

**RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL****MUNICIPAL YEAR 2017-2018****PENSION FUND COMMITTEE****13<sup>TH</sup> NOVEMBER 2017****REPORT OF: THE GROUP DIRECTOR,  
CORPORATE AND FRONTLINE  
SERVICES****AGENDA ITEM NO.6****PENSION FUND AUDITED  
FINANCIAL STATEMENTS  
2016/17****Author – Barrie Davies, Director of Financial Services (01443) 680559****1.0 PURPOSE OF REPORT**

- 1.1 This report sets out the role of the Committee with regard the approval process for the Pension Fund Accounts and provides members with the opportunity to discharge their responsibilities in this regard.

**2.0 RECOMMENDATIONS**

- 2.1 It is recommended that the Committee :
- 2.1.1 Note the audited financial statements of the Pension Fund for the financial year 2016/17; and
- 2.1.2 Note the Audit Report on the financial statements as provided by the Wales Audit Office.

**3.0 BACKGROUND**

- 3.1 The role of the Pension Fund Committee with regard to the Fund financial statements is set out in the terms of reference, namely :

- Considering the Fund's financial statements as part of the approval process and agreeing the Fund's Annual Report. Receive internal and external audit reports on the same.

**4.0 CONCLUSION**

- 4.1 This report satisfies the responsibilities of the Committee with regard to the financial statements of the Pension Fund.

## **Rhondda Cynon Taf Pension Fund Accounts**

### **Background to the Fund**

The Rhondda Cynon Taf Pension Fund was established with effect from 1<sup>st</sup> April 1996, upon the reorganisation of Local Government in Wales under the Local Government Pension Scheme (Local Government Reorganisation in Wales) Regulations, 1995. The Local Government Pension Scheme (LGPS) is open to all employees in Local Government apart from teachers, who have their own scheme. It is also open to employees of other organisations that have been accepted into the fund.

The Rhondda Cynon Taf Pension Fund provides pension benefits for employees of Rhondda Cynon Taf, Bridgend and Merthyr Tydfil County Borough Councils, together with employees from around 40 other bodies. Organisations participating in the fund include:

- Scheduled bodies, which are local authorities and similar bodies whose staff are automatically entitled to be members of the fund.
- Admitted bodies, which are other organisations that participate in the fund under an admission agreement between the fund and the relevant organisation. Admitted bodies include voluntary, charitable and similar bodies or private contractors undertaking a local authority function following outsourcing to the private sector.

### **Fund Administration and Investments**

Rhondda Cynon Taf CBC has responsibility for the interpretation of pension legislation, the creation and maintenance of records, the calculation and payment of benefits and the provision of information to employees, employers and other relevant bodies.

The Pension Fund Committee is responsible for the strategic management of the RCT Pension Fund in accordance with its term of reference.

The Group Director Corporate and Frontline Services (in their capacity as S151 officer) supported by an Investment and Administration Advisory Panel, has delegated responsibility for all day to day operational matters.

The Pension Fund Investment and Administration Panel, is chaired by the Group Director Corporate & Frontline Services, and consists of two independent investment advisors and other Senior Finance Officers.

The Panel meets quarterly to consider both administration and investment issues and determine policy in light of market movements and to question and challenge the Investment Managers on their activities and performance. At the Net Assets Statement date there were six Investment Managers carrying out the actual day-to-day investment management of the Fund's assets:

- Baillie Gifford (Global Equities and High Alpha Equities)
- Newton (High Alpha Equities)
- BlackRock (UK Equities and Passive Equities)

- Invesco (UK Equities)
- BMO Global Asset Management (Bonds)
- CBRE (Property)

The Pension Board was established in accordance with the Public Service Pensions Act 2013 to assist Rhondda Cynon Taf CBC as 'scheme manager' with achieving effective and efficient governance and administration of the Rhondda Cynon Taf Pension Fund.

### **All Wales Pension Fund Investment Pooling**

On the 15<sup>th</sup> March the Council approved the establishment of a Joint Governance Committee to oversee the pooling of the investments of the eight Local Government Pension Scheme (LGPS) funds in Wales.

Under the new arrangements Rhondda Cynon Taf CBC and the other administering authorities will retain control over setting their own funds investment strategy and detailed asset allocation. This continues to allow the broad risk and return objectives of the investment strategy to be determined in line with each pension fund's overall funding strategy. Funds will then invest in the Pool through asset Sub-Funds which will be made available by the appointed Pool Operator.

**Fund Account**

2015/16			2016/17	
£'000		Note:	£'000	£'000
	<b>Contributions</b>			
(85,799)	Employer contributions	8.0	(83,216)	
(25,663)	Member contributions	8.0	(25,388)	
<b>(111,462)</b>				<b>(108,604)</b>
	<b>Transfers in from other Pension Funds</b>			
0	Group Transfers in from other schemes or funds		0	
(4,047)	Individual Transfers from other schemes or funds		(3,939)	
				<b>(3,939)</b>
(9,112)	<b>Other income</b>		(3,599)	
				<b>(3,599)</b>
<b>(124,621)</b>				<b>(116,142)</b>
	<b>Benefits</b>			
94,818	Pensions		97,391	
24,198	Commutation of pensions and lump sum retirement benefits		18,504	
2,684	Lump sum death benefits		2,573	
<b>121,700</b>		8.0		<b>118,468</b>
	<b>Payments to and on account of leavers</b>			
334	Refunds to members leaving Scheme or Fund		244	
153	Payments to members joining State Scheme or Fund		101	
0	Group Transfers to other schemes		0	
6,312	Individual transfers to other schemes		8,094	
<b>6,799</b>				<b>8,439</b>
<b>128,499</b>				<b>126,907</b>
3,878	Net Addition/(Withdrawals) from Dealings with Members		10,765	
				<b>10,765</b>
9,718	Management Expenses	9.0	11,499	
				<b>11,499</b>
<b>13,596</b>	<b>Net Additions/(Withdrawals) Including Fund Management Expenses</b>			<b>22,264</b>
	<b>Investment income</b>			
(31,142)	Dividends from equities		(32,203)	
(23,137)	Income from bonds		(20,067)	
0	Income from index-linked securities		0	
(2,724)	Income from pooled investment vehicles		(2,539)	
(5,953)	Income from pooled property investments		(7,230)	
(93)	Interest on cash deposits		(38)	
<b>(63,049)</b>				<b>(62,077)</b>

