



ORKNEY
ISLANDS COUNCIL

**ANNUAL REPORT AND ACCOUNTS
OF THE PENSION FUND
2013/2014**

CONTENTS

FOREWORD BY HEAD OF FINANCE.....	1
OPERATING AND FINANCIAL REVIEW	4
Fund Performance.....	4
Investment Strategy	4
Investment Performance	5
Fund Update	6
STATEMENT OF RESPONSIBILITIES FOR THE STATEMENT OF ACCOUNTS	8
STATEMENT ON THE SYSTEM OF INTERNAL FINANCIAL CONTROL	9
STATEMENT OF ACCOUNTS 2013/14.....	11
Fund Account	11
Net Assets Statement.....	12
Notes to the Annual Accounts	13
GOVERNANCE ARRANGEMENTS.....	28
GOVERNANCE COMPLIANCE STATEMENT	31
INDEPENDENT AUDITOR'S REPORT	35
ANNEX 1 - Scheduled and Admitted Bodies	37
ANNEX 2 – Actuarial Statement for 2013/14.....	38
ANNEX 3 - Glossary of Terms	40
ADDITIONAL INFORMATION.....	42

FOREWORD BY HEAD OF FINANCE

Introduction

Welcome to the Annual Report and Accounts for the Orkney Islands Council Pension Fund for the year ended 31 March 2014.

The Local Government Pension Scheme Amendment (Scotland) Regulations 2010 (SSI 2010/349) require the Council, as administering authority for the Fund, to produce a separate statement of accounts for the Pension Fund and incorporate it into an Annual Report.

This Annual Report has been produced to provide Elected Members, Employers, scheme members and other interested parties with information concerning the administration and performance of the fund in financial year 2013/14 and I hope you find its content useful.

The Statement of Accounts contained in this report present the Fund's financial position for the year ended 31 March 2014. These have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 ("the Code"), supported by International Financial Reporting Standards (IFRS).

The Annual Report also contains a Governance Compliance Statement which demonstrates how well the Fund complies with the best practice principles set out by the Scottish Government.

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 current liabilities of the Fund. The net assets of the Fund (assets less current liabilities) represent the funds available to provide for pension benefits at the statement date.

Key Facts And Figures:

Value of the Fund at 31 March 2014 was £227.0 million (£204.7m at 31 March 2013).

An Operational and Investment Income Surplus of £22.3 million was generated on the activities of the fund (compared to £34.0m for year ended 31 March 2013).

The Increase in the Value of the Fund has been achieved mainly through a surplus of contributions over expenditure (£3.5m), investment net income (£4.1m) and increases in the market value of investments (£14.7m).

Performance of the Fund on a three year rolling average basis has been 10.3% p.a., giving a relative return above benchmark of 2.7%.

Fund membership increased by 194 to 3,213.

Employers contributed £6.9 million to the Fund (£6.8m to 31 March 2013).

Employees contributed £2.5 million (£2.3m to 31 March 2013).

Pension and other benefits paid out were £5.5 million (£5.4m to 31 March 2013).

Net Transfer values paid into the Fund because staff changed employers were £0.33 million (£0.034m to 31 March 2013).

Future Developments

Regulations 2014

The Independent Public Sector Pension Commission (the Hutton Review) reported in March 2011 with its key recommendation being the introduction of a career average earnings pension scheme (CARE). The aim of Lord Hutton was to strike an appropriate balance between those working for the public sector and the tax payer ensuring access to good pensions for staff while also improving control over future costs. The Hutton Review has been subject to much public debate and consultation, especially in England and Wales. In Scotland, the local Government Pension Scheme (Scotland) Regulations 2014 come into effect on 1 April 2015 and replace the current scheme. In contrast to the current scheme, which is a final salary pension scheme in which unreduced benefits are payable to members from the age of 65, the new scheme provides for members to accrue pension on a career average revalued earnings basis and for unreduced benefits to be payable from their state pension age.

Auto Enrolment

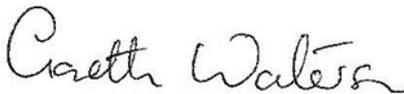
Auto-enrolment of employees has been implemented by the Orkney Islands Council during 2013/14. 83 employees have been auto enrolled since the staging date of 1 August 2013.

Development of the Investments Sub-Committee

Training activity for the members of the Investment Sub-Committee has been undertaken during the financial year 2013/14 to enable Councillors charged with the governance of the Fund to execute their role as a quasi-trustee effectively. On 15 April 2014, the Policy and Resources Committee agreed to establish a Local Government Pension Scheme Pension Fund Forum which once operational will report to the Investment Sub Committee.

Acknowledgement

I would like to take this opportunity to thank my colleagues in Corporate Services and the members of the Investment Sub-Committee for their help and co-operation in managing the financial affairs of the Pension Fund.



Gareth Waterson, BAcc, CA

Head of Finance

25 September 2014

OPERATING AND FINANCIAL REVIEW

Fund Performance

In the year to 31 March 2014 the fund rose 9.3%, performing ahead of its benchmark which rose 6.0%.

During the 12 months to 31 March, most major investment markets delivered strong returns. This was partly due to increasing investor confidence, partly to improving economic and corporate fundamentals, and partly in response to the continuation of the exceptionally loose monetary policy that remained a feature in many developed countries for much of the period.

In the US, signs that the economic recovery was gathering momentum proved to be particularly beneficial to the performance of equity markets. In December, the Federal Reserve unveiled plans to reduce its bond buying programme and subsequently announced plans to further trim the levels of support. There was also increased optimism over prospects for the UK, where economic data suggested that the worst of the slowdown had passed, and prompted talk of a possible interest rate rise. Meanwhile, the Japanese government of Shinzo Abe continued to try to address longstanding economic problems in their country, and this had a generally positive impact on the domestic stock market. The more upbeat mood extended to the Eurozone, where even the states hit hardest by the financial crisis showed tentative signs of improvement.

Although the investment environment is continuing to improve, the fund managers, Baillie Gifford have no doubt that further political and economic challenges lie ahead. However, our fund managers are generally optimistic on the outlook for the global economy. Markets may be volatile in the coming months, but our fund managers continue to focus on identifying and investing in companies with excellent growth prospects over the longer term.

Of the £22m increase in the value of the Fund, £7.1m was due to unrealised gains in the market value of investments. The surplus of contributions receivable over pensions payable was £3.5m (2013: £3.3m surplus), the cause of the increase being an increase in the total contributions receivable in the year from employer, employees and from transfers in. There was also an increase in the total benefits payable of £0.14m. Net investment income (dividends and interest) accounted for the remaining change in value of the Fund.

Detail of the performance of the Fund against benchmarks is shown on page 5.

(* m = million)

“Realised and Unrealised” Gains and Losses.

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

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

Our Accounts are however based on the market value of investments at 31 March 2014. This means that we have to show what profit or loss we would have made if we had sold all our investments on that day. The result is a notional “unrealised” profit or loss.

Investment Strategy

The detail of the Funds investment structure was reviewed in December 2010. The revised asset allocation and range guidelines that were applied with effect from 1 April 2011 are shown in the table below. Baillie Gifford’s performance target is to outperform the WM Performance Services (WM) Local Authority benchmark excluding property (re-balanced quarterly) by 1% p.a. when

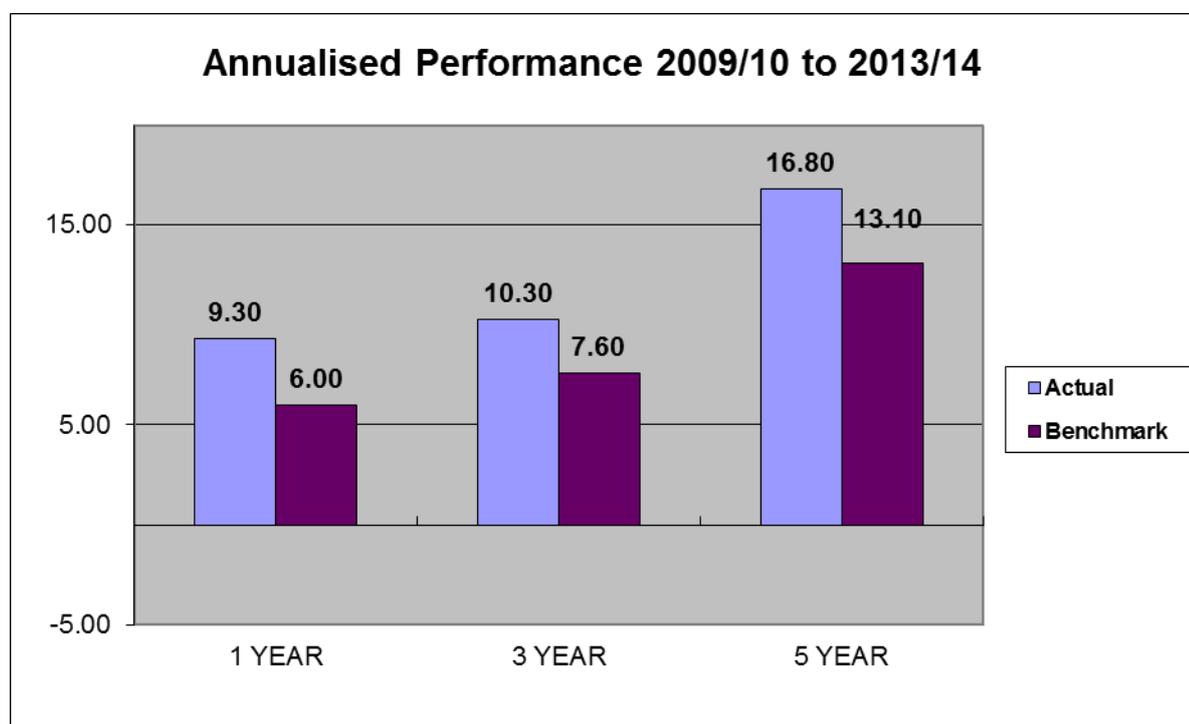
assessed over rolling 5 year periods, with effect from 1 July 2006. Baillie Gifford's asset allocation is periodically compared to the benchmark WM Local Authority average allocation for each asset class.

The following table indicates the 31 March 2014 position in relation to asset allocation versus the range guidelines and benchmark:

Asset Class	Asset Allocation at 31/03/14 %	Range %	Revised Benchmark %
UK Equities	26.4	20-50	26.8
Overseas Equities	46.4	25-55	35.9
Bonds	14.2	10-30	16.9
Alternative Investments	0	0-20	8.5
Cash	1.3	0-10	2.9
Pooled Funds	11.7	0-35	9.0
Total	100		100

Investment Performance

On an annualised basis the investment performance can be summarised as follows over the 1 year, 3 year and 5 year periods:-



The overall Fund return over 5 years was 16.80% versus the benchmark of 13.10%.

The top 10 direct equity holdings at 31 March 2014 were:-

Company	Market Value of Holding £ m
Prudential	5.3
Naspers	3.3
Royal Caribbean Cruises	3.0
Roche	2.7
British American Tobacco	2.4
Google	2.3
eBay	2.3
Ryanair	2.2
TD Ameritrade Holding Corp	2.2
Bunzl	2.2

Fund Update

Membership Details

Member Status	As at 31/3/2013	As at 31/3/2014
Contributing members	1,583	1,685
Pensioners	659	700
Deferred members	777	828
Total	3,019	3,213

Contributing Member	Someone who is currently employed by a scheduled or admitted body and is making contributions from pay to the Pension Scheme. Such a person is sometimes referred to as an “active” member.
Deferred Member	Someone who was once a contributing member and who has chosen to leave his or her accumulated contributions in the Fund to benefit from a pension in due course.
Pensioner/Dependant Member	Someone who is receiving benefits from the Fund either as a former contributor or as a dependent of a former contributor who has deceased.

Employer Bodies

The Fund invests and administers pensions on behalf of 11 current and former employers. These include Scheduled Bodies, brought into the Fund by legislation, and Admitted Bodies, which choose to join the Fund. The detailed listing of employers and their membership numbers is contained in Note 21 of the Statement of Annual Accounts for the Fund (page 20).

Pension Increases

Pensions which are in payment and deferment are increased each April in accordance with the Pension (Increase) Act 1971. Since April 2011, this increase has been linked to the Consumer Price Index (CPI) rather than the Retail Price Index (RPI).

Pensions Administration

Orkney Islands Council as administering authority to the Orkney Islands Council Pension Fund applies the following key service standards in its day to day activities:

	Performance Standard
Pension Estimate Turnaround Time	Within 10 working days
Query Response Time	Within 10 working days
Annual Benefit Statements	Issued by 31 March of the following year

Actuarial Valuation

Annex 2 contains the formal Actuarial Statement for 2013/14 which is prepared in line with the International Accounting Standard (IAS) 26 and supports the preparation of the Financial Statements for the Pension Fund.

Under Local Government Pension Scheme (LGPS) requirements the Fund will undertake its triennial valuation at the 31 March 2014. However this will not be available until the next financial year.

The last triennial valuation, as at the 31 March 2011, revealed that the Fund's assets at 31 March 2011 were valued at £160m, and were sufficient to meet 106.3% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. This compared with 86.3% at the previous March 2008 valuation. The resulting surplus at the 2011 valuation was £9m.

The improvement in the funding position reflected the positive cash flow and good investment performance of the Fund since the previous valuation. Investment returns for the three years to 31 March 2011 were significantly better than anticipated. In addition, the change of linking pension increases from a Retail Price Index (RPI) inflation measure to a Consumer Price Index (CPI) inflation measure has reduced the value of the liabilities significantly, helping improve the funding position. As a result of the valuation process, the Fund's actuary (Hymans Robertson) calculated the contribution rate at 16.5%. However, taking into account recent market conditions, the actuary recommended that the current contribution rate of 21.4% be maintained until 2014/15.

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.

The most recent funding update produced at 31 March 2014 showed that the funding surplus has decreased since the last full valuation. Falling real bond yields were offset by strong asset returns and have resulted in an improvement to last year's funding level of 95% which was estimated at 11 April 2013, to 104% at 31 March 2014.

STATEMENT OF RESPONSIBILITIES FOR THE STATEMENT OF ACCOUNTS

Responsibilities of the Council as Administering Authority

The Council is required to:

- Make arrangements for the proper administration of the financial affairs of the Orkney Islands Council Pension Fund (the Fund) and to secure that one of its officers has the responsibility for the administration of those affairs. In this Council, that officer is the Head of Finance.
- Manage the affairs of the Fund to secure economic, efficient and effective use of resources and safeguard its assets.
- Lay the audited accounts before a meeting of the Council within two months of receipt of the audit certificate.

The Head of Finance's responsibilities

The Head of Finance is responsible for the preparation of the Statement of Accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code on Local Authority Accounting in the United Kingdom (the Code).

In preparing this Statement of Accounts, the Head of Finance has:

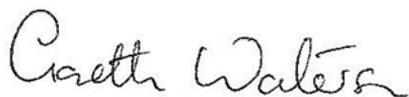
- Selected suitable accounting policies and then applied them consistently
- Made judgements and estimates that were reasonable and prudent
- Complied with the Code of Practice on Local Authority Accounting

The Head of Finance has also:

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

Statement of Accounts

The Statement of Accounts presents a true and fair view of the financial position of the Orkney Islands Council Pension Fund as at 31 March 2014, and of its income and expenditure for the year ended 31 March 2014.



Gareth Waterson, BAcc, CA

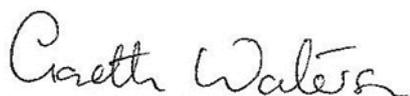
Head of Finance

25 September 2014

STATEMENT ON THE SYSTEM OF INTERNAL FINANCIAL CONTROL

1. This statement is given in respect of the Accounts for Orkney Islands Council Pension Fund. As Statutory Officer for Finance (Section 95 officer) for the Council as Administering Authority, I acknowledge my responsibility for ensuring the proper administration of the financial affairs of the Pension Fund. This includes ensuring appropriate advice is given to the Pension Fund on all financial matters, keeping proper financial records and accounts, and maintaining an effective system of internal financial control.
2. The system of internal financial control operates within a financial strategy and is based on a framework of delegation and accountability for officers and elected members embodied in procedural standing orders, financial regulations, scheme of delegation, scheme of administration, committees and sub-committees, supported by a framework of administrative procedures including the segregation of duties, and regular financial management information. In particular, this includes:
 - Comprehensive accounting systems that record income and expenditure for both member and investment activities,
 - Regular reviews of investment reports that measure investment returns against agreed benchmarks,
 - Regular reviews of investment manager reports that measure performance against agreed targets, and
 - Independent performance reviews of the Fund by the Fund's investment consultant and performance monitoring services provider.
3. The system can provide only reasonable and not absolute assurance that assets are safeguarded, transactions authorised and properly recorded, and that material errors or irregularities are either prevented or would be detected within a timely period.
4. The Pension Fund responds to findings and recommendations of external audit, scrutiny and inspection bodies and its own independent internal audit section. The Monitoring and Audit Committee is integral to overseeing independent and objective assurance and monitoring improvements in internal control and governance.
5. During 2013/14 in response to recommendations in the annual audit plan, budgets were put in place to enable better monitoring of administration performance of the Pension Fund.
6. The Chief Internal Auditor (CIA) reports to the Chief Executive and the Monitoring and Audit Committee and is in regular contact with the Head of Finance and Monitoring Officer. The CIA provides an independent and objective annual assurance statement on the effectiveness of internal control, risk management and governance based on the delivery of an approved plan of systematic and continuous internal audit review of the Council's arrangements. However for the year ended 31 March 2014, Internal Audit did not carry out any specific work on the Pension Fund.
7. My review of the effectiveness of the system of internal financial control is informed by:
 - The work of professional accountancy staff within the Council;
 - The External Auditors' reports.

8. I have undertaken the role of the Statutory Officer for Finance (Section 95 Officer), whose duties include putting in place the arrangements for the proper administration of financial affairs of the Pension Fund. Having reviewed the above, it is my opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's internal financial control systems during the year ended 31 March 2014.
9. However, I have noted that further work on implementing recommendations made by External Audit, with particular emphasis on prompt implementation of high priority recommendations, would further enhance the internal financial control environment to manage financial risks. In addition there is an on-going need for the regular review and compliance testing of Procedural Standing Orders, Financial Regulations and the Scheme of Delegation. Any updates to these governance documents would be subject to formal adoption by the Pension Fund.



Gareth Waterson, BAcc, CA
Head of Finance
25 September 2014

STATEMENT OF ACCOUNTS 2013/14

Fund Account

2012/13 £'000		2013/14 £'000	Notes
	Dealings with members, employers and others directly involved in the scheme		
8,746	Contributions Receivable	8,915	5,13
263	Transfers In	492	6
9,009		9,407	
(5,197)	Benefits Payable	(5,313)	7,13
(251)	Payments to and on account of leavers	(188)	8
(259)	Administration expenses	(348)	15
(5,707)		(5,849)	
3,302	Net Additions/(Withdrawals) from dealings with members	3,558	
	Return on Investments		
4,640	Investment Income	4,784	9
26,639	Profits and losses on disposal of investments and changes in the market value of investments	14,699	10
(207)	Taxes on Income	(213)	
(417)	Investment Management Expenses	(489)	
30,655	Net Return on Investments	18,781	
33,957	Net increase/(decrease) in the Fund during the year	22,339	
170,731	Opening Net Assets of the Scheme	204,688	
204,688	Closing Net Assets of the Scheme	227,027	

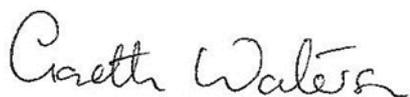
Net Assets Statement

As at 31 March 2014

2012/13 £'000		2013/14 £'000	Notes
153,161	Investment Assets Equities	163,201	
	Managed Funds		
46,205	Pooled Investment Vehicles	61,062	
5,061	Cash Deposits	3,010	
204,427		227,273	11,12
	Current Assets & Liabilities		
760	Cash Balances	693	
64	Contributions due from Employers	62	
(563)	Other Current Liabilities	(1,001)	14
261		(246)	
204,688	Net Assets	227,027	

The Fund Account and Net Assets Statement do not show any liability to pay pensions or other benefits in the future. The liability to pay pensions is detailed in Note 4 Actuarial Present Value of Promised Retirement Benefits.

The unaudited accounts were issued on 26 June 2014 and the audited accounts were authorised for issue on 25 September 2014.



Gareth Waterson, BAcc, CA
Head of Finance
25 September 2014

Notes to the Annual Accounts

1. The Local Government Pension Scheme

The Local Government Pension Scheme is a funded defined benefit, final salary scheme, established under the Superannuation Act 1972, with pensioners receiving index-linked pensions. It is administered by Orkney Islands Council in accordance with The Local Government Pension Scheme (Scotland) Regulations 2008 (as amended) and is contracted out of the State Second Pension. The Pension Fund is subject to a triennial valuation by an independent, qualified Actuary, whose report indicates the required future employer's contributions.

2. Basis of Preparation of the Financial Statements

Local authorities have a duty under section 12 of the Local Government in Scotland Act 2003 to observe proper accounting practices.

The accounts for the Fund have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

3. Statement of Accounting Policies

A summary of the more important accounting policies has been set out below:

3.1 Basis of Preparation

The accounts have been prepared on an accruals basis and do not take account of liabilities to pay pensions and other benefits after the year end. However, the actuarial position does account for such obligations. This is disclosed in Note 4 of the accounts and should be read in conjunction with Note 24 and the Actuarial Statement (Annex 2). The going concern concept assumes that the Pension Fund will continue in existence for the foreseeable future.

3.2 Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the fund during the financial year and are calculated in accordance with the LGPS Regulations.

Individual transfers in/out are accounted for when 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 to purchase scheme benefits are accounted for on a receipts basis and are included in Transfers in.

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

3.3 Financial Instruments

Investments

Investments are included at market values, which are assessed as follows:-

- 3.3.1 UK quoted securities are valued at bid market prices at close of business on the last working day of the financial year.
- 3.3.2 Overseas securities are valued at bid market prices from the relevant overseas stock exchanges converted at closing rates of exchange on the last day of the financial year.
- 3.3.3 Pooled investments, which comprise the fund manager's unit trusts and open ended investment companies, are valued at bid market prices on the last working day of the financial year as supplied by the fund manager.

Since Investments are all held at market value, disclosure in the accounts is at fair value through profit and loss. Fair values are derived from unadjusted quoted prices in active markets.

Debtors and Creditors

The accounts have been prepared on an accruals basis; that is income and expenditure is included as it is earned or incurred, not as it is received or paid, except for transfer values which are included when they are paid or received.

Investment Income

Income from fixed interest, index linked securities and other interest receivable is taken into account on an accruals basis. Income from all other marketable securities is taken into account on the date when stocks are quoted ex-dividend.

Foreign Currency

Income and expenditure arising from transactions denominated in a foreign currency are translated into £ sterling at the exchange rate in operation on the date on which the transaction occurred. Where the transaction is to be settled at a contracted rate, that rate is used.

3.4 Investment Management Expenses

Investment management expenses consist of direct charges in line with management agreements, management charges levied on pooled funds, overseas charges and non-recoverable withholding tax.

3.5 Acquisition Cost

Any acquisition costs of investments are included in the book cost of the investment.

3.6 Critical Judgements in Applying Accounting Policies

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 International Accounting Standard 19. Assumptions underpinning the valuations are agreed with the actuary and are summarised in Note 24. This estimate is subject to significant variances based on changes to the underlying assumptions.

3.7 Assumptions made about the future and other major sources of estimation and uncertainty

The Statement of Accounts contains estimated figures that are based on assumptions made by the Pension 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 balances cannot be determined with certainty, actual results could be materially different from the assumptions and estimate. The items in the Net Assets Statement at 31 March 2014 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:-

Item	Uncertainties
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 sensitivities regarding the principal assumptions used to measure the scheme liabilities are set out below:

Change in assumptions at year ended 31 March 2014:	Approximate % increase to Employer Liability	Approximate monetary amount (£000)
0.5% decrease in Real Discount Rate	11%	24,721
1 year increase in member life expectancy	3%	7,032
0.5% increase in the Salary Increase Rate	3%	8,149
0.5% increase in the Pension Increase Rate	7%	16,068

3.8 Accounting Standards that were issued but not yet adopted

There is a requirement in the Code to disclose the expected impact where a new accounting standard has been issued but not yet adopted. Changes to accounting standards that came into effect on or before 1 January are not expected to have an impact on the Fund. Several new standards come into effect in 2014/15, namely IFRS 13 Fair value measurement, IAS 32 Financial instruments presentation and annual improvements to IFRSs 2009-2011 cycle.

4. Actuarial Present Value of Promised Retirement Benefits

The actuarial value of promised retirement benefits at the accounting date, calculated in line with the International Accounting Standard 19 Employee Benefits (IAS 19) assumptions of Orkney Islands Council, is estimated to be £251m at 31 March 2014 (2013: £222m). This figure is used for statutory accounting purposes by Orkney Islands Council Pension Fund and complies with the requirements of IAS 26 Accounting and Reporting by Retirement Benefit Plans. The assumptions underlying the figure are shown below. The figure is only prepared for the purposes of IAS 26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

Assumptions Applied	2013	2014
Inflation/pension increase rate	2.8%	2.8%
Salary increase rate	5.1%	5.1%
Discount rate	4.5%	4.3%

5. Contributions Receivable

2012/13						2013/14				
Employers		Members		Total		Employers		Members		Total
*	**	*	**			*	**	*	**	
£'000	£'000	£'000	£'000	£'000		£'000	£'000	£'000	£'000	£'000
5,965	727	1,767	228	8,687	Normal	6,106	720	1,788	224	8,838
59	0	0	0	59	Additional	77	0	0	0	77
6,024	727	1,767	228	8,746	Total	6,183	720	1,788	224	8,915

* Administering Body

** Admitted Bodies

6. Transfers In

There were no group transfers in to the scheme during 2013/14 or 2012/13 and the total of £0.5m (2012/13: £0.3m) represents the total of transfer values in respect of individual members joining the scheme.

7. Benefits Payable

2012/13 £'000		2013/14 £'000
(3,783)	Pension Payments	(4,022)
(1,231)	Retirement Lump Sums	(839)
(183)	Death Benefits	(452)
(5,197)		(5,313)

8. Payments to and on Account of Leavers

2012/13 £'000		2013/14 £'000
(16)	Contributions Returned	(21)
(229)	Individual Transfers to other Schemes	(160)
(6)	State Scheme Premiums	(7)
(251)		(188)

9. Investment Income

2012/13 £'000		2013/14 £'000
0	Income from Fixed Interest Securities	795
3,177	Dividends from Equities	3,150
1,364	Income from Pooled Investment Vehicles	568
0	Income from Index Linked Securities	229
24	Interest on Cash Deposits	(8)
75	Recoverable Tax	50
4,640		4,784

10. Change in the Market Value of Investments

2012/13 £'000		2013/14 £'000
(906)	Realised	7,623
27,545	Unrealised	7,076
26,639	Total	14,699

11. Analysis of Investments

As at 31 March 2014 the market value of the assets under management is as follows:

	31 March 2013	31 March 2014
Baillie Gifford	£000	£000
Equities UK	49,270	57,711
Equities Global	103,891	105,490
Pooled Investment Vehicles – British Small Companies	2,096	2,207
Pooled Investment Vehicles – UK Fixed Income	25,031	32,294
Pooled Investment Vehicles – Diversified Growth	19,078	26,561
Cash Balance Held by Managers	5,061	3,010
Totals	204,427	227,273

All the investments are quoted on the Stock Exchange.

12. Reconciliation of Movements in Investments

As at 31 March 2014 assets valued at £227m were quoted on the Stock Exchange (31 March 2013: £204m). During 2013/14, sales of investments totalled £40m and purchases totalled £50m. Transaction costs are included in the cost of purchases and sales proceeds.

The following values of investments exceed 5% of the total value of the net assets of the Pension Fund at 31 March 2014.

	£'000
Baillie Gifford & Company - (Diversified Growth Fund)	26,561

Investment Transactions

2013/14	Opening Market Value	Purchases	Sales	Change in Market Value	Closing Market Value
	£'000	£'000	£'000	£'000	£'000
Investment Assets					
Equities	153,161	31,388	(37,965)	16,617	163,201
Managed Funds					
Pooled Investment – British Small Companies	2,096	240	(623)	494	2,207
Pooled Investment – Fixed Interest	25,031	11,358	(1,718)	(2,377)	32,294
Pooled Investment – Diversified Growth	19,078	7,492	0	(9)	26,561
Cash Deposits	5,061	0	0	(2,051)	3,010
	204,427	50,478	(40,306)	12,674	227,273
Internal Net Current Assets	261				(246)
Total	204,688				227,027

2012/13	Opening Market Value	Purchases	Sales	Change in Market Value	Closing Market Value
	£'000	£'000	£'000	£'000	£'000
Investment Assets					
Equities	125,944	25,837	(21,298)	22,678	153,161
Managed Funds					
Pooled Investment	37,888	4,439	0	3,878	46,205
Cash Deposits	5,327	37	0	(303)	5,061
	169,159	30,313	(21,298)	26,253	204,427
Internal Net Current Assets	1,572				261
Total	170,731				204,688

13. Analysis of Contributions and Benefits

	2012/13		2013/14	
	Benefits Payable	Contributions Receivable	Benefits Payable	Contributions Receivable
	£'000	£'000	£'000	£'000
Orkney Islands Council	4,786	7,791	4,746	7,971
Admitted Bodies	411	955	567	944
Total	5,197	8,746	5,313	8,915

14. Current Liabilities

	31 March 2013	31 March 2014
	£'000	£'000
Orkney Islands Council	359	541
Other Creditors	204	460
Total	563	1,001

15. Administration Expenses

	2012/13 £'000	2013/14 £'000
Audit costs	21	21
Professional costs	25	16
Administration costs	186	283
Bank charges	25	24
Tax	3	4
Total	260	348

16. Audit Remuneration

In 2013/14 the agreed audit fee for the year was £21,000: (2012/13 £21,000).

17. Statement of Investment Principles and Funding Strategy Statement

The Council as Administering Body approved its current Statement of Investment Principles in 2013. The Statement defines the Fund's operational framework insofar as investments are concerned. It is reviewed periodically to ensure that it continues to reflect the needs of the Fund and the views of its stakeholders.

The Funding Strategy Statement defines how the Fund intends to meet its financial obligations and is effective from 31 March 2009.

Both these documents are published on the Council's web site and are available on request from the Council's Head of Finance.

18. Investment Management Arrangements

The Orkney Islands Council Pension Fund investments are managed on an active basis by external fund manager Baillie Gifford.

From the 1 July 2006 the benchmark was revised to the WM Local Authority Average. The target is to outperform the WM Local Authority (excluding Property) Universe by 1% p.a. over rolling five year periods.

The total Fund return for the year was 9.3% which was 3.3% ahead of the benchmark.

Over three years the Fund has generated an annualised return of 10.3% per annum which outperformed the benchmark by 2.7% per annum. Over five years the Fund has generated an annualised return of 16.8% per annum which outperformed the benchmark by 3.7% per annum.

19. Stock Lending

In accordance with the Funding Strategy Statement, stock lending is not permitted within any of its segregated investment mandates. As at 31 March 2014 no stock had been released to a third party under a stock lending arrangement.

20. Related Party Transactions

Orkney Islands Council Pension Fund is administered by Orkney Islands Council. The Council incurred costs of £0.240m (2012/13: £0.180m) in relation to administration of the Fund and was subsequently reimbursed by the Fund for these expenses. The Council is also the single

largest employer of members of the Pension Fund and contributed £6.9m to the fund in 2013/14 (2012/13: £6.8m). All monies owing to and from the Fund were paid in the year.

The Fund had a balance of advances from the Orkney Islands Council loans fund of £0.541m as at 31 March 2014 (£0.360m as at 31 March 2013).

The members of the investment sub-committee are active members of the Pension Fund. Each Councillor is required to declare their interests at each meeting.

The employees who hold key positions in the financial management of the Pension Fund; and their financial relationship with the fund (expressed as cash-equivalent transfer values) are set out below:

	Accrued pension benefits As at 31 March 2014		Accrued pension benefits As at 31 March 2013	
	Pension £	Lump Sum £	Pension £	Lump Sum £
Executive Director of Corporate Services	33,487	79,197	31,750	78,409
Head of Finance / Section 95 Officer	23,034	48,050	21,631	48,050

21. Membership Details

Under the Local Government Pension Scheme (LGPS), member contributions are paid on a tiered basis, the contribution rate being determined by the amount of salary falling into each earnings tier.

Eligibility to join the scheme

Orkney Islands Council employees with a contract for 3 months duration or more are automatically entered into the LGPