 month return for the asset class since 2010. Improving economic sentiment in the UK and increased investor appetite, in a low interest environment, led to an increase in capital values and rental outlook which drove the strong performance in the sector over the year.

Private Equity – Fundraising in private equity continued at reasonable levels over the year. Private equity fundraising in Europe was up significantly compared to last year as conditions improved and sovereign debt worries subsided. In Q3 2013 Europe had the highest level of activity since 2008.

Pension Fund Investment Performance

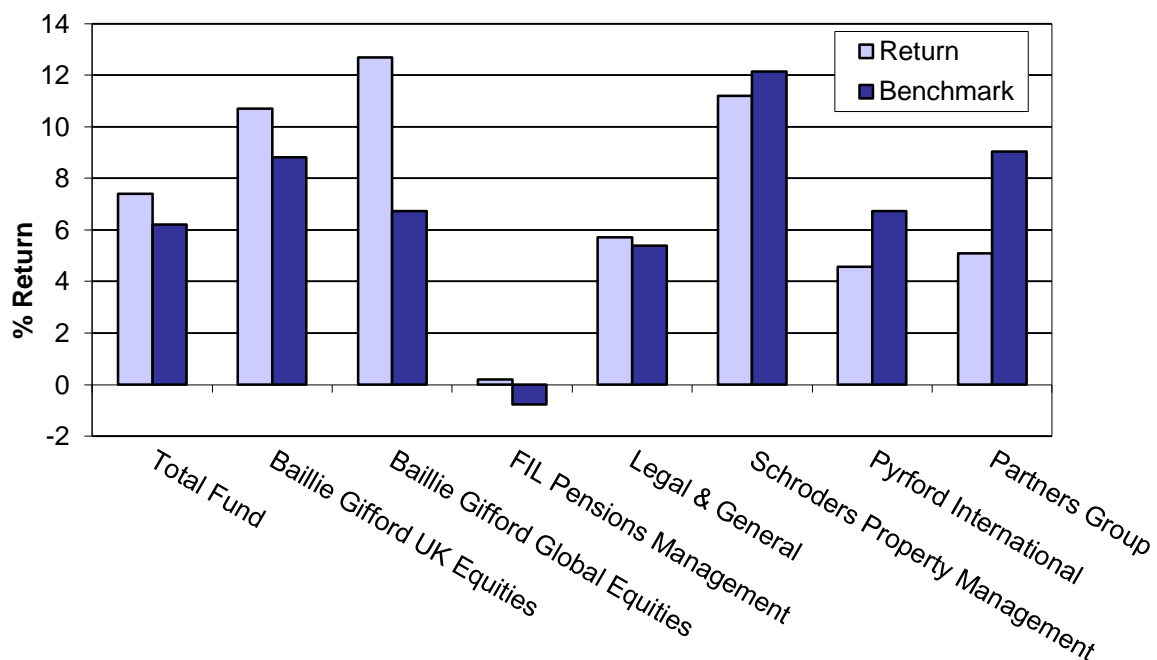
In the year to 31 March 2014, the Highland Council Pension Fund achieved a return on investments of +7.4% against its customised benchmark of +6.2%. The overall level of performance was positive, as was the out-performance of the benchmark, in what continues to be challenging economic times and market conditions.

The market value of the Fund's net investment assets as at 31 March 2014 was £1,268m up from £1,173m at 31 March 2013.

Overall the main positive contributors to performance have been UK and Global equities, as a result of overall equity market performance (benchmark return), and in addition strong manager stock selection and market out-performance (excess return).

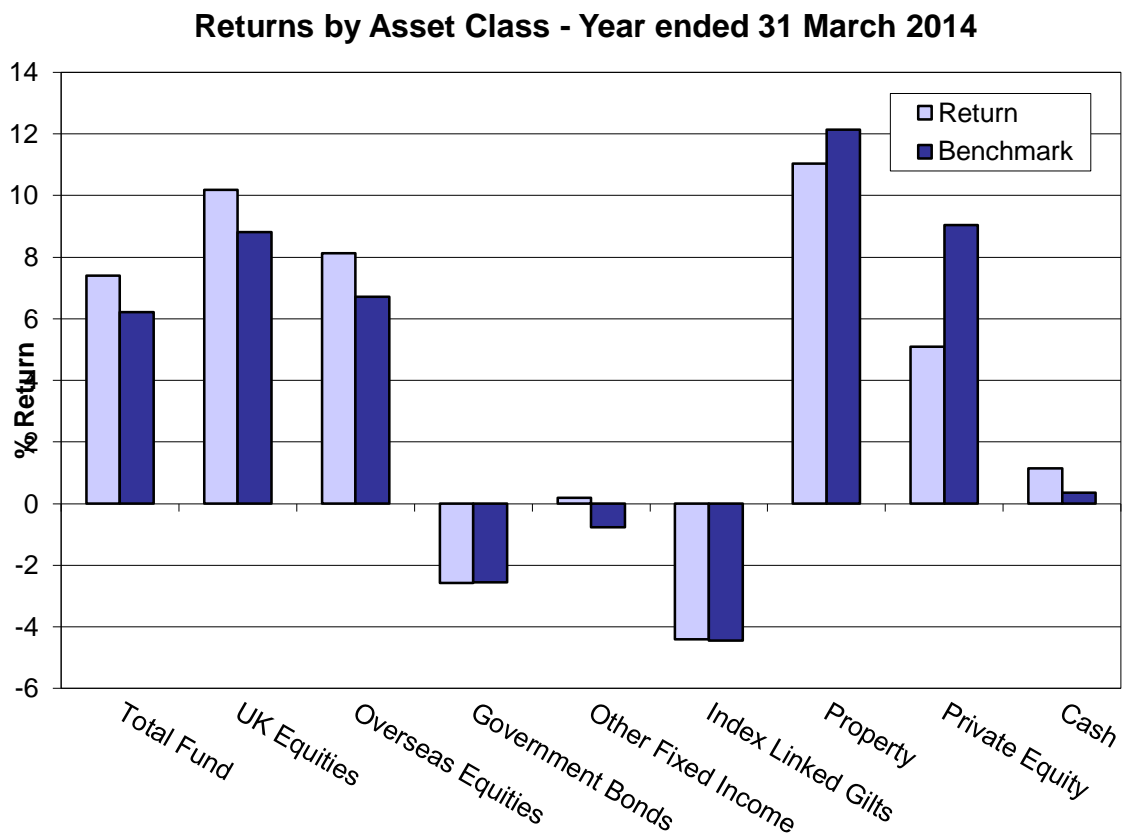
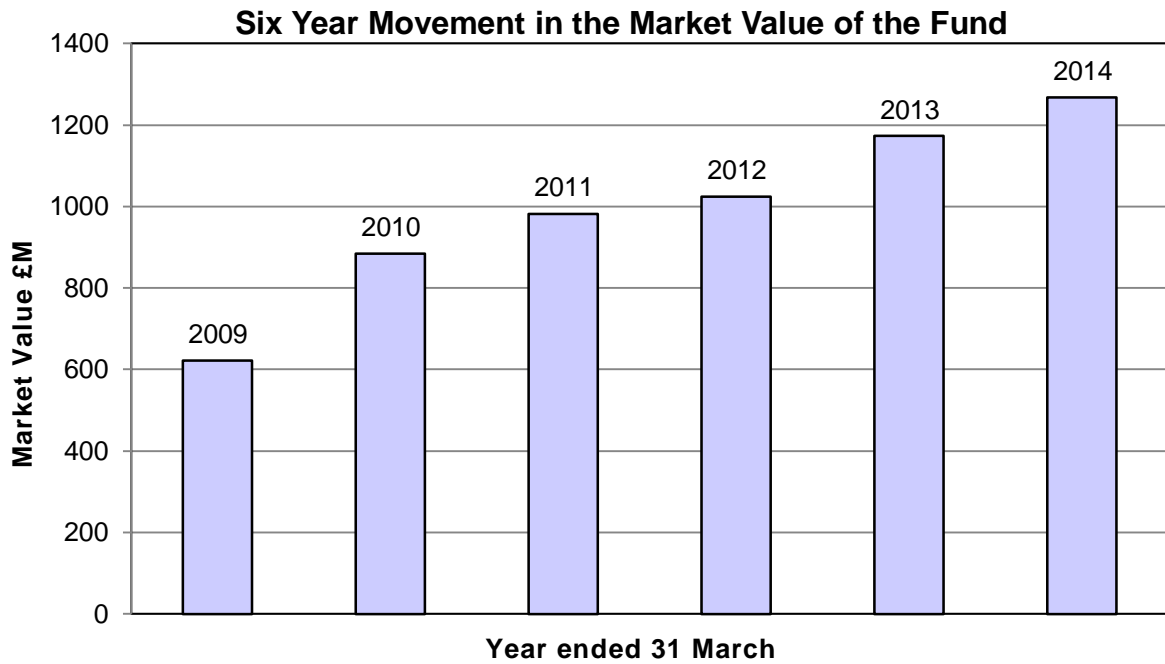
Details of the Fund's investments, analysed by investment category, and by Fund manager, are shown in the financial statements (refer to Note 15).

Annual Return by Fund Manager year ended 31 March 2014



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Statement of Investment Principles – Summary

Background

The Highland Council is the administering authority of the Highland Council Pension Fund. Elected members recognise that they have fiduciary duties and responsibilities towards beneficiaries, employers and local tax payers that are similar to those holding the office of Trustee in the private sector.

Advisors

Independent Investment Managers, Investment Advisers, Actuaries and Performance Measurement Advisers are employed to give on-going expert advice and assistance in the managing of the Fund.

Funding Policy

The Fund is a defined benefit pension scheme which provides members with pensions and lump sums related to their final salaries. The fundamental objective is to meet these benefits on retirement, or the dependant's benefits on death before or after retirement.

The funding policy is directed to ensuring that in normal market conditions, all accrued benefits are fully covered by the actuarial value of the Fund's assets and that the appropriate level of contributions is agreed by the administering authority to meet the cost of future benefits accruing.

A Funding Strategy Statement for the Pension Fund has been prepared in accordance with Regulation 75A (1) of the Local Government Pension Scheme (Scotland) Regulations 1998 as amended by the Local Government Pension Scheme (Scotland) Amendment Regulations 2005. The Statement describes the strategy of the Highland Council in acting in its capacity as Administering Authority for the funding of the Highland Council Pension Fund. The Statement can be viewed at:

<http://www.highlandpensionfund.org/themes/highland/scheme%20documents/Funding%20Strategy%20Statement.pdf>

Investment Policy

The Fund's Investment Policy will be directed to ensuring that in normal market conditions, all accrued benefits are fully covered by the actuarial value of the Fund's assets and that an appropriate level of contributions is agreed by the administering authority to meet the cost of future employees' benefits accruing.

The long term investment objective of the Fund is to achieve a real rate of return of 3-4% per annum on average. With 75% of the Fund's investments in active management and 25% in index tracking (passive), it is hoped that an efficient balance will be met between risk and return in light of liability profile and the funding level.

Asset Mix of Investments

The overall investment portfolio for the Fund is weighted to the equity market, both UK and Overseas and some Private Equity. However, the portfolio also has invested in Index-Linked Gilts, Property, UK Bonds, Overseas Bonds and Cash.

This diverse range of investments over 6 different Managers (5 active and 1 passive) is employed to minimise the effect of risk and enhance overall performance of the

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Fund for its Members.

Each Manager, with the exception of the index tracking Manager, has full discretion in asset mix and stock selection, subject to the investment principles.

Monitoring

The Investment Sub Committee meets quarterly. Each of its Investment Managers attends these meetings on a rotational basis to monitor performance relative to performance targets and officers meet and discuss these with managers throughout the year.

Adoption of the strategic benchmark and the performance monitoring constrains the Investment Managers from deviating significantly from the intended approach. However, it also permits flexibility to manage the Fund in such a way as to enhance returns.

Risk

The Fund pursues a policy of lowering risk through diversification of both investments and investment managers. A management agreement is in place for each Investment Manager, which sets out the relevant benchmark performance target, asset allocation ranges, and any restrictions, as determined by the Fund.

Realisation of Investments

The majority of the investments held by the Fund are quoted on major stock markets and may be realised quickly if required. Property and private equity investment are relatively illiquid and together make up approximately 11% of the total Fund.

Underwriting

Managers are permitted to underwrite and sub underwrite stock issues on the basis that the subject stock is already held in the portfolio or that the Manager wishes to acquire a long term holding.

Social, Environmental and Ethical Considerations

The Fund recognises that social, environmental and ethical considerations are among the factors which Managers will take into account, where relevant, when selecting investments for purchase, retention or sale.

In general terms, this means that there is a group of socially responsible investment concerns which investors need to be aware of and which should be taken into consideration when the decision to invest is being made. This does not mean that the decision whether or not to invest depends entirely on the assessment of these factors but that they should be weighed in the balance along with all over relevant factors when decisions to buy, hold or sell investments are being made.

The Council has instructed the Investment Managers to take into account the key principles of socially responsible investment primarily through a policy of engagement with Companies that demonstrate appropriate observance of these principles.

Corporate Governance

The Fund ensures that the votes attached to its holdings in all UK quoted companies are exercised whenever practical. The Fund's votes are exercised by its Investment Managers in accordance with their own policies and practices and taking account of

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the Combined Code on Corporate Governance.

Custody

The Fund has a Global Custodian responsible for the safekeeping of all assets and execution of transactions.

The Global Custodian also provides all the reporting data to the Council for performance monitoring and independent reconciliation purposes for each Investment Manager.

Stock Lending

The Fund has no stock released to a third party under a securities lending agreement at this time.

Compliance

Investment Managers and the Custodian will provide an annual statement to the Council confirming that they have given effect to the investment principles contained in this document so far as is reasonably practicable.

Adhering to guidance given by Scottish Ministers, The Fund is compliant with the six revised principles on investment decision making for occupational pension schemes, as set out in guidance published by the Chartered Institute of Public Finance and Accountancy in December 2009 called 'Investment Decision Making and Disclosure in the Local Government Pension Scheme: A Guide to the Application of the Myners Principles'.

A detailed version of this Statement of Investment Principles (SIP) expanding on the paragraphs above can be obtained from the address below:

Corporate Budgeting, Taxation and Treasury, Finance Service, Highland Council, Glenurquhart Road, Inverness, IV3 5NX or Treasury.Team@Highland.gov.uk

Strategic asset allocation

The Fund's strategic asset allocation targets are as follows:

Portfolio	Target %	Comment
UK Equities	30.5*	18% Baillie Gifford – active 12.5% L&G – passive
Global Equities	32.0	15% Baillie Gifford – active 12% Pyrford – active 5% L&G – passive
Private Equity	5.0*	Partners Group - active
Property	10.0	Schroder – active fund of funds
Bonds	22.5	15% Fidelity– active 7.5% L&G – passive manager

* When private equity is fully funded.

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Actuarial Position

Employers' contributions are assessed every three years by an independent actuary and expressed as a percentage of pensionable pay. The Common Rate of Contribution payable by each authority under Regulation 32 of the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008 is 17.3% of pensionable pay on the basis of the last actuarial valuation as at 31 March 2011, applying to financial years 2012/13 – 2014/15.

The "Projected Unit Method" was used for employers open to new staff and the "Attained Age Method" was used for employers that are closed to new staff.

Individual employers' rates will vary from the common contribution rate depending on the demographic and actuarial factors particular to each employer. Full details of the contribution rates payable can be found in the 2011 actuarial valuation report and the funding strategy statement on the Pension Fund website.

<http://www.highlandpensionfund.org/about-us/forms-and-publications.aspx>

Demographic assumptions are used to estimate future consequences for the Fund. They take account of expected future trends (for instance future improvements in life expectancy) as well as the past experience in the Fund.

As at the 2011 actuarial valuation, the fund was assessed as 97% funded (2008 valuation: 98%). This corresponded to a deficit of £33m at that time (2008 valuation: deficit of £16.3m). The 2011 funding level had decreased marginally from 98% in March 2008 largely due to investment returns achieved by the Fund being less than were assessed at the previous valuation.

Financial assumptions

Financial assumptions are used to estimate the amount of benefits and contributions payable and to place a current value on these benefits and contributions. The key financial assumptions are:

Financial Assumptions	March 2011		March 2008	
	Nominal p.a.	Real (RPI) p.a.	Nominal p.a.	Real p.a.
Investment Return				
Equities/absolute return funds	6.9%	3.4%	7.4%	3.7%
Gilts	4.3%	0.8%	4.6%	0.9%
Bonds & Property	5.5%	2.0%	6.1%	2.4%
Discount Rate	6.4%	2.9%	6.9%	3.1%
Pay Increase	5.0%	1.5%	5.2%	1.5%
Price Inflation	3.5%	0.0%	3.7%	-
Pension Increases	3.0%	(0.5%)	3.7%	-

The actuarial projection of the Market Value of the Fund's assets as at 31 March 2011 was £986m. The aim is to achieve 100% solvency over a period of 20 years and to provide stability in employer contribution rates by spreading any increases in rates.

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Mortality assumptions

The key mortality assumptions are that all members will follow the mortality experience of a table which is based on the mortality assumptions underlying the 110% S1PA tables allowing for CMI projections, with a long term rate of 1%.

Future life expectancy based on the Actuary's fund-specific mortality review was:

Mortality assumption at age 65	Male	Female
Current pensioners	21.3	23.5
Future pensioners (assumed current age 45)	22.6	25.1

Commutation assumption

Half the members will commute their commutable pension for cash at retirement. Active members will retire one year later than they are first able to do so without reduction.

The Actuary's Statement for 2013/14 is included in pages 64 and 65 of this report.

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Statement of Responsibilities for the Statement of Accounts

The Authority's Responsibilities

The Highland Council, as the administering authority for the Highland Council Pension Fund, is required to:

- make arrangements for the proper administration of its financial affairs and to ensure that one of its officers has the responsibility for the administration of those affairs. In this authority, that officer in the year to 31 March 2014 was the Director of Finance (Section 95 Officer).
- manage its affairs, to secure economic, efficient and effective use of resources and safeguard its assets.

The Director of Finance's Responsibilities

The Director of Finance is responsible for the preparation of the Pension Fund's statement of accounts in accordance with proper practices as set out in the CIPFA/LASAAC *Code of Practice on Local Authority Accounting in the United Kingdom 2013/14* (the Code).

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

- selected suitable accounting policies and applied them consistently,
- made judgements and estimates that were reasonable and prudent,
- complied with the local authority Code

The Director of Finance has also:

- kept proper accounting records which are up to date,
- taken reasonable steps for the prevention and detection of fraud and other irregularities.

I, the Director of Finance of Highland Council as Chief Finance Officer state that the accounts for the year ended 31 March 2014 give a true and fair view of the financial transactions of the Fund during the year ended 31 March 2014, and of the amount and disposition at that date of its assets and liabilities.

Derek Yule B.Com. CPFA. IRRV (Hons)
Director of Finance
29 September 2014

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Statement on the System of Internal Financial Control

Responsibilities for Internal Control

This statement is given in respect of the statement of accounts for the Highland Council Pension Fund. I acknowledge my responsibility for ensuring that an effective system of internal financial control is maintained and operated in connection with the resources concerned.

It is the responsibility of senior management to establish an appropriate and sound system of internal control, and to monitor the continuing effectiveness of that system.

The Head of Internal Audit and Risk Management, Highland Council, provides an annual overall assessment of the robustness of the system of internal control.

Internal Control

Internal control is defined as "*the whole system of checks and controls, financial or otherwise, established by management in order to provide reasonable assurance*" regarding the achievement of one or more of the following objectives:

- The reliability and integrity of information.
- Compliance with policies, plans, procedures, laws, regulations and contracts.
- The safeguarding of assets.
- The economical and efficient use of resources.
- The accomplishment of established objectives and goals for operations or plans.

Any system of control can only provide reasonable, and not absolute assurance that control weaknesses or irregularities do not exist, or that there is no risk of material errors, losses, fraud or breaches of laws and regulations. Accordingly the Fund should seek continual improvement in the effectiveness of its systems of internal control.

Internal Audit

Public Sector Internal Audit Standards define internal auditing as "*an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes*".

The Internal Audit Section operates in accordance with the Standards and as required, a risk based tactical audit plan is produced each year, and submitted for approval to the Pension Committee.

The work undertaken by Internal Audit is documented in an audit report and issued to management. Any areas of concern together with the management agreed actions and target dates for implementation are summarised in an Action Plan within the report. It is the responsibility of management to ensure that implementation of these actions takes place as agreed. The Internal Audit Section will undertake periodic follow-up reviews to ensure that the management agreed actions have been satisfactorily implemented and the results of this will be reported to the Pensions Committee.

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Internal Audit work

The work undertaken by the Internal Audit Section during the year to 31 March 2014 consists of that undertaken directly for the Fund and indirectly where the Highland Council's financial systems are used. The 2013/14 audit plan was presented to the Pensions Committee on 23/05/13 and this consisted of the following two audits:

- A review of the systems of internal control for the financial year 2013/14 consisting of a high level review of the adequacy and effectiveness of the Fund's system of internal control and targeted testing of key controls. These key controls, summarised below are examined to confirm that the main financial systems are operating as intended.
 - Financial procedures and guidance issued to staff;
 - Segregation of duties;
 - User access levels and appropriateness;
 - System backups.

No control issues have been identified from this work and the audit findings will be addressed in a separate report.

- An audit of the Pension Fund contributions. Details of this audit were provided to the Pensions Committee on 14/11/13 including the audit opinion of "Full Assurance". The report contained one low grade management agreed action which has been implemented.

Assurance is also provided by individual audits of the Council's main financial systems. For this year this consisted of budgetary control and the creditors system whereby the process for the ordering and payment of goods and services was examined. Again, no major control issues have been identified which will affect the audit opinion.

Assurances from Fund Managers and Global Custodian

The 6 Fund Managers and the Global Custodian each provide an annual assurance report (AAF 01/06/ISAE 3402) which sets out the control procedures in place during the year, and includes an assessment, by an independent accountant, of the effectiveness of the systems of internal controls in operation throughout the period examined.

These reports were obtained and reviewed, and it was confirmed that reasonable assurances were provided by the independent accountants.

Governance arrangements

Local Government Pension Schemes are required to measure compliance of their governance arrangements against compliance standards and this is included within the Pension Fund's Governance Compliance statement on pages 59 to 61.

The Pension Fund also has a Governance Policy Statement which is one of a number of key documents it must hold and this was updated in May 2013. The governance arrangements have been enhanced further by updating and strengthening the training policy for the Pension Fund. This policy has adopted the CIPFA Code of Practice on Public Sector Pensions Finance Knowledge and Skills,

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and CIPFA's supporting Framework and guidance documentation, and applies to both officers responsible for supporting the Fund, and Members of the Pensions Committee and Investment Sub-Committee charged with governance and decision making.

The Highland Council, as administering authority of the Pension Fund, has approved and adopted a Local Code of Corporate Governance, which is consistent with the principles and reflects the requirements of the CIPFA/SOLACE Framework Note for Scottish Authorities – Delivering Good Governance in Local Government (2007). This framework has been updated with regard to the CIPFA Statement on the Role of the Chief Financial Officer (CFO) in Public Service Organisations and a supporting CIPFA/SOLACE application note has been produced. The arrangements of the Pension Fund comply with the CIPFA Statement.

The Role of the CFO and future governance position will be further strengthened by a revision of the Council's Financial Regulations to clarify that the Director of Finance, as well as the Head of Internal Audit and Risk Management, have direct access to the Pensions Committee, and Chair of Pensions Committee, to raise any concerns they may have.

Risk Management

CIPFA guidance on "Managing risk in the Local Government Pension Scheme" was issued in November 2012 and this sets out the role of the Pensions Committee as follows:

- Determining the risk policy and reconciling this with the wider organisational risk policy;
- Setting the risk management strategy in line with the risk policy;
- Overseeing the risk management process.

Within the Governance Policy Statement reference is made to the Fund's Risk Management arrangements whereby identified risks and their countermeasures are contained within the Funding Strategy Statement (FSS). This also states that the Fund has adopted the Council's risk management arrangements.

A specific risk register for the Pension Fund has recently been drafted using the format set out in the CIPFA guidance. This has been reviewed by Management and it is intended that this will be finalised shortly. Within the register, the risks have been "ragged" (marked as Red, Amber or Green depending on impact and likelihood of risk, taking into account any mitigating controls) and it is intended that those shown as Amber (there are no Reds) will be reported to the Pensions Committee in August.

Audit Opinion

On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Pension Fund's internal control systems for the year to 31 March 2014.

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Intercompany Accounts

Work continues to improve the processes associated with the Pension Fund bank account to confirm the accuracy of balances in the Highland Council and Pension Fund accounts. During the year-end audit, External Audit required further analysis of the intercompany account balance. This was provided to the external auditor along with an assurance in the new financial year the Finance Service would regularly analyse the balance on the intercompany account so as to provide appropriate assurance that the balance on that account represented the net position of valid transfers due between the Pension Fund. Additional resources will be allocated during the financial year to help with the analysis. The introduction of a new financial information system on 1st April 2015 will remove the need for the intercompany account.

Derek Yule B.Com. CPFA. IRRV (Hons)
Director of Finance
29 September 2014

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Pension Fund Account

2012/13 £000		Notes	2013/14 £000
	Dealings with members, employers and others directly involved in the scheme		
48,689	Contributions receivable	6 & 7	50,578
1,843	Transfers in from other pension funds	8	2,184
(40,776)	Benefits payable	9	(43,101)
(2,131)	Payments to and on account of leavers	10	(2,784)
(842)	Administrative expenses	11	(1,081)
<hr/>			<hr/>
6,783	Net additions from dealings with members		5,796
	Returns on Investments		
22,665	Investment income	12	25,097
126,223	Profit and losses on disposal of investments and changes in values of investments	15.1	62,787
(205)	Taxes on income	13	(205)
(2,698)	Investment management expenses	14	(3,188)
<hr/>			<hr/>
145,985	Net Return on Investments		84,491
<hr/>			<hr/>
152,768	Net increase in the net assets available for benefits during the year		90,287
<hr/>			<hr/>
1,032,678	Opening net assets as at the start of the year		1,185,446
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1,185,446	Closing net assets as at the end of the year		1,275,733
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Net Assets Statement as at 31 March 2014

As at 31/03/13 £000		Notes	As at 31/03/14 £000
1,155,943	Investment assets	15.1	1,251,750
17,117	Cash deposits	15.1	13,803
2,921	Investment income due	15.1	2,621
1,143	Amounts receivable for sales	15.1	2,112
(3,940)	Investment liabilities	15.1	(1,799)
1,173,184	Total net investment assets	15.1	1,268,487
	<u>Current assets</u>		
7,267	Debtors	22	6,884
7,516	Bank accounts		6,842
14,783	Total current assets		13,726
	<u>Less current liabilities</u>		
(2,521)	Sundry creditors	23	(6,480)
1,185,446	Closing net assets as at the end of the year available to fund benefits at the period end¹		1,275,733

The unaudited statement of accounts was issued on 9 June 2014 and the audited statement of accounts was authorised for issue on 29 September 2014.

Derek Yule B.Com. CPFA. IRRV (Hons)
Director of Finance
29 September 2014

¹ The Fund's financial statements do not take account of liabilities to pay pensions and other benefits after the period end. The actuarial present value of promised retirement benefits is disclosed at Note 18.

HIGHLAND COUNCIL PENSION FUND 2013/14

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Notes to Accounts

1. Description of Fund

The Highland Council is the administering authority of the Highland Council Pension Fund ("the Fund") and is the reporting entity for the Fund.

For further information, reference should be made to the "About the Fund" section on page 7 of this document.

General

The Fund is governed by the Local Government Superannuation Scheme, the primary legislation being the Superannuation Act 1972.

2. Basis of preparation

The Pension Fund Accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 which is based upon International Reporting Standards (IFRS) as amended for the UK public sector.

The accounts summarise the transactions of the Fund and report on the net assets available to pay pension benefits. The accounts do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present value of the promised retirement benefits, valued on an International Accounting Standard (IAS) 19 basis is disclosed at Note 18 of these accounts.

3. Summary of Significant Accounting Policies

Fund account – revenue recognition

a. Contribution income

Normal contributions, both from the members and from the employer, are accounted for on an accruals basis at the percentage rate recommended by the fund actuary in the payroll period to which they relate.

Employers' augmentation contributions and pension strain contributions are accounted for in the period in which the liability arises. Any amount due in year but unpaid will be classed as a current asset (sundry debtor).

b. Transfer to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the Local government Pension Scheme Regulations (see Notes 8 and 10).

Individual transfers in/out are accounted for when received/paid, which is normally when the member liability is accepted or discharged.

Transfers in from members wishing to use the proceeds of their additional voluntary contributions (see below) to purchase scheme benefits are accounted for on a receipts basis and are included in Transfers in (see Note 8).

Bulk (group) transfers are accounted for on an accruals basis in accordance with the terms of the transfer agreement.

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c. Investment income

i) Interest income

Interest income is recognised in the Fund account as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination. Income includes the amortisation of any discount or premium, transactions costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

ii) Dividend income

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

iii) Distributions from pooled funds

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the net assets statement as a current asset (sundry debtor).

iv) Property-related income

The Fund does not invest directly in property. All property investments are on a 'fund of funds' basis.

v) 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.

Fund account – expense items

d. 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 (sundry creditors).

e. Taxation

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

f. Administrative expenses

All administrative expenses are accounted for on an accruals basis. Management, accommodation and other overheads are apportioned to the Fund in accordance with Council policy.

g. Investment management expenses

All investment management expenses are accounted for on an accruals basis.

Fees of the external investment managers and custodian are agreed in the respective mandates 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.

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In advance of preparing the year end a request is made to all Investment Managers for their fee to the end of March 2014 or an estimated fees accrual figure.

The cost of obtaining investment advice from external advisers is included in the investment manager charges and as above a request is sent to all external advisers for their fee to the end of March 2014 or an estimated fees accrual figure.

A proportion of the Council's costs representing management time spent by officers on investment management are also charged to the Fund.

Net Assets Statement

h. Financial assets

Financial assets are included in the net assets statement on a fair value basis as at the reporting date. A financial asset is recognised in the net assets statement on the date the Fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in the fair value of asset are recognised by the Fund.

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

- i) **Market-quoted investments**
The value of an investment for which there is a readily available market price is determined by the bid market price ruling on the final day of the accounting period.
- ii) **Fixed interest securities**
Fixed interest securities are recorded at net market value based on their current yields.
- iii) **Unquoted investments**
The fair value of investments for which market quotations are not readily available is determined as follows:
 - Unquoted holdings in private equity funds have been included at the Fund managers' valuation adjusted for cash movements since the last valuation date. Unquoted Fund investments are valued at fair value as determined by the Directors or General Partner. The valuations provided by the general partners or managers typically reflect the fair value of the Company's capital account balance of each Fund investment, including unrealised gains and losses, as reported in the Financial Statements of the respective Fund. Private equity investments are typically illiquid and resale is restricted.
- iv) **Pooled investment vehicles**
Pooled investment vehicles are valued at closing bid price if both bid and offer prices are published; or if single priced, at the closing single price. In the case of pooled investment vehicles that are accumulation funds, change in market value also includes income which is reinvested in the Fund, net of applicable withholding tax.

i. 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 and purchases and sales

HIGHLAND COUNCIL PENSION FUND 2013/14

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outstanding at the end of the reporting period.

j. Derivatives

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

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

The value of futures contracts is determined using exchange prices at the reporting date. Amounts due from or owed to the broker are the amounts outstanding in respect of the initial margin and variation margin.

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

k. Cash and cash equivalents

Cash comprises cash in hand and demand deposits.

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

l. Financial liabilities

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

m. Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits is assessed on a triennial basis by the scheme actuary in accordance with the requirements of IAS 19 and relevant actuarial standards (Code Para 6.5.2.8).

As permitted under IAS 26 the Fund has opted to disclose the actuarial present value of the promised retirement benefits by way of a note to the Net Assets Statement (Note 18).

n. Additional voluntary contributions

The Highland Council Pension Fund provides an additional voluntary contributions (AVC) scheme for its members, the assets of which are invested separately from those of the Fund. The Fund has appointed Prudential as its AVC provider. AVCs are paid to the AVC provider by employers and are specifically for providing additional benefits for individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and their movements in the year.

AVCs are not included in the accounts in accordance with section 4 (2) (b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 (Statutory Instrument 2010/233). However, Note 19 provides AVC figures for information purposes only.

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4. Critical Judgements in Applying Accounting Policies

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 2014 was £20.3m and prior year comparator (£13.0m).

Pension fund liability

The pension fund liability is calculated every three years by the appointed actuary, with annual updates in the intervening years. The methodology used is in line with accepted guidelines and in accordance with IAS 19. Assumptions underpinning the valuations are agreed with the actuary and are summarised in the Actuarial Position (Note 18). 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 uncertainty

This Statement of Accounts contains estimated figures that are based on assumptions made by the Fund about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because outcomes cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

The items in the Financial Statements at 31 March 2014 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	Estimation of the net liability to pay pensions 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. A firm of consulting actuaries is engaged to provide the Fund with expert advice about the assumptions to be applied.	The effects on the net pension liability of changes in individual assumptions can be measured. For instance, a 0.5% decrease in the discount rate assumption would result in an increase to employer liability of 10% (£124 million). A 1 year increase in member life expectancy would result in an increase in the employer liabilities of 3% (£37.5 million).
Private equity	Private equity investments are valued at fair value in accordance with British Venture Capital Association guidelines. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total private equity investments in the financial statements are £20.3m. There is a risk that this investment may be under or overstated in the accounts.

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6. Events after the Balance Sheet Date

The unaudited statement of accounts was issued on 9 June 2014 and the audited statement of accounts was authorised for issue on 29 September 2014. Events taking place after this date are not reflected in the accounts or notes.

In June 2014, a report was received from the Pension Fund's actuaries regarding the Highlands and Islands Structural Fund Partnership termination value which was calculated at £0.840m. An adjustment has been made to the accounts to reflect this as a debtor in the Net Assets Statement (see Note 7).

7. Contributions Receivable

By category	2012/13	2013/14
	£000	£000
Members' pension contributions	11,996	12,291
Employers' pension contributions	36,693	38,287
Total contributions	48,689	50,578

As Highland Council Pension Fund had a deficit at the last actuarial valuation in 2011, the employers were required to make a contribution towards restoring the funding position in excess of the amount required to fund the on-going accrual of benefits. The table below shows an estimate of the split between normal contributions (required to fund the accrual of benefits for current service) and the amount attributable to deficit funding. This estimate is calculated based on a future service contribution rate excluding deficit contribution of 16.3% (as stated in the actuarial valuation at 31 March 2011). The Strain on the Fund is the cost to the Fund of the early release of Pension Benefits. These costs are payable by the Employer. The contribution rates that have been certified by the Actuary have been set to fund each employer's share of the deficiency in the Fund over the next 20 years.

The outcome of the 2011 valuation resulted in revised contribution rates for years 2012/13 onwards.

Analysis of Contributions by Authority

2012/13		2013/14			Totals
		Highland Council	Scheduled Bodies	Admitted Bodies	
£000		£000	£000	£000)	£000
34,131	Normal contribution	19,189	8,006	8,095	35,290
637	Deficit funding	391	158	972*	1,521
34,768		19,580	8,164	9,067	36,811
1,925	Strain on Fund	600	791	85	1,476
36,693	Employer's contributions	20,180	8,955	9,152	38,287
11,996	Members' pension contributions	6,609	2,793	2,889	12,291
48,689	Total contributions	26,789	11,748	12,041	50,578

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*This amount includes termination value for Highlands and Islands Structural Fund Partnership which was calculated at £0.840m on information received after the balance sheet date – see note 6 above

Number of Contributors and Pensioners

2013/14	Contributors	Pensioners	Deferred Pensioners
Highland Council	6,781	5,659	5,513
Scheduled Bodies	2,647	1,625	1,726
Admitted Bodies	2,422	381	593
Total	11,850	7,665	7,832
2012/13			
Highland Council	6,337	5,442	5,552
Scheduled Bodies	2,624	1,543	1,599
Admitted Bodies	2,493	288	498
Total	11,454	7,273	7,649

8. Transfers in from other Pension Funds

	2012/13 £000	2013/14 £000
Group transfers	-	-
Individual transfers	1,843	2,184
	1,843	2,184

9. Benefits payable

By category	2012/13 £000	2013/14 £000
Pensions	(31,011)	(32,844)
Lump sum retirement benefits	(7,650)	(9,063)
Lump sum death benefits	(2,115)	(1,194)
	(40,776)	(43,101)

By authority	2012/13 £000	2013/14 £000
Highland Council	(29,189)	(30,069)
Scheduled Bodies	(8,717)	(8,361)
Admitted Bodies	(2,870)	(4,671)
	(40,776)	(43,101)

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10. Payments to and on account of leavers

	2012/13	2013/14
	£000	£000
Refunds to members leaving service	(100)	(118)
Payments for members joining state scheme	(80)	(93)
Group transfers	-	(92)
Individual transfers	(1,951)	(2,481)
	(2,131)	(2,784)

At the year-end there are potential liabilities of a further £0.817m in respect of individuals transferring out of the pension fund upon whom the Fund is awaiting final decisions. No provision has been made for these potential liabilities within the statement of accounts.

11. Analysis of administration expenses

	31 March 2013	31 March 2014
	£000	£000
Accommodation charges	(11)	(9)
Support Services – IT	(37)	(17)
Employee Costs	(742)	(978)
Actuarial fees	(16)	(38)
Other administration	(5)	(6)
External Audit fee	(31)	(33)
	(842)	(1,081)

12. Analysis of investment income

	31 March 2013	31 March 2014
	£000	£000
Dividends from equities	13,736	15,034
Income from pooled investments	8,606	9,389
Interest on cash deposits	152	250
Private equity income	145	347
Other investments	26	77
	22,665	25,097

13. Taxes on income

	31 March 2013	31 March 2014
	£000	£000
Withholding tax – fixed interest securities	-	-
Withholding tax - equities	(205)	(205)
Withholding tax – pooled	-	-
	(205)	(205)

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14. Investment management expenses

	31 March 2013	31 March 2014
	£000	£000
Custodial fees & performance measurement	(163)	(139)
Management fees	(2,208)	(2,613)
Investment advisory fees	(54)	(57)
Investment expenses	(254)	(358)
General fees	(19)	(21)
	(2,698)	(3,188)

The management fees disclosed above include all investment management fees directly incurred by the Fund including those charged on pooled fund investments. For certain investments in accordance with industry practice and investment agreements, some management expenses are netted off investment returns at source by managers and are not separately disclosed.

15. Investment assets

15.1. Reconciliation of movements in investments and derivatives

2013/14

Classifications	Market value at 1 April 2013	Purchases at cost & derivative payments	Sales proceeds & derivative receipts	Change in market value	Market value at 31 March 2014
	£000	£000	£000	£000	£000
Investment assets					
Equities	539,803	81,094	(77,796)	39,080	582,181
Unitised insurance policies	339,994	-	-	19,460	359,454
Unit trusts (property)	91,199	25,802	(3,974)	7,018	120,045
Unit trusts (other)	171,508	6,166	(5,505)	(2,487)	169,682
Private equity	12,982	7,818	(1,089)	552	20,263
Currency forwards	457	-	-	(332)	125
Investment liabilities					
Currency Forwards	-	-	-	(305)	(305)
	1,155,943	120,880	(88,364)	62,986	1,251,445
Other investment balances					
Cash deposits	17,117	-	-	(3,314)	13,803
Investment income due	2,921	-	-	(300)	2,621
Amounts receivable for sales	1,143	-	-	969	2,112
Amounts payable for purchases	(3,940)	-	-	2,446	(1,494)
Total net investment assets	1,173,184	120,880	(88,364)	62,787	1,268,487

HIGHLAND COUNCIL PENSION FUND 2013/14

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2012/13

Classifications	Market value at 1 April 2012	Purchases at cost & derivative payments	Sales proceeds & derivative receipts	Change in market value	Market value at 31 March 2013
	£000	£000	£000	£000	£000
Investment assets					
Equities	461,658	198,042	(189,027)	69,130	539,803
Unitised insurance policies	305,512	121,637	(131,873)	44,718	339,994
Unit trusts (property)	88,934	17,502	(13,177)	(2,060)	91,199
Unit trusts (other)	153,359	6,124	-	12,025	171,508
Private equity	-	15,182	(4,138)	1,938	12,982
Equity futures	18	-	-	(18)	-
Currency forwards	6	-	-	451	457
Investment liabilities					
Equity futures offsets	(18)	-	-	18	-
Currency forwards	(21)	-	-	21	-
	1,009,448	358,487	(338,215)	126,223	1,155,943
Other investment balances					
Cash deposits	14,060	-	-	3,057	17,117
Investment income due	2,772	-	-	149	2,921
Amounts receivable for sales	9	-	-	1,134	1,143
Amounts payable for purchases	(2,248)	-	-	(1,692)	(3,940)
Total net investment assets	1,024,041	358,487	(338,215)	128,871	1,173,184

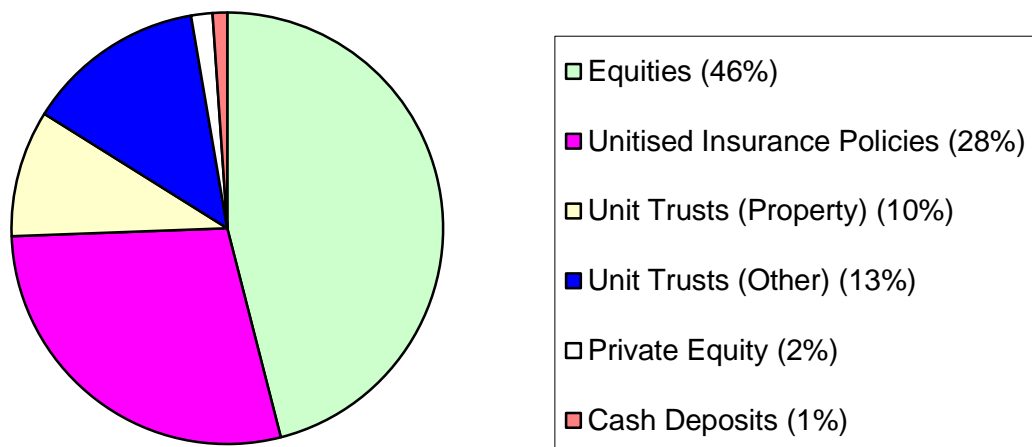
The change in market value of investments during the year comprises of all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

Transaction costs are included in the cost of purchases and sale proceeds. Transaction costs include costs charged directly to the Fund such as commissions, stamp duty and fees. Transaction costs incurred during the year amounted to £0.290m (£0.354m 2012/13). In addition to the transaction costs disclosed above, some indirect investment costs are incurred due to the nature of some of the investment funds. The amount of indirect costs is not separately provided to the Fund.

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15.2. Analysis of investments



2012/13		Portfolio Distribution	2013/14	
UK	Overseas	UK & overseas	UK	Overseas
£000	£000		£000	£000
		Investment assets		
238,749	301,054	Equities	254,812	327,369
282,727	57,267	Unitised insurance policies	302,188	57,266
81,682	9,517	Unit trusts (property)	111,664	8,381
171,508	-	Unit trusts (other)	169,682	-
-	12,982	Private equity	-	20,263
-	457	Currency forwards	-	125
14,742	2,375	Cash deposits	12,904	899
1,713	1,208	Investment income due	1,364	1,257
655	488	Amounts receivable for sales	-	2,112
791,776	385,348		852,614	417,672
		Investment liabilities		
-	-	Currency forwards	-	(305)
(3,455)	(485)	Amounts payable for purchases	-	(1,494)
788,321	384,863	Net total	852,614	415,873
	1,173,184	Total UK & overseas		1,268,487

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2012/13		Portfolio Distribution – (Quoted / Unquoted)	2013/14	
Quoted £000	Unquoted £000		Quoted £000	Unquoted £000
		Investment assets		
539,803	-	Equities	582,181	-
339,994	-	Unitised insurance policies	359,454	-
91,199	-	Unit trusts (property)	120,045	-
171,508	-	Unit trusts (other)	169,682	-
-	12,982	Private equity	-	20,263
-	457	Currency forwards	-	125
-	17,117	Cash deposits	-	13,803
2,921	-	Investment income due	2,621	-
-	1,143	Amounts receivable for sales	-	2,112
1,145,425	31,699		1,233,983	36,303
		Investment liabilities		
-	-	Currency forwards	-	(305)
-	(3,940)	Amounts payable for purchases	-	(1,494)
1,145,425	27,759	Net total	1,233,983	34,504
	1,173,184	Total quoted & unquoted		1,268,487

15.3. Funds under External Management

The Market Value of the assets (at 1 April 2013 and 31 March 2014) which were under the management of fund managers and the proportion managed by each manager are below.

2012/13		Manager Analysis	2013/14	
Market Value £000	% of Fund		Market Value £000	% of Fund
424,968	36.2	Baillie Gifford (UK and global equity)	457,183	36.0
144,899	12.4	Pyrford (global equity)	151,785	12.0
158,582	13.5	Fidelity (bond fund)	159,213	12.6
339,997	29.0	Legal and General (managed fund)	359,457	28.3
208	-	Legal and General (transition)	31	-
91,337	7.8	Schroders (property fund)	120,507	9.5
13,193	1.1	Partners Group (private equity)	20,311	1.6
1,173,184	100.0	Combined Fund	1,268,487	100.0

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15.4. Top 10 Equity Holdings by Market Value

Holding at 31 March 2014	Market Value £000	% of Total Equity Investments	Classification
Prudential	14,223	1.50	Insurance
British American Tobacco	13,229	1.40	Tobacco
Bunzl	9,025	0.95	Support Services
BG Group	8,865	0.94	Oil & Gas
Ashtead Group	8,591	0.91	Industrial good & services
Legal & General	8,236	0.87	Insurance
Roche Holdings	8,185	0.86	Pharmaceuticals
St James's Place	8,082	0.85	Insurance
Rolls Royce Holdings	8,079	0.85	Aerospace
Royal Dutch Shell 'B'	7,334	0.77	Oil & Gas
Total	93,849	9.90	

15.5. Holdings exceeding 5% by total net assets

The Fund holds the following investments that exceed 5% of the net assets available for benefits.

Fund Manager & Category	Market Value at 31 March 2013 £000	% of total net assets %	Market Value at 31 March 2014 £000	% of total net assets %
Fidelity UK Inst Stg Core Plus	79,438	6.7	79,710	6.2
Legal & General (UK Equity Index)	199,703	16.8	217,606	17.1
Fidelity Instl UK Agg Bond	79,145	6.7	79,504	6.2
Total net assets available for benefits	1,185,446		1,275,733	

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15.6. Derivatives - Summary of Contracts at 31 March 2014

Settlement	Currency bought	Local value	Currency sold	Local value	Asset value	Liability value
		000		000	£000	£000
One to six months	GBP	14,815	CHF	(21,575)	125	-
One to six months	GBP	11,638	AUD	(21,658)	-	(281)
One to six months	GBP	5,746	CAD	(10,645)	-	(24)
Up to one month	GBP	12	MYR	(67)	-	-
Up to one month	JPY	8,287	GBP	(48)	-	-
Up to one month	HKD	1,291	GBP	(100)	-	-
Up to one month	GBP	15	AUD	(27)	-	-
Up to one month	EUR	236	GBP	(195)	-	-
Up to one month	HKD	1,334	GBP	(103)	-	-
Up to one month	GBP	20	USD	(32)	-	-
					125	(305)
						(180)
					457	

Investment Managers Pyrford International and Baillie Gifford hold short term currency forwards for the Fund. These investments are used to ensure that cash can remain invested short term in equities. The sale of currency forwards, traded over the counter (OTC), is undertaken in order to hedge foreign currency exposure risk back to the portfolio's base currency of GBP.

15.7. Stock lending

As at 31 March 2014, no stock was released to a third party under a securities lending agreement.

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16. Financial Instruments

16.1. Classification of financial instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the carrying amount of financial asset and liabilities by category and net assets statement heading. No financial assets were reclassified during the accounting period.

	31 March 2014			
	Fair value through profit & loss	Loans & receivables £000	Financial liabilities at amortised cost	Total
	£000	£000	£000	£000
Financial assets				
Equities	582,181	-	-	582,181
Unitised insurance policies	359,454	-	-	359,454
Unit trusts (property)	120,045	-	-	120,045
Unit trusts (other)	169,682	-	-	169,682
Private equity	20,263	-	-	20,263
Derivative contracts – currency forwards	125	-	-	125
Cash deposits	-	13,803	-	13,803
Investment income due	2,621	-	-	2,621
Amounts receivable for sales	2,112	-	-	2,112
Sundry debtors	-	6,884	-	6,884
Bank	-	6,842	-	6,842
	1,256,483	27,529	-	1,284,012
Financial liabilities				
Derivative contracts - equity futures offsets	-	-	-	-
Derivative contracts – currency forwards	(305)	-	-	(305)
Amounts payable for purchases	(1,494)	-	-	(1,494)
Sundry creditors	-	-	(6,480)	(6,480)
Closing net assets	1,254,684	27,529	(6,480)	1,275,733

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	31 March 2013			
	Fair Value through profit & loss	Loans & receivables	Financial liabilities amortised cost	Total
	£000	£000	£000	£000
Financial assets				
Equities	539,803	-	-	539,803
Unitised insurance policies	339,994	-	-	339,994
Unit trusts (property)	91,199	-	-	91,199
Unit trusts (other)	171,508	-	-	171,508
Private equity	12,982	-	-	12,982
Derivative contracts - currency forwards	457	-	-	457
Cash deposits	-	17,117	-	17,117
Investment income due	2,921	-	-	2,921
Amounts receivable for sales	1,143	-	-	1,143
Sundry debtors	-	7,267	-	7,267
Bank	-	7,516	-	7,516
	1,160,007	31,900	-	1,191,907
Financial liabilities				
Derivative contracts - equity futures	-	-	-	-
Derivative contracts - currency forwards	-	-	-	-
Amounts payable for purchases	(3,940)	-	-	(3,940)
Sundry creditors	-	-	(2,521)	(2,521)
Closing net assets	1,156,067	31,900	(2,521)	1,185,446

16.2. Net gains and losses on financial instruments

	31 March 2013	31 March 2014
	£000	£000
Financial assets		
Fair value through profit and loss	126,223	62,986
Loans and receivables	1	668
Financial liabilities measured at amortised cost	-	-
Financial liabilities	-	-
Fair value through profit and loss	-	-
Loans and receivables	-	-
Financial liabilities measured at amortised cost	(1)	(867)
Total	126,223	62,787

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16.3. Fair value of financial instruments and liabilities

The following table summarises the carrying values of the financial assets and financial liabilities by class of instrument compared with their fair value activity.

2012/13			2013/14	
Carrying value	Fair value		Carrying value	Fair value
£000	£000	Financial assets	£000	£000
852,566	1,160,007	Fair value through profit and loss	919,233	1,256,483
31,900	31,900	Loans and receivables	27,529	27,529
884,466	1,191,907	Total financial assets	946,762	1,284,012
		Financial liabilities		
(3,940)	(3,940)	Fair value through profit and loss	(1,803)	(1,799)
(2,521)	(2,521)	Financial liabilities measured at amortised cost	(6,480)	(6,480)
(6,461)	(6,461)	Total financial liabilities	(8,283)	(8,279)
878,005	1,185,446		938,479	1,275,733

The Fund has not entered into any financial guarantees that are required to be accounted for as financial instruments.

16.4. Valuation of financial instruments carried at fair value

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

Level 1

Financial instruments at Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities, quoted fixed securities, quoted index linked securities and unit trusts.

Listed investments are shown at bid prices. The bid value of the instrument is based on the bid market quotation of the relevant stock exchange.

Level 2

Financial instruments at Level 2 are those where quoted market prices are not available; for example where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3

Financial instruments at Level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data. Such instruments would include unquoted equity investments which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

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Values at 31 March 2014

	Quoted market price	Using observable input	With significant unobservable inputs	
	Level 1	Level 2	Level 3	Total
Financial assets	£000	£000	£000	£000
Financial assets at fair value through profit and loss	1,116,175	120,045	20,263	1,256,483
Loans and receivables	27,529	-	-	27,529
Total financial assets	1,143,704	120,045	20,263	1,284,012
Financial liabilities				
Financial liabilities at fair value through profit and loss	(1,799)	-	-	(1,799)
Financial liabilities at amortised cost	(6,480)	-	-	(6,480)
Total financial liabilities	(8,279)	-	-	(8,279)
Net financial assets	1,135,425	120,045	20,263	1,275,733

Values at 31 March 2013

	Level 1	Level 2	Level 3	Total
Financial assets	£000	£000	£000	£000
Financial assets at fair value through profit and loss	1,056,745	90,281	12,981	1,160,007
Loans and receivables	31,900	-	-	31,900
Total financial assets	1,088,645	90,281	12,981	1,191,907
Financial liabilities				
Financial liabilities at fair value through profit and loss	(3,940)	-	-	(3,940)
Financial liabilities at amortised cost	(2,521)	-	-	(2,521)
Total financial liabilities	(6,461)	-	-	(6,461)
Net financial assets	1,082,184	90,281	12,981	1,185,446

17. The 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 benefit payable to members). Therefore the aim of investment risk management is to minimise the risk of an overall reduction in the

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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. The Fund manages these investment risks as part of its overall pension fund risk management programme.

The Pensions Committee is responsible for the Fund's risk management strategy. There is a risk register in place which follows the CIPFA guidance on 'Managing risk in the LGPS'. This will be regularly reviewed going forward and significant risks will be reported to future meetings of the Pensions Committee.

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.

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 Fund and its investment advisors undertake appropriate monitoring of market conditions and benchmark analysis.

The Fund manages these risks by ensuring that specific risk exposure is limited by applying risk-weighted maximum exposures to individual investments.

Equity futures contracts and exchange traded option contracts on individual securities may also be used to manage market risk on equity investments. It is possible for over-the-counter equity derivative contracts to be used in exceptional circumstances to manage specific aspects of market risk.

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 instruments or its issuer or factors affecting all such instruments in the market.

The Fund is exposed to share and derivative price risk. This arises from investments held by the Fund for which the future price is uncertain. All securities investments present a risk of loss of capital. Except for shares sold short, the maximum risk resulting from financial instruments is determined by the fair value of the financial instruments. Possible losses from shares sold short are unlimited.

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

Other price risk – sensitivity analysis

Following analysis of historical data and expected investment return movement during the financial year, in consultation with the Fund's investment advisors, the

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Fund has determined that the following movements in market price risk are reasonably possible for the 2013/14 reporting period:

Asset type	Potential market movement (+/-)%	Potential market movement (+/-)%
	2012/13	2013/14
UK equities	22.5	20.0
Global equities (excluding UK)	26.0	20.5
UK fixed income unit trusts	9.0	9.0
Corporate bonds (medium term)	9.0	9.0
UK fixed gilts (medium term)	11.0	11.0
UK index linked gilts (medium term)	9.0	9.0
Property	16.0	14.5
Private Equity	29.0	26.0
Cash	-	-

The potential price changes disclosed above are broadly consistent with a one-standard deviation movement in the value of the assets. The sensitivities are consistent with the assumptions contained in the investment advisors' most recent review. The Fund's investment advisors suggest that the approach to modelling market price risk should take account of the diversification of assets in the Fund. This approach is different to that outlined in the CIPFA recommended code of practice, where the sum of all potential changes in asset class values are taken to determine the impact on the total value of the Fund. Consequently the total Fund volatility takes into account the expected interactions between the different asset classes shown, based on the underlying volatilities and correlations of the assets, in line with mean variance portfolio theory.

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 would have been as follows (the prior year comparator is shown below):

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Asset type	Value as at 31 March 2014	Percentage change	Value on increase	Value on decrease
	£000	%	£000	£000
Cash and cash equivalents	13,803	0.0	13,803	13,803
Investment portfolio assets:				
UK equities	254,812	20.0	305,774	203,850
Global equities (excluding UK)	327,369	20.5	394,480	260,258
UK fixed income unit trusts	365,051	9.0	397,906	332,196
Corporate bonds (medium term)	79,504	9.0	86,659	72,349
UK fixed gilts (medium term)	50,504	11.0	56,059	44,949
UK index linked gilts (medium term)	34,077	9.0	37,144	31,010
Property	120,045	14.5	137,452	102,638
Private equity	20,263	26.0	25,531	14,995
Net currency forwards	(180)	0.0	(180)	(180)
Investment income due	2,621	0.0	2,621	2,621
Amounts receivable for sales	2,112	0.0	2,112	2,112
Amounts payable for purchases	(1,494)	0.0	(1,494)	(1,494)
Net investment assets	1,268,487		1,457,867	1,079,107

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Asset type	Value as at 31 March 2013	Percentage change	Value on increase	Value on decrease
	£000	%	£000	£000
Cash and cash equivalents	17,117	0.0	17,117	17,117
Investment portfolio assets:				
UK equities	238,749	22.5	292,468	185,030
Global equities (excluding UK)	301,054	26.0	379,328	222,780
UK fixed income unit trusts	349,333	9.0	380,773	317,893
Corporate bonds (medium term)	79,145	9.0	86,268	72,022
UK fixed gilts (medium term)	48,073	11.0	53,361	42,785
UK index linked gilts (medium term)	34,951	9.0	38,097	31,805
Property	91,199	16.0	105,791	76,607
Private equity	12,982	29.0	16,747	9,217
Net currency forwards	457	0.0	457	457
Investment income due	2,921	0.0	2,921	2,921
Amounts receivable for sales	1,143	0.0	1,143	1,143
Amounts payable for purchases	(3,940)	0.0	(3,940)	(3,940)
Net investment assets	1,173,184		1,370,531	975,837

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 advisors in accordance with the Fund's risk management strategy, including monitoring the exposure to interest rates and assessment of actual interest rates against the relevant benchmarks.

The Fund's direct exposure to interest rate movements as at 31 March 2014 and 31 March 2013 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value:

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Asset type	As at 31 March 2013	As at 31 March 2014
	£000	£000
Cash deposits	17,117	13,803
Cash and cash equivalents	7,516	6,842
Legal & General fixed interest gilts	48,073	50,504
Legal & General index linked gilts	34,951	34,077
Fidelity unit trust equity	79,438	79,710
Fidelity unit trust bonds	79,145	79,504
Total	266,240	264,440

Interest rate risk sensitivity analysis

The Fund 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 Fund's investment advisors suggest that a 100 basis point (BPS) movement in interest rates is appropriate for carrying out the interest rate sensitivity analysis.

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 BPS (1%) change in interest rates:

Asset type	Carrying amount as at 31 March 2014 £000	Change in year in the net assets available to pay benefits	
		+100 BPS	-100 BPS
		£000	£000
Cash deposits	13,803	138	(138)
Cash and cash equivalents	6,842	68	(68)
Legal & General fixed interest gilts	50,504	505	(505)
Legal & General index linked gilts	34,077	341	(341)
Fidelity unit trust equity	79,710	797	(797)
Fidelity unit trust bonds	79,504	795	(795)
Total change in assets available	264,440	2,644	(2,644)

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Asset type	Carrying amount as at 31 March 2013	Change in year in the net assets available to pay benefits	
		+100 BPS	-100 BPS
	£000	£000	£000
Cash deposits	17,117	171	(171)
Cash and cash equivalents	7,516	75	(75)
Legal & General fixed interest gilts	48,073	481	(481)
Legal & General index linked gilts	34,951	350	(350)
Fidelity unit trust equity	79,438	794	(794)
Fidelity unit trust bonds	79,145	791	(791)
Total change in assets available	266,240	2,662	(2,662)

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 (£ Sterling).

The Fund's currency rate is routinely monitored by the Council and its investment advisors in accordance with the Fund's risk management strategy, including monitoring the range of exposure to currency fluctuations.

The following table summarises the Fund's currency exposure as at 31 March 2014 and as at the previous period end:

Currency exposure – asset type	Asset value as at 31 March 2013	Asset value as at 31 March 2014
	£000	£000
Overseas quoted securities	301,054	327,369
Overseas unit trusts	57,267	57,266
Overseas property fund	9,517	8,381
Overseas unquoted private equity	12,982	20,263
Total overseas assets	380,820	413,279

Currency risk - sensitivity analysis

A 13% fluctuation in the currency is considered reasonable based on the Fund advisor's analysis of long-term historical movements in the month-end exchange rates over a rolling 36-month period. This analysis assumes that all other variables, in particular interest rates, remain constant.

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A 13% strengthening/weakening of the pound against the various currencies in which the Fund holds investments would increase/decrease the net assets available to pay benefits as follows:

Currency exposure - asset type	Asset value as at 31 March 2014	Change to net assets available to pay benefits	
		+13%	-13%
	£000	£000	£000
Overseas quoted securities	327,369	369,927	284,811
Overseas unit trusts	57,266	64,711	49,821
Overseas property fund	8,381	9,471	7,291
Overseas unquoted private equity	20,263	22,897	17,629
Total change in assets available	413,279	467,006	359,552

Currency exposure - asset type	Asset value as at 31 March 2013	Change to net assets available to pay benefits	
		+13%	-13%
	£000	£000	£000
Overseas quoted securities	301,054	340,191	261,917
Overseas unit trusts	57,267	64,712	49,822
Overseas property fund	9,517	10,754	8,280
Overseas unquoted private equity	12,982	14,670	11,294
Total change in assets available	380,820	430,327	331,313

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 value of investments generally reflects 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.

In essence the Fund's entire investment portfolio is exposed to some form of credit risk, with the exception of the derivatives positions, where the risk equates to the net market value of a positive derivative position. However 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.

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Contractual credit risk is represented by the net payment or receipt that remains outstanding and the cost of replacing the derivative position in the event of a counterparty default. The residual risk is minimal due to the various insurance policies held by the exchanges to cover defaulting counterparties.

None of the investment managers of the Pension Fund have a mandate to specifically manage cash and so cash is generally held by the Custodian and invested in Money Market Funds (Sterling, Euro and US Dollar Funds). The Northern Trust Money Market Funds are triple A rated. In addition the Fund's surplus cash from scheme member's contributions is managed as part of the administering authority's treasury management function. Prior to transfer to the Fund's investment managers, cash surpluses, are deposited with the Pension Fund's bank and the Royal Bank of Scotland thus minimising credit risk

Liquidity Risk

Liquidity risk represents the risk that the Fund will not 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.

Following the triennial valuation at 31 March 2011 the Fund's actuary was asked to assess the projected cash flows of the Fund assuming a variety of possible maturity profiles. This study concluded that, provided the investment income yield remains at current levels, then the time when assets need to be sold to meet benefit payments still looks a long way off. The actuary stated that there is no need to review investment strategy in the short term in any significant way although the cash flow position should continue to be monitored.

Refinancing Risk

The key risk is that the Fund will be bound to replenish a significant proportion of its Pension Fund financial instruments at a time of unfavourable interest rates. The Fund does not have any financial instruments that have a refinancing risk as part of its treasury management and investment strategies.

18. Actuarial Present Value of Promised Retirement Benefits

CIPFA's Code of Practice on Local Authority Accounting 2013/14 requires administering authorities of LGPS funds that prepare pension fund accounts to disclose what IAS 26 refers to as the actuarial present value of promised retirement benefits.

If an actuarial valuation has not been prepared as at the date of the financial statements as is the case, IAS 26 requires the most recent valuation to be used as a base and the date of the valuation disclosed. The valuation should be carried out using assumptions in line with IAS 19 and not the Pension Fund's funding assumptions.

Assumptions underpinning the valuations are agreed with the actuary and are summarised in the Actuarial Position (page 17). This estimate is subject to significant variances based on changes to the underlying assumptions.

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The actuarial present value of promised retirement benefits is as follows:

Net Pension Asset as at	31 March 2014 £m	31 March 2013 £m	31 March 2012 £m
Present Value of Promised Retirement Benefits*	1,779	1,557	1,417

Liabilities have been projected using a roll forward approximation from the previous IAS 26 statement as at 31 March 2013 prepared by Barnett Waddingham, which was based on the latest formal funding valuation as at 31 March 2011.

The Actuary estimates that the liability at 31 March 2014 comprises of £909m in respect of employee members, £225m in respect of deferred pensioners and £645m in respect of pensioners. The approximation involved in the roll forward model means that the split of scheme liabilities between the three classes of member may not be reliable. However, the Actuary is satisfied the aggregate liability is a reasonable estimate of the actuarial present value of benefit promises. The Actuary has not made any allowance for unfunded benefits.

Assumptions

The assumptions used are those adopted for the Administering Authority's IAS 19 report as required by the Code of Practice. These are given below. The Actuary estimates that the impact of the change of assumptions to 31 March 2014 is to increase the actuarial present value by £145m.

Financial Assumptions

The financial assumptions used for the purposes of the actuarial calculations are calculated on an IAS 19 basis and therefore differ from the results of the 2011 triennial funding valuation (see Actuarial Statement page 64) because IAS 19 stipulates a discount rate rather than a rate which reflects market values. The Financial Assumptions are as follows:

Assumptions as at	31 March 2014		31 March 2013		31 March 2012	
	%p.a.	Real	%p.a.	Real	%p.a.	Real
Inflation/Pensions Increase Rate	2.6%	-0.8%	2.6%	-0.8%	2.5%	-0.8%
Salary Increase Rate	4.9%*	1.5%	4.8%	1.4%	4.8%	1.5%
Discount Rate	4.1%	-0.7%	4.5%	1.1%	4.6%	1.3%

*Salary increases are assumed to be 1% p.a. until 31 March 2015 reverting to the long term assumption shown thereafter.

Discount rate

IAS 19 states that the discount rate used to place a value on the liabilities should be "determined by reference to market yields at the end of the reporting period on high

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quality corporate bonds". It further states that "the currency and term of the corporate bonds shall be consistent with the currency and estimated term of the post-employment benefit obligations". The Actuary derived the discount rate from a Corporate bond yield curve based on the constituents of the iBoxx £ Corporates AA index and using the UBS delta curve fitting methodology.

Separate discount rates are then set (and corresponding RPI/CPI inflation assumptions – see below) for individual employers, dependent on their own weighted average duration. Each employer is allocated to a duration category, as defined below:

Weighted average duration	Discount rate category
Less than 17 years	Short
Between 17 and 23 years	Medium
More than 23 years	Long

Retail price inflation assumption

This assumption is typically derived from yields available on fixed interest and index linked government bonds, and should be consistent with the derivation of the discount rate.

For consistency with the assessment described in paragraph above, the Actuary's recommended RPI inflation assumption for each discount rate category defined above has been identified at appropriate durations from the Bank of England implied inflation curve as at 31 March 2014.

Pension increase assumption

The pension increase assumption will be in line with the Consumer Prices Index (CPI). The CPI assumption is calculated as RPI less 0.8% p.a., with RPI being calculated as outlined above.

Salary increase assumption

The Actuary has taken into account the Government's public sector pay restraints (originally announced in June 2010 and extended as per the November 2011 announcement). The Actuary's recommended salary increase assumption is therefore 1% p.a. until 31 March 2015, reverting to RPI plus 1.5% p.a. thereafter, plus an allowance for promotional increases.

Demographic assumptions

The mortality assumptions used are consistent with those used for the formal funding valuation as at 31 March 2011.

The post-retirement mortality assumptions used are the 110% S1PA tables allowing for CMI projections with a long term rate of 1%.

The other demographic assumptions adopted (e.g. commutation, pre-retirement mortality) are the same as those used for the formal funding valuation as at 31 March 2011. Full details of these assumptions are set out in the formal valuation report (see Actuarial Statement page 64).

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19. Additional Voluntary Contributions (AVCs)

The AVC facility is provided by the Prudential Assurance Company Limited and is a money purchase arrangement where members have the choice to invest in a range of low, medium and high risk investment funds. In accordance with regulation 5 [2] [C] of the Pension Scheme (Management and Investment of Funds) Regulations 1998 [S1 1998 No. 1831], these figures do not form part of the accounts of the Pension Fund and are stated for information only.

2012/13	2013/14
£000	£000
9,764 Opening Value	10,134
(6) Adjustments due to new system	0
0 Correction Work	1
1,265 Contributions Invested	1,262
460 Interest, Bonuses & Transfers	427
(1,349) Sale of Investments	(1,784)
10,134 Closing Value	10,040

20. Related Parties

With effect from 01 April 2011 the Pension Fund opened and maintained its own separate bank accounts. As a result, as at 31 March 2014 no internal deposit was held with the Highland Council Loans Fund. The Council's Treasury Management team manage surplus cash balances prior to transmission of funds to the Fund Managers for investment.

The following Senior Officer of the Highland Council held a key position in the financial management of the Pension Fund during the financial year to 31 March 2014.

Name	Resp	Pension Contributions in year to		Accrued Pension Benefits as at		Difference in Accrued Pension benefits compared to March 2014
		31/03/13	31/03/14	31.03.14		
Derek Yule	Director of Finance	£18,981	£19,171	Pension	£47,001	£2,222
				Lump Sum	£114,377	

Pension receipts and payments are transacted using the Highland Council financial systems and the pension fund's banking arrangements. Throughout the year, the fund maintains a cash balance for this purpose which is listed as Bank accounts in the net assets statement.

As at 31 March 2014, the Pension Fund had debtor balances (£3.963m) and creditor balances (£5.312m) representing sums due from/to the Highland Council. These balances cover a range of activity including debtor and creditors arising from central cost recharges and strain on fund recharges to the Pension Fund.

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21. Contingent assets, liabilities and contractual commitments

There are two contingent assets and one contingent liability.

During 2006/07, the Highland Council Pension Fund joined a group litigation to recover tax credits on overseas dividends and foreign income dividends. The estimated claim, gross of fees is £1.7m. As at 31 March 2014, these claims are still active although many of the tax authorities are resisting claims thus delaying the recovery process.

During 2009/10, KPMG were contracted to submit 'EU Fokus Bank' claims for recovery of withholding tax with an estimated value of £1.3m gross of fees. An additional revised contract was agreed in April 2012 with KPMG to continue with the claim although the Fund opted not to pursue a top up claim in Germany as this was not financially viable. Spain issued repayments during 2013/14 of €0.088m (£0.071m).

The Fund has appointed a new private equity investment manager, and in total made a €50m commitment to funding the new mandate. It will take several years for the full €50m commitment to be drawn down on a phased basis. During financial year 2013/14, there were 6 drawdowns, and as a result the Fund has invested €23.7m of their €50m commitment (47%) to the new private equity mandate.

There is a contingent liability of £0.713m for frozen refunds representing 2,887 frozen refund records.

22. Debtors

2012/13	Debtors	2013/14
£000		£000
399	Contributions due - employees	1,011
5,586	Contributions due - employers	3,965*
1,282	Sundry debtors	1,908
7,267	Total debtors	6,884

*contributions due amount includes a debtor for £0.840m for the termination value for the Highlands and Islands Structural Fund Partnership.

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Analysis of debtors

2012/13	Debtors	2013/14
£000		£000
1	Central government bodies	19
6,223	Other local authorities	4,710
435	NHS bodies	406
-	Public corporations and trading funds	2
608	Other entities and individuals	1,747
7,267		6,884

23. Creditors

2012/13	Creditors	2013/14
£000		£000
(2,420)	Sundry creditors	(6,342)
(7)	Transfer values payable (leavers)	-
(94)	Benefits payable	(138)
(2,521)		(6,480)

Analysis of creditors

2012/13	Creditors	2013/14
£000		£000
(29)	Central government bodies	(40)
(1,570)	Other local authorities	(5,567)
(7)	NHS bodies	-
(915)	Other entities and individuals	(873)
(2,521)		(6,480)

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Governance Policy Statement

The Highland Council as the Administering Authority for the Highland Council Pension Fund has published a Governance Policy Statement in accordance with The Local Government Pension Scheme (Administration) (Scotland) Regulations 2008.

The Statement is available on the Highland Council Pension Fund website <http://www.highlandpensionfund.org/about-us/forms-and-publications.aspx> and documents the governance arrangements for the Pension Scheme administered by the Highland Council. A short summary is provided below.

The Administering Authority and the Regulatory Framework

The Highland Council is the Administering Authority for the Highland Council Pension Fund established within the Local Government Pension Scheme. The Fund provides pensions for those employees of the Council, Comhairle Nan Eilean Siar, and of other Scheduled and Admitted Bodies which are eligible to join it.

The Scottish Public Pensions Agency is responsible for regulating the Local Government Pension Scheme in Scotland and the Council administers the Fund in accordance with relevant legislation and regulations.

Committee Structure

The Council has established a Pensions Committee which exercises, on behalf of the Council, all the powers and duties of the Council in relation to its functions as Administering Authority of the Highland Council Pension Fund (the Fund), except where they have been specifically delegated by the Council to another Committee or to an officer(s). The Pension Committee has 11 Highland Council Elected Members who have voting rights, and 4 “non-voting” members; 2 represent other employers and 2 represent scheme members. All committee papers and minutes are publicly available on the Council’s website and meetings are webcast.

In addition the Council has established an Investment Sub-Committee (ISC) comprising of 7 Elected Members from the Highland Council who have voting rights and 2 “non-voting” members representing other employers. The ISC reports to the Pensions Committee on the management and investment of the Pension Fund investment assets.

Both Committees meet at least four times per annum and additional meetings are called as required.

Under the Highland Council’s Scheme of Delegation to Officers and Financial Regulations, the Director of Finance has powers and duties to administer the Local Government Pension Scheme in accordance with the Regulations and agreed policy.

The arrangements for delegation, and how these comply with guidance given by Scottish Ministers are outlined below.

Training

The Fund recognises the importance of training as a key aspect of good governance, and has arrangements in place for the regular training of members and officers which are detailed in the Training Knowledge and Skills Policy statement on page 62.

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Stakeholder Communication

Committee papers and minutes are publicly available on the Council's website.

http://www.highland.gov.uk/meetings/committee/48/pensions_committee

A Pension Fund Report and Accounts and all policy documents are available on the Highland Council Pension Fund website.

<http://www.highlandpensionfund.org/about-us/forms-and-publications.aspx>

Communication with scheme members is undertaken through the annual distribution of a personal benefit statement and opportunity is provided on an annual basis to attend a presentation by an LGPS representative and representative from Prudential, which is the appointed Additional Voluntary Contributions (AVC) Provider. Pensioners receive a monthly pension advice slip. There is a Pension Fund website where all current newsletters and relevant publications are available for scheme members <http://www.highlandpensionfund.org/>

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Governance Compliance Statement

The Regulations that govern the management of LGPS funds in Scotland require that a Governance Compliance Statement is published. The Governance Compliance Statement which sets out the extent to which governance arrangements comply with best practice, is provided below.

Principle	Full Compliance	Comments
Structure		
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	The Highland Council as administering authority has delegated all pension scheme matters to the Pensions Committee. In addition a small Investment Sub Committee has been established to enhance the Council's management and investment of the assets of the Pension Fund in accordance with the respective objectives and strategies of the Fund (Minute of The Highland Council 27 October 2011).
That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.	Yes	The Pensions Committee has two non-voting members representing other employers and two non-voting members representing scheme members. The Investment Sub Committee has two non-voting members representing other employers.
That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	Yes	The minutes of the Investment Sub Committee are presented to the Pensions Committee and there is significant commonality in the membership of the two committees.
That 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 minutes of the Investment Sub Committee are presented to the Pensions Committee and there is significant commonality in the membership of the two committees.
Representation		
That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include: <ul style="list-style-type: none"> • Employing authorities (including non-scheme employers, e.g. admitted bodies); • Scheme members (including deferred and pensioner scheme members) • Where appropriate, independent professional observers, and 	Yes	As stated above there are employer and employee representatives on both Pension Fund Committees. The Fund's investment advisers regularly attend the Pension Investment Sub-Committee and the Fund's actuaries attend the Pension Committee when appropriate. In addition, Fund Managers attend the Investment Sub Committee on

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<ul style="list-style-type: none"> Expert advisors (on an ad-hoc basis). 		a rotational basis.
That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.	Yes	All Pensions Committee members are provided with training, as well as access to papers in advance of Committee meetings and have the opportunity to contribute to the decision making process.
Selection and Role of Lay Members		
That committee or panel members are made fully aware of the status, role and function that they are required to perform on either a main or secondary committee.	Yes	<p>A comprehensive training programme including induction is in place.</p> <p>Training for Pension Committee & Investment Sub Committee members includes presentations from investment managers, Custodian, actuary and investment advisors. Attendance at meetings and training is monitored and reported.</p>
That at the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.	Yes	The declaration of Member's interests is a standard item on the agenda of both Pension Fund Committees.
Voting		
The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees.	Yes	The policy on voting rights is clearly stated in the remits of both Pension Fund Committees.
Training /Facility Time /Expenses		
That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision making process.	Yes	There is a training, knowledge and skills policy in place which was approved by Pensions Committee in November 2013 and incorporates the CIPFA Code of Practice on Public Sector Pensions Knowledge and Skill (2011). The training policy recognises the importance of ensuring that it has the necessary resources to discharge its pensions administration responsibilities and that all staff and members charged with financial administration, governance and decision-making with regard to the pension scheme are fully equipped with the knowledge and skills to discharge the duties and responsibilities allocated to them.

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That where such a policy exists it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	Yes	All members are treated equally under the training policy regardless of whether or not they have voting rights.
That the administering authority considers the adoption of annual training plans for committee members and maintains a log of all such training.	Yes	Members receive training each year and this is monitored and reported.
Meeting Frequency		
That an administering authority's main committee or committees meet at least quarterly.	Yes	The Pensions Committee meets at least four times a year with the option to hold special meetings as necessary.
That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committees sits.	Yes	The Investment Sub-Committee meets at least four times a year with the option to hold special meetings as necessary. The Investment Sub-Committee meetings will be timed so minutes can be presented to the Pensions Committee.
That an administering authority who 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.	N/A	There is a Scheme Members' representative on the Pensions Committee.
Access		
That subject to any rules in the council's constitution, all members of main and secondary committees or panels have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	Yes	All Members of both Pension Fund committees have full access to agendas, reports and minutes. Voting rights are restricted to Highland Council Elected Members.
Scope		
That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Yes	The Pension Committee has an overview of investment, funding and member benefit matters.
Publicity		
That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express interest in wanting to be part of those arrangements.	Yes	The Highland Council publishes governance documents and communicates regularly with employers and scheme members. http://www.highlandpensionfund.org/about-us/forms-and-publications.aspx

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Training, Knowledge and Skills - Policy Statement

On 14 November 2013, the Highland Council Pension Committee formally adopted the CIPFA Knowledge and Skills Framework for public sector pensions finance.

In adopting that framework, the Committee agreed the following training policy statement:

1. The Pensions Committee recognises the importance of ensuring that it has the necessary resources to discharge its pensions administration responsibilities and that all staff and members charged with financial administration, governance and decision-making with regard to the pension scheme are fully equipped with the knowledge and skills to discharge the duties and responsibilities allocated to them.

2. It therefore seeks to utilise individuals who are both capable and experienced and it will provide and/or arrange training for staff and members of the pensions decision-making and governance bodies to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills.

The Pensions Committee also agreed to delegate responsibility for implementation to the Director of Finance, and that there would be annual reporting on the Pension Fund's training policy and its implementation.

For the year ended 31 March 2014, a number of strategic training needs were identified and fulfilled in relation to the reform of the Local Government Pension Scheme in 2015, and the actuarial valuation taking place during 2014.

The table below summarises how training needs were fulfilled during the year.

Cipfa Framework Core Competency Area	Training Specifics	Training Event	Attendees
Pensions accounting & audit standards.	Training and knowledge sharing on Pension Fund Accounts preparation.	17/04/13: CIPFA Pensions Network training course.	Council officers (2)
Investment performance & risk management. Financial markets & products knowledge. Pensions accounting & audit standards. Pensions legislative & governance context. Actuarial methods, standards & practices.	Income producing assets, audit and the fund accounts, governance, legal developments, managing multi-employer funds, actuarial valuation 2014.	18/09/13: CIPFA Pensions Network Workshops	Pensions Committee member (1)
Investment performance & risk management. Financial markets & products knowledge.	Investment strategies and investment products, long-term planning and	02/10/13 – 03/10/13: 'LGPS 2100' Local Authority Investment	Council officer (1) and Investment Sub-Committee members (3)

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	stewardship.	Seminar by Baillie Gifford	
Pensions legislative & governance context. Investment performance/risk management. Actuarial methods, standards & practices.	Legal background and context, implications for scheme member pensions, benchmarking, actuarial valuation 2014, economic outlook.	17/12/13: Reform of the LGPS in Scotland. Event run by LGPS Scotland Investment & Governance Group.	Members of Pensions Committee and Investment Sub-Committee (5)
Pensions legislative & governance context. Actuarial methods, standards & practices.	Update on LGPS 2015 reform. Overview of 2014 Actuarial Valuation process.	21/02/14: Presentation by Actuary to Pensions Committee.	Pension Committee members (12)

The specific training events set out above are supplemented by additional knowledge and skills acquired through other 'on the job' activities including; participation in working groups, attendance at meetings, general reading and research e.g. agenda reports and presentations, investment manager reports and briefings, magazines and other periodicals, online reading etc.

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Actuary's Statement as at 31 March 2014

HYMANS ROBERTSON LLP

This statement has been prepared in accordance with Regulation 31A(1)(d) of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008, and Chapter 6 of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the UK 2013/14.

Description of Funding Policy

The funding policy is set out in the administering authority's Funding Strategy Statement (FSS), dated January 2013. In summary, the key funding principles are as follows:

- ensure that sufficient resources are available to meet all liabilities as they fall due;
- enable employer contribution rates to be kept as nearly constant as possible and at reasonable cost to the taxpayers and employers;
- manage employers' liabilities effectively; and
- maximise the returns from investments within reasonable risk parameters.

The FSS sets out how the administering authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 32 of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008 was by Barnett Waddingham LLP as at 31 March 2011. This valuation revealed that the Fund's assets, which at 31 March 2011 were valued at £991 million on a smoothed basis, were sufficient to meet 97% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2011 valuation was £33 million. Individual employers' contributions for the period 1 April 2012 to 31 March 2015 were set in accordance with the Fund's funding policy as set out in its FSS.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in Barnett Waddingham's valuation report dated March 2012.

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth to retirement or expected earlier date of leaving pensionable membership.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market related value.

The key financial assumptions adopted for the 2011 valuation were as follows:

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Financial assumptions	31 March 2011	
	% p.a. Nominal	% p.a. Real(CPI)
Discount rate	6.4%	3.4%
Pay increases	5.0%	2.0%
Price inflation/Pension increases	3.0%	-

The key demographic assumption was the allowance made for longevity. The life expectancy assumptions are based on the SAPS series of tables with improvements in line with the CMI model subject to a long term rate of improvement of 1% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	21.3 years	23.5 years
1. Future Pensioners*	22.6 years	25.1 years

*Currently aged 45

Copies of the 2011 valuation report and Funding Strategy Statement are available on request from The Highland Council, the Administering Authority to the Fund.

Experience over the period since April 2011

Experience has been mixed since the last valuation (excluding the effect of any membership movements). Real bond yields have fallen (increasing the value placed on liabilities) whilst asset returns have been slightly higher than expected. Overall, it is likely that the funding level has fallen since the 2011 valuation.

The next actuarial valuation will be carried out as at 31 March 2014. The Funding Strategy Statement will also be reviewed at that time.

Richard Warden

FFA Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
13 May 2014

Hymans Robertson LLP
20 Waterloo Street
Glasgow

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Independent Auditor's Report

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

I certify that I have audited the financial statements of The Highland Council Pension Fund for the year ended 31 March 2014 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Pension 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 2013/14 (the 2013/14 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, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Respective responsibilities of the Director of Finance and auditor

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

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on financial statements

In my opinion the financial statements:

- give a true and fair view in accordance with applicable law and the 2013/14 Code of the financial transactions of The Highland Council Pension Fund during the

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year ended 31 March 2014, 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 2013/14 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973 and the Local Government in Scotland Act 2003.

Opinion on other prescribed matters

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

Matters on which I am required to report by exception

I am required to report to you if, in my opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- I have not received all the information and explanations I require for my audit; or
- the Governance Compliance Statement does not comply with guidance from the Scottish Ministers; or
- the Statement on the System of Internal Financial Control does not comply with the 2013/14 Code.

I have nothing to report in respect of these matters.

Stephen Boyle CPFA
Assistant Director of Audit

Audit Scotland
4th floor South Suite
8 Nelson Mandela Place
Glasgow G2 1BT

29 September 2014