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13,034	<b>(Profits) and losses on disposal of investments and changes in the value of investments</b>		(477,314)	
				<b>(477,314)</b>
1,610	<b>Taxes on income</b>		744	
				<b>744</b>
<b>(48,405)</b>	<b>Net Returns on Investments</b>			<b>(538,647)</b>
<b>(34,809)</b>	<b>Net (increase)/decrease in net assets available for benefits during the year</b>			<b>(516,383)</b>
<b>(2,448,339)</b>	<b>Opening Net Assets</b>			<b>(2,483,148)</b>
<b>(2,483,148)</b>	<b>Closing Net Assets</b>			<b>(2,999,531)</b>

**Net Assets Statement**

31/03/2016			31/03/2017	
£'000		Note:	£'000	£'000
	<b>Investment Assets</b>	4.0		
1,412,631	Equities		1,823,693	
514,703	Bonds		566,144	
59,862	Pooled Investment Vehicles - Open Ended investment companies		81,025	
232,587	Pooled Investment Vehicles - Managed funds		280,565	
162,106	Pooled Property Investments		169,498	
<b>2,381,889</b>				<b>2,920,925</b>
<b>86,063</b>	<b>Cash deposits</b>			<b>63,023</b>
	<b>Other investment balances</b>			
5,753	Accrued interest		6,284	
7,662	Investment debtors		11,113	
2,940	Tax recoverable		2,575	
<b>16,355</b>				<b>19,972</b>
<b>2,484,307</b>				<b>3,003,920</b>
	<b>Investment Liabilities</b>			
<b>(5,828)</b>	Investment creditors			<b>(10,220)</b>
	<b>Current Assets</b>			
5,118	Contributions due from employers and employees	10.0	5,209	
2,161	Cash balances		3,055	
389	Amount owed from RCTCBC		20	
1,638	Other current assets		1,300	
<b>9,306</b>				<b>9,584</b>
	<b>Current Liabilities</b>			
<b>(4,637)</b>	Current liabilities			<b>(3,753)</b>
	<b>Net assets of the scheme available to fund benefits at period end</b>			
<b>2,483,148</b>				<b>2,999,531</b>

The accounts summarise the transactions of the scheme and deal with the net assets at the disposal of the trustees. They do not take into account obligations to pay pensions and benefits which fall due after the end of the scheme year. A summary of the actuarial position of the scheme, which takes account of these obligations, is included in note 4. These accounts should be read in conjunction with the Actuarial Valuation Report.

## **1.0 Introduction**

These accounts have been prepared in accordance with the requirements of the CIPFA Code of Practice on Local Authority Accounting 2016/17 which is based upon International Financial Reporting Standards (IFRS) as amended for the UK public sector. A more detailed Pension Fund Annual Report is available on request from the Group Director Corporate & Frontline Services.

## **2.0 Accounting Policies**

### **2.1 Accruals Concept**

Where material, accruals are made for employee and employer contributions, investment income, benefits paid, administration costs, investment management fees and advisors fees. Transfer values are accounted for on a cash basis, with the exception of material group transfers, which are accounted for during the year of effective date of transfer or the year in which the actuary values the transfer if later.

### **2.2 Investment Valuation of Financial Instruments**

In terms of "Fair Value", all investments have quoted prices in active markets, with the exception of Pooled Property Funds. Listed securities are valued in accordance with IAS 39 – Financial Instruments, using bid prices as at 31<sup>st</sup> March 2017 obtained from recognised Stock Exchanges. Fixed interest securities are valued "clean", excluding accrued interest. Sterling valuations of securities denominated in foreign currencies are based on closing exchange rates as at 31<sup>st</sup> March 2017.

Pooled Property Funds are valued by Fund Managers using reliable valuation techniques to determine Fair Value. Property valuations are represented by unit prices, based on underlying independent professional valuations. No assets require significant judgements or assumptions to determine Fair Value.

### **2.3 Additional Voluntary Contributions (AVCs)**

Scheme members may elect to make additional voluntary pension contributions from their salaries. These AVCs are not included in the Pension Fund Accounts in accordance with regulation 5(2)(b) of the Pension Scheme (Management and Investment of Funds) Regulations 2016.

The amount of AVCs paid during the year amounted to £1,210k (£1,273k in 2015/16) and the market value of separately invested AVCs at the Balance Sheet date was £8,094k (£6,939k in 2015/16).

### **2.4 Acquisition and Disposal Costs**

Transaction costs incurred in acquiring or disposing of investments are included as part of the purchase cost or netted off against sales proceeds, as appropriate. Transaction costs include fees, commissions and duties.

Transaction costs incurred during 2016/17 amounted to £0.7m (£0.7m in 2015/16).

In addition to the direct costs disclosed above, indirect costs are incurred through the bid-offer spread on investments within pooled investment vehicles. The amount of indirect costs is not separately provided to the scheme.

## **2.5 Taxation**

As a registered public service scheme the pension fund is exempt from UK income tax and capital gains tax. Overseas investment income incurs withholding tax in the country of origin unless exemption is granted.

Irrecoverable tax is accounted for as an expense in the Fund Account, with any recoverable tax shown as an asset in the Net Assets Statement.

There is a small liability to income tax on refunds of contributions and compounded pensions (small pensions converted into lump sums). These amounts are paid to HMRC on a quarterly basis.

VAT is recoverable on all activities, so the accounts are shown exclusive of VAT.

## **3.0 Actuarial Position**

The Fund's Actuary, AON Hewitt carried out an actuarial valuation of the Fund as at 31<sup>st</sup> March 2016 in compliance with Regulation 36 of the Local Government Pension Scheme (Administration) Regulations 2013. Actuarial valuations take place on a triennial basis with a number of key assumptions being made.

The methodology to calculate the pension fund liability reflects assumptions and estimates depending 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 return on pension fund assets.

Where a valuation reveals a deficiency (or surplus), employer contribution rates are adjusted to seek restoration of a 100% funding ratio. The recovery period for each employer is set by the Administering Authority in consultation with the Actuary.

The funding policy of the scheme is to ensure that:

- Employer contribution rates are kept as nearly constant as possible and at reasonable cost to the employers and taxpayers.
- Sufficient resources are available to meet all liabilities as they fall due.
- Employers' liabilities are managed effectively by seeking regular actuarial advice.
- Income from investments is maximised within reasonable risk parameters.



The result of the 2016 valuation is shown in the table below.

	<b>31/03/2016</b>	<b>31/03/2013</b>
	<b>£'m</b>	<b>£'m</b>
Funding Target	3,064	2,665
Market Value of Assets	2,485	2,080
Funding Deficit	579	585
Funding Ratio	81%	78%

The aggregate employer future service contribution rate is 17.1% of pensionable pay. To restore the funding ratio to 100% using a recovery period of 22 years the aggregate employer contribution rate is calculated to be 24.3%.

Contribution rates payable by each scheme employer will vary depending on their particular circumstances. Some employers will also phase in contribution increases over a maximum period of 3 years. Further details are available in the actuarial report.

Contribution rates have been calculated using the Projected Unit Method for most employers. The Attained Age Method has been used for some employers who do not permit new employees to join the Fund. The key assumptions made are listed below:

	<b>2016 Valuation</b>	<b>2013 Valuation</b>
<b>Assumption</b>	<b>% p.a.</b>	<b>% p.a.</b>
Average in service discount rate	4.5%	5.6%
Average left service discount rate	4.5%	5.6%
RPI inflation	3.1%	3.3%
CPI inflation	2.0%	2.4%
Pensionable Pay increases	3.3%	3.9%
Post-retirement mortality assumption - base table	SAPS Normal tables with scaling factors Men 100% Women 100%	SAPS Normal tables with scaling factors Men 100% Women 95%
Post-retirement mortality assumption - future improvements	CMI 2014 core projections with long-term improvement rate of 1.5% pa	CMI 2012 core projections with long-term improvement rate of 1.5% pa

In addition to the triennial funding valuation, the fund's actuary also undertakes a valuation of the pension fund liabilities, on an IAS 19 basis, every year using the same base data as the funding valuation rolled forward to the current financial year, taking account of changes in membership numbers and updating assumptions to the current year. This valuation is not carried out on the same basis as that used for setting fund contribution rates and the fund accounts do not take account of liabilities to pay pensions and other benefits in the future. In order to assess the value of the benefits on this basis, the actuary has updated the actuarial assumptions (set out below) from those used for funding

purposes. The actuary has also used valued ill health and death benefits in line with IAS 19.

The CIPFA Code of Practice on Local Authority Accounting also requires the disclosure of the relationship between the actuarial present value of promised retirement benefits and the net assets.

	Value as at 31/03/2016	Value as at 31/03/2013
	£'m	£'m
Fair Value of net assets	2,485	2,079
Actuarial present value of promised retirement benefits	3,471	3,200
Surplus / (deficit) in the Fund as measured for IAS 26 purposes	(985)	(1,121)

As noted above, the liabilities above are calculated on an IAS 19 basis and therefore will differ from the results of the 2016 triennial funding valuation because IAS 19 stipulates a discount rate rather than a rate which reflects market rates.

#### 4.0 Analysis of Investments at Fair Value

	2015/16		2016/17	
	£'000	£'000	£'000	£'000
<b><u>Equities</u></b>				
UK	360,050		446,452	
Overseas	1,052,581		1,377,241	
		<b>1,412,631</b>		<b>1,823,693</b>
<b><u>Bonds</u></b>				
UK	456,709		504,792	
Overseas	57,994		61,352	
		<b>514,703</b>		<b>566,144</b>
<b><u>Index linked</u></b>				
UK	0		0	
Overseas	0		0	
		<b>0</b>		<b>0</b>
<b><u>Pooled funds</u></b>				
UK	145,808		164,456	
Overseas - other	146,641		197,134	
		<b>292,449</b>		<b>361,590</b>
<b><u>Pooled funds - property</u></b>				
UK – other	153,427		162,407	
Overseas - other	8,679		7,091	
		<b>162,106</b>		<b>169,498</b>
<b>Total long-term investments</b>		<b>2,381,889</b>		<b>2,920,925</b>

The Fund does not participate in any stock lending arrangements. All investments held are quoted investments with the exception of property, which is valued at Fair Value and no assets reclassified. Carrying values of assets held in the Net Assets Statement are the same as the Fair Values shown above.

All investments above are deemed to be Financial Instruments designated "Fair Value through Profit and Loss". All investment income, profits/losses on disposals of investments, and changes in the value of investments recognised in the Fund Account arise from Financial Instruments designated "Fair Value through Profit and Loss", with the exception of interest on cash deposits. Cash deposits are deemed to be Financial Instruments designated "Loans and Receivables".

Quoted equities and cash are classed as fair value hierarchy level 1. Bond and pooled property are classified as fair value hierarchy level 2.

## 5.0 Fund Manager Asset Allocation

The market values of investments held by the fund managers employed by the fund are detailed in the following table.

Fund Manager	Market Value		Proportion of Fund	
	31/03/2016	31/03/2017	31/03/2016	31/03/2017
	£'000	£'000	%	%
Baillie Gifford (Equities)	510,410	656,126	20.7	22.0
Baillie Gifford (High Alpha Equities)	489,916	661,065	19.9	22.2
Newton (High Alpha Equities)	404,498	493,328	16.4	16.5
Invesco (UK Equities)	131,535	146,034	5.3	4.9
BlackRock (UK Equities)	117,889	138,748	4.8	4.7
L&G (Passive Equities)	101,052	0	4.1	0.0
BlackRock (Passive Equities)	0	134,531	0.0	4.5
BMOgam (Bonds)	531,141	573,558	21.5	19.2
CBRE (Property)	162,530	173,373	6.6	5.8
Internal	18,621	7,005	0.7	0.2
<b>Total</b>	<b>2,467,592</b>	<b>2,983,768</b>	<b>100</b>	<b>100</b>

No single investment accounted for more than 5% of the Fund's assets.

The market value of investments shown in this table includes short-term investments such as cash balances and money deposits, and so differs from the total of long-term investments only, as shown in note 4.0 and note 7.0.

Investment risk is mitigated by employing a number of fund managers to diversify manager risk, with mandates covering a variety of assets including equities, bonds and property. Managers must maintain a diversified portfolio of investments and comply with the LGPS investment regulations, and any additional restrictions set by the Pension Fund Investment and Administration

Panel. The underlying investments are further diversified by country and industry sector.

Each manager's performance is monitored quarterly by the Pension Fund Investment and Administration Panel against a target linked to an asset allocation benchmark, effectively constraining managers from deviating significantly from the intended approach, while still permitting some flexibility to enhance returns.

## 6.0 Contingencies

There is a contingent liability of £449k (£375k in 2015/16) in respect of refundable contributions for leavers who have not yet claimed refunds.

## 7.0 Reconciliation of Investment Asset Valuation

A reconciliation of the opening and closing investment valuations is given below.

<b>Fund Manager</b>	<b>Market Value 01/04/16</b>	<b>Purchases</b>	<b>Sales at Historic Book Cost</b>	<b>Change in Market Value</b>	<b>Market Value 31/03/17</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
Baillie Gifford (Equities)	495,741	96,606	(46,093)	104,352	650,606
Baillie Gifford (High Alpha Equities)	481,339	63,321	(41,005)	147,975	651,630
Newton (High Alpha Equities)	381,514	123,209	(78,771)	43,763	469,715
Invesco (UK Equities)	131,535	1,726	0	12,773	146,034
BlackRock (UK Equities)	113,899	13,660	(10,105)	15,383	132,837
BlackRock (Passive Equities)	0	124,238	0	10,221	134,459
L&G (Passive Equities)	101,052	0	(79,466)	(21,586)	0
BMOgam (Bonds)	514,703	600,274	(560,234)	11,403	566,146
CBRE (Property)	162,106	20,655	(24,432)	11,169	169,498
<b>Total</b>	<b>2,381,889</b>	<b>1,043,689</b>	<b>(840,106)</b>	<b>335,453</b>	<b>2,920,925</b>

## 8.0 Contributions Receivable and Benefits Payable

Contributions received and benefits paid are shown in the table below.

Type of Body	Member Contributions		Employer Contributions		Pensions, Lump Sums and Death Benefits	
	2015/16	2016/17	2015/16	2016/17	2015/16	2016/17
	£'000	£'000	£'000	£'000	£'000	£'000
Administering	8,171	8,018	28,243	28,285	33,015	31,017
Admitted	3,281	3,376	13,814	14,076	12,707	13,654
Scheduled	14,211	13,994	43,742	40,855	75,978	73,797
<b>Total</b>	<b>25,663</b>	<b>25,388</b>	<b>85,799</b>	<b>83,216</b>	<b>121,700</b>	<b>118,468</b>

Included in employer contributions are £8,179k of deficit funding contributions (£10,879k in 2015/16). There are no augmented contributions (£26k in 2015/16).

## 9.0 Management Expenses

The management expenses borne by the Fund in 2016/17 are set out below:

	2015/16	2016/17
	£'000	£'000
Administrative Costs	1,803	1,748
Investment Management Expenses	7,781	9,456
Oversight and Governance Costs	134	295
<b>Total</b>	<b>9,718</b>	<b>11,499</b>

Management Expenses represents 0.33% (0.39% in 2015/16) of the value of the Pension Fund as at 31<sup>st</sup> March, 2017.

The investment management expenses borne by the fund in 2016/17 are set out below:

	2015/16	2016/17
	£'000	£'000
Management Fees	6,073	6,479
Performance Related Fees	856	2,033
Custody Fees	153	264
Transaction Costs	699	680
<b>Total</b>	<b>7,781</b>	<b>9,456</b>

## 10.0 Transactions with Related Parties

In the course of fulfilling its role as administering authority to the Fund, Rhondda Cynon Taf CBC provided services to the Fund for which it charged £1.5m (£1.6m in 2015/16). These costs are mainly in respect of those staff employed in ensuring that the pension service is delivered.

At the year-end, contributions outstanding from the Employing Bodies in the Fund amounted to £5.2m (£5.1m in 2015/16), of which £3.9m related to employer contributions and £1.3m to employee contributions.

There are members of the Pension Fund Investment and Administration Panel, the Pension Fund Board and the Pension Fund Committee who are also members of the Rhondda Cynon Taf Pension Fund.

The administration of the Rhondda Cynon Taf Pension Fund is a function of full Council, with responsibility being delegated to the Group Director, Corporate and Frontline Services. As such, the Group Director is required to declare any interests with related parties. The disclosure can be found in the main accounts of Rhondda Cynon Taf County Borough Council.

Officer remuneration and Members allowances can be found in the main accounts of Rhondda Cynon Taf County Borough Council.

### **11.0 Membership of the Fund**

Fund membership at 31<sup>st</sup> March is as follows:

	<b>2016</b>	<b>2017</b>
Active Employers	46	49
Contributors	25,501	23,918
Pensioners	15,830	16,315
Dependants	2,640	2,640
Deferred Beneficiaries	22,358	24,641

### **12.0 Group Transfers**

No material group transfers are recognised in 2016/17. However, the Fund is currently processing inward and outward group transfers. Such transfers are either not material to the financial statements or are in the initial stages of actuarial discussions. Amounts are also due in respect of final settlement of transfers recognised in 2014/15. Estimates are not yet available.

### **13.0 Nature and Extent of Risks Arising From Financial Instruments**

A financial instrument is defined as any contract that gives rise to a financial asset of one entity and a financial liability (or equity instrument) of another entity. There are three main ways in which the Pension Fund is exposed to risk from financial instruments:

- Credit Risk
- Liquidity Risk
- Market Risk

The overall objective is to minimise the risk of a reduction in the value of the Fund, and to maximise the opportunity for gains within reasonable risk parameters.

The Funding Strategy Statement identifies key risks to the Pension Fund together with the countermeasures undertaken to mitigate the risks.

### 13.1 Credit Risk

Credit risk is the possibility that a counterparty will fail to discharge its obligation to the Pension Fund, causing a financial loss. Counterparties considered are banks and financial institutions with whom investments are placed, employers within the Fund and Investment Managers. The risk of counterparties failing to discharge obligations is managed in a number of ways:

- Counterparties for cash investments made by the Administering Authority must meet the strict credit criteria set out in the Rhondda Cynon Taf CBC Treasury Management Strategy.
- Participating employers may be required to provide a bond to cover the risk to the Fund should they be unable to meet their pension contribution obligations.
- Investment Managers manage funds that are held in the name of the Pension Fund, not in the name of the Investment Managers. In the event of the Investment Manager being unable to fulfil their obligations the Fund's investments will not be considered part of their asset portfolio.

The Pension Fund has had no experience of counterparty default in the last five years. Cash deposits held by the Administering Authority for the Pension Fund as at 31<sup>st</sup> March 2017 amounted to £3.9m with the institutions shown in the table below.

Institution	Balance at 31/03/17 £'000	Maturity Date
Debt Management Account Deposit Facility	3,950	03/04/2017
<b>Total</b>	<b>3,950</b>	

The Treasury Management strategy sets a limit of £15m for cash deposits with individual Local Authorities.

### 13.2 Liquidity Risk

Liquidity risk is the risk that the Pension Fund will not be able to meet its financial obligations as they fall due. This risk is managed by:

- Maintaining a robust cash flow monitoring and forecasting model.
- Ensuring that the Pension Fund has access to cash in the short and medium-term to pay pensions by managing cash flow from money-market investments.

- Taking actuarial advice to set employer contribution rates at triennial valuations in order to meet the long-term funding requirements to pay pensions and other commitments.

The Administering Authority has immediate access to internally managed Pension Fund cash balances held with its own bank, Barclays. The Authority also invests Pension Fund cash in short-term deposits with the Debt Management Office or other UK public bodies for periods normally less than 3 months.

### 13.3 Market Risk

Market risk is the risk of a loss in the value of investment assets from movements in investment markets e.g. asset prices, interest rates and currency exchange rates. This risk is managed by ensuring that the Fund invests in a broad range of assets diversified by Investment Manager, asset class and geographical region.

Following analysis of historic data, State Street, the Fund's custodian, have provided a view of potential market movements for the 2017/18 financial year. The possible impact of movements is shown in the following tables:

Asset type	31/03/17	Change	Value on	Value on
	Value		increase	decrease
	£'000	%	£'000	£'000
UK Equities	610,908	8.6	663,446	558,370
Overseas Equities	1,574,375	10.21	1,735,119	1,413,631
Bonds	566,144	6.77	604,472	527,816
Property	169,498	2.46	173,668	165,328
Cash	61,889	0.01	61,895	61,883
<b>Total</b>	<b>2,982,814</b>		<b>3,238,600</b>	<b>2,727,028</b>

The Fund's interest rate risk is monitored regularly with the advice of the Administering Authority's treasury advisors. Interest rates changes can affect Fund income and asset values.

Assuming that all other variables, particularly exchange rates, remain unchanged, a movement in interest rates of 1% for the 2017/18 financial year would have the following effect:

Asset type	31/03/17	Value on	Value on
	Value	increase	decrease
	£'000	£'000	£'000
Bond securities	566,144	571,805	560,483
Cash deposits & balances	61,889	62,508	61,270
<b>Total</b>	<b>628,033</b>	<b>634,313</b>	<b>621,753</b>



Currency risk is the risk to income and investment asset values from changes in foreign exchange rates. The Fund is exposed to this risk from non-sterling denominated investments in a range of assets.

A movement in currency exchange rates of 8.64% would have the following effect:

<b>Asset type</b>	<b>31/03/17</b>	<b>Value on</b>	<b>Value on</b>
	<b>Value</b>	<b>increase</b>	<b>decrease</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
Overseas Equities	1,574,375	1,710,401	1,399,147
Overseas Bonds	61,352	66,653	54,524
Overseas Pooled Property	7,091	7,704	6,302
<b>Total</b>	<b>1,642,818</b>	<b>1,784,758</b>	<b>1,459,973</b>



WALES AUDIT OFFICE  
SWYDDFA ARCHWILIO CYMRU

Archwilydd Cyffredinol Cymru  
Auditor General for Wales

# Audit of Financial Statements Report and Management Letter – Rhondda Cynon Taf Pension Fund

Audit year: 2016-17

Date issued: September 2017

Document reference: **491A2017**

This document has been prepared as part of work performed in accordance with statutory functions.

In the event of receiving a request for information to which this document may be relevant, attention is drawn to the Code of Practice issued under section 45 of the Freedom of Information Act 2000.

The section 45 code sets out the practice in the handling of requests that is expected of public authorities, including consultation with relevant third parties. In relation to this document, the Auditor

General for Wales and the Wales Audit Office are relevant third parties. Any enquiries regarding

disclosure or re-use of this document should be sent to the Wales Audit Office at

[infoofficer@audit.wales](mailto:infoofficer@audit.wales).

We welcome correspondence and telephone calls in Welsh and English. Corresponding in Welsh will not lead to delay. Rydym yn croesawu gohebiaeth a galwadau ffôn yn Gymraeg a Saesneg. Ni fydd gohebu yn Gymraeg yn arwain at oedi.

# Contents

This document summarises the conclusions on the audit of Pension Fund's financial statements for 2016-17 including our recommendations for the year. The Auditor General intends to issue an unqualified audit report on your financial statement, although there are some issues to report to you prior to their approval.

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# Summary report

## Introduction

- 1 The purpose of this report is twofold:
  - to set out for consideration the matters arising from the audit of the financial statements of the Rhondda Cynon Taf Pension Fund (the Pension Fund), for 2016-17, that require reporting to those charged with governance, in time to enable appropriate action; and
  - to capture the recommendations arising from our audit work.
- 2 The Auditor General is responsible for providing an opinion on whether the financial statements give a true and fair view of the financial position of the Pension Fund at 31 March 2017 and its income and expenditure for the year then ended.
- 3 We do not try to obtain absolute assurance that the financial statements are correctly stated, but adopt the concept of materiality. In planning and conducting the audit, we seek to identify material misstatements in your financial statements, namely, those that might result in a reader of the accounts being misled.
- 4 The quantitative level at which we judge such misstatements to be material for the Pension Fund is £30 million. Whether an item is judged to be material can also be affected by certain qualitative issues such as legal and regulatory requirements and reader sensitivity.

## Status of the audit

- 5 We received the draft financial statements for the year ended 31 March 2017 on 16 June 2017, in line with the timetable we had agreed, and have now substantially completed the audit work. The statutory deadlines remain as 30 June for accounts preparation and 30 September for audit certification, however from 2020/21 onwards these dates will be brought forward to 31 May and 31 July respectively.
- 6 This is a noteworthy achievement by the finance team and we would like to thank them for their efforts. Undertaking the production and audit of the accounts earlier has identified a number of learning points for both the finance team and ourselves. We will consider these in more detail at a future post project learning session to ensure they are captured and built into processes for future years. Given the earlier statutory deadlines mentioned above, the next few years are undoubtedly going to be challenging for both the Council's finance team and auditors alike.
- 7 We are reporting to you the more significant issues arising from the audit, which we believe you must consider prior to approval of the financial statements. The audit team has already discussed these issues with Group Director Corporate & Frontline Services and his senior finance team.

## Proposed audit report

- 8 It is the Auditor General's intention to issue an unqualified audit report on the financial statements once you have provided us with a Letter of Representation based on that set out in [Appendix 1](#).
- 9 The proposed audit report is set out in [Appendix 2](#). Please note that this audit report covers both Rhondda Cynon Taf County Borough Council and RCT Pension Fund.

## Significant issues arising from the audit

### Uncorrected misstatements

- 10 We set out below the uncorrected misstatement we identified in the financial statements, which has been discussed with management but remains uncorrected as management consider that it does not have a material effect on the accounts. If you decide not to correct this misstatement, there will be no impact upon the opinion given in our audit report as we also consider this item to be non-material.
  - **The Cash and Current Liabilities figures on the balance sheet are overstated by £3 million.** Whilst the physical cash was held in the correct bank account, this has been accounted for incorrectly in the financial statements, due to a miscoding error. It was therefore accounted for as Pension Fund cash instead of Rhondda Cynon Taf County Borough Council cash. If corrected, both figures would be reduced by this amount.

### Corrected misstatements

- 11 There were a small number of narrative and minor amendments made as a result of the audit, which we do not consider significant enough to be drawn to your attention.

### Other significant issues arising from the audit

- 12 In the course of the audit, we consider a number of matters both qualitative and quantitative relating to the accounts and report any significant issues arising to you. There were no issues arising in these areas this year:
  - **We have no concerns about the qualitative aspects of your accounting practices and financial reporting.** In general we found the information provided to be relevant, reliable, comparable, material and easy to understand. We concluded that accounting policies and estimates are appropriate and financial statement disclosures unbiased, fair and clear. However, we have some made some recommendations for future improvement at [Appendix 3](#).

- **We did not encounter any significant difficulties during the audit.** We received information in a timely and helpful manner and were not restricted in our work.
- **There were no significant matters discussed and corresponded upon with management which we need to report to you.**
- **There are no other matters significant to the oversight of the financial reporting process that we need to report to you.**
- **We did not identify any material weaknesses in your internal controls.**
- **There are not any other matters specifically required by auditing standards to be communicated to those charged with governance.**

## Recommendations arising from our 2016-17 audit work

- 13 The recommendations arising from our audit work are set out in [Appendix 3](#). Management has responded to them and we will follow up progress on them during next year's audit. Where any actions are outstanding, we will continue to monitor progress and report it to you in next year's report.

## Independence and objectivity

- 14 As part of the finalisation process, we are required to provide you with representations concerning our independence.
- 15 We have complied with ethical standards and in our professional judgment, we are independent and our objectivity is not compromised. There are no relationships between the Wales Audit Office and the Pension Fund that we consider to bear on our objectivity and independence.

# Appendix 1

## Suggested Letter of Representation

[Audited body's letterhead]

Auditor General for Wales  
Wales Audit Office  
24 Cathedral Road  
Cardiff  
CF11 9LJ

[Date]

### Representations regarding the 2016-17 financial statements

This letter is provided in connection with your audit of the financial statements of Rhondda Cynon Taf Pension Fund (the Pension Fund) for the year ended 31 March 2017 for the purpose of expressing an opinion on their truth and fairness.

We confirm that to the best of our knowledge and belief, having made enquiries as we consider sufficient, we can make the following representations to you.

### Management representations

#### Responsibilities

We have fulfilled our responsibilities for:

- The preparation of the financial statements in accordance with legislative requirements and the Code of Practice on Local Authority Accounting in the United Kingdom; in particular the financial statements give a true and fair view in accordance therewith.
- The design, implementation, maintenance and review of internal control to prevent and detect fraud and error.

#### Information provided

We have provided you with:

- Full access to:
  - all information of which we are aware that is relevant to the preparation of the financial statements such as books of account and supporting documentation, minutes of meetings and other matters;
  - additional information that you have requested from us for the purpose of the audit; and



- unrestricted access to staff from whom you determined it necessary to obtain audit evidence.
- The results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- Our knowledge of fraud or suspected fraud that we are aware of and that affects the Pension Fund and involves:
  - management;
  - employees who have significant roles in internal control; or
  - others where the fraud could have a material effect on the financial statements.
- Our knowledge of any allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, regulators or others.
- Our knowledge of all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.
- The identity of all related parties and all the related party relationships and transactions of which we are aware.
- We have informed you of any concerns or comments made by regulators about the Pension Fund, its fund managers and any assets/liabilities.

## Financial statement representations

All transactions, assets and liabilities have been recorded in the accounting records and are reflected in the financial statements. The Pension Fund holds the title for the investment assets recognised at 31 March 2017.

Significant assumptions used in making accounting estimates, including those measured at fair value, are reasonable.

Related party relationships and transactions have been appropriately accounted for and disclosed.

All events occurring subsequent to the reporting date which require adjustment or disclosure have been adjusted for or disclosed.

All known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

The financial statements are free of material misstatements, including omissions. The effects of uncorrected misstatements identified during the audit are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. A summary of these items is set out below:

- Detail required of the £3 million cash item not adjusted.

## Representations by Rhondda Cynon Taf Pension Fund

We acknowledge that the representations made by management, above, have been discussed with us.

We acknowledge our responsibility for the preparation of true and fair financial statements in accordance with the applicable financial reporting framework. The financial statements were approved by the Members of Rhondda Cynon Taf County Borough Council on 20 September 2017.

We confirm that we have taken all the steps that we ought to have taken in order to make ourselves aware of any relevant audit information and to establish that it has been communicated to you. We confirm that, as far as we are aware, there is no relevant audit information of which you are unaware.

Signed by:

Officer who signs on behalf of management

Date:

Signed by:

Officer or Member who signs on behalf of those charged with governance

Date:

## Appendix 2

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### Audit report of the Auditor General to the Members of Rhondda Cynon Taf County Borough Council

I have audited the accounting statements and related notes of:

- Rhondda Cynon Taf County Borough Council; and
- Rhondda Cynon Taf County Borough Council Group; and
- Rhondda Cynon Taf Pension Fund;

for the year ended 31 March 2017 under the Public Audit (Wales) Act 2004.

Rhondda Cynon Taf County Borough Council's (RCTCBC) accounting statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, and the Cash Flow Statement.

RCTCBC's Group accounting statements comprise the Group Movement in Reserves Statement, the Group Comprehensive Income and Expenditure Statement, the Group Balance Sheet and the Group Cash Flow Statement.

Rhondda Cynon Taf Pension Fund's accounting statements comprise the Fund Account and the Net Assets Statement.

The financial reporting framework that has been applied in their preparation is applicable law and the Code of Practice on Local Authority Accounting in the United Kingdom 2016-17 based on International Financial Reporting Standards (IFRSs).

#### **Respective responsibilities of the responsible financial officer and the Auditor General for Wales**

As explained more fully in the Statement of Responsibilities for the Statement of Accounts set out on page 13, the responsible financial officer is responsible for the preparation of the statement of accounts, including RCTCBC's Group accounting statements Rhondda Cynon Taf Pension Fund's accounting statements, which gives a true and fair view.

My responsibility is to audit the accounting statements and related notes in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Financial Reporting Council's Ethical Standards for Auditors.

#### **Scope of the audit of the accounting statements**

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements and related notes sufficient to give reasonable assurance that the accounting statements and related notes are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the RCTCBC's, and RCTCBC Group's and Rhondda Cynon Taf Pension Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the

responsible financial officer and the overall presentation of the accounting statements and related notes.

In addition, I read all the financial and non-financial information in the Explanatory Foreword to identify material inconsistencies with the audited accounting statements and related notes 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 the accounting statements of RCTCBC**

In my opinion the accounting statements and related notes:

- give a true and fair view of the financial position of RCTCBC as at 31 March 2017 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016-17.

#### **Opinion on the accounting statements of RCTCBC Group**

In my opinion the accounting statements and related notes:

- give a true and fair view of the financial position of RCTCBC Group as at 31 March 2017 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016-17.

#### **Opinion on the accounting statements of Rhondda Cynon Taf Pension fund**

In my opinion, the Pension Fund accounts and related notes:

- give a true and fair view of the financial transactions of Rhondda Cynon Taf Pension Fund during the year ended 31 March 2017 and of the amount and disposition of the fund's assets and liabilities as at that date; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016-17.

#### **Opinion on other matters**

In my opinion, the information contained in the Explanatory Foreword is consistent with the accounting statements and related notes.

#### **Matters on which I report by exception**

I have nothing to report in respect of the following matters, which I report to you, if, in my opinion:

- adequate accounting records have not been kept;
- the accounting statements are not in agreement with the accounting records and returns; or
- I have not received all the information and explanations I require for my audit;
- the Governance Statement does not reflect compliance with guidance.

**Certificate of completion of audit**

I certify that I have completed the audit of the accounts of Rhondda Cynon Taf County Borough Council in accordance with the requirements of the Public Audit (Wales) Act 2004 and the Auditor General for Wales' Code of Audit Practice.

For and on behalf of  
Huw Vaughan Thomas  
Auditor General for Wales  
September 2017

Wales Audit Office  
24 Cathedral Road  
Cardiff  
CF11 9LJ

# Appendix 3

## Recommendations arising from our 2016-17 audit work

We set out all the recommendations arising from our audit with management's response to them. We will follow up these next year and include any outstanding issues in next year's audit report.

### Exhibit 1: Matter arising 1

<b>Matter arising 1 – Improvement in reporting the Fund Manager Asset Allocations in Note 5</b>	
<b>Findings</b>	The market value of the investments held by the Fund Managers employed by the Fund are detailed in Note 5. These include cash held by the Fund Manager and are not readily reconcilable to the balances in the Net Assets Statement due to timing differences for transactions at the year-end.
<b>Priority</b>	Medium
<b>Recommendation</b>	The format of the Note should be reviewed to enable the reader of the accounts to readily reconcile the Note with the figures in the Net Assets Statement.
<b>Benefits of implementing the recommendation</b>	To demonstrate that the accounts comply with the Code of Practice on Local Authority Accounting 2016-17.
<b>Accepted in full by management</b>	Yes
<b>Management response</b>	The Note will be reviewed to improve consistency between the Note and Net Asset Statement.
<b>Implementation date</b>	15 June 2018

### Exhibit 2: Matter arising 2

<b>Matter arising 2 – Improvement in reporting the profits and losses on disposal of investments and changes in the value of investments in Note 7</b>	
<b>Findings</b>	Note 7 reconciles the opening market value of the investments in the Net Assets Statement, the in-year purchases and sales, and the change in market value, to the closing market value of the investments. The change in market value does not agree to the figure in the Fund Account for 'Profit/loss on sale of investments and change in market value', because the sales are currently included in the Note at book cost, and not the sales proceeds.
<b>Priority</b>	Medium

<b>Matter arising 2 – Improvement in reporting the profits and losses on disposal of investments and changes in the value of investments in Note 7</b>	
<b>Recommendation</b>	The format of the Note should be reviewed so that the change in market value figure in the Note reconciles with the figure in the Fund Account.
<b>Benefits of implementing the recommendation</b>	To demonstrate that the accounts comply with the Code of Practice on Local Authority Accounting 2016-17.
<b>Accepted in full by management</b>	Yes
<b>Management response</b>	The Note will be reviewed to improve consistency between the Note and Fund Account.
<b>Implementation date</b>	15 June 2018

Exhibit 3: Matter arising 3

<b>Matter arising 3 – improved clarity in the reporting in Note 13.3</b>	
<b>Findings</b>	The Equities and Overseas Equities figures in Note 13.3 include both Equities and Pooled investments. As a result, the figures do not agree to the analysis of investments in Note 4, Analysis of Investments at Fair Value.
<b>Priority</b>	Low
<b>Recommendation</b>	The analysis of the investments in Note 13.3 should be on a consistent basis with the other Notes in the accounts.
<b>Benefits of implementing the recommendation</b>	To demonstrate that the accounts comply with the Code of Practice on Local Authority Accounting 2016-17.
<b>Accepted in full by management</b>	Yes
<b>Management response</b>	The Note will be reviewed to improve consistency between the notes relating to investments.
<b>Implementation date</b>	15 June 2018





Wales Audit Office  
24 Cathedral Road  
Cardiff CF11 9LJ

Tel: 029 2032 0500

Fax: 029 2032 0600

Textphone.: 029 2032 0660

E-mail: [info@audit.wales](mailto:info@audit.wales)

Website: [www.audit.wales](http://www.audit.wales)

Swyddfa Archwilio Cymru  
24 Heol y Gadeirlan  
Caerdydd CF11 9LJ

Ffôn: 029 2032 0500

Ffacs: 029 2032 0600

Ffôn testun: 029 2032 0660

E-bost: [post@archwilio.cymru](mailto:post@archwilio.cymru)

Gwefan: [www.archwilio.cymru](http://www.archwilio.cymru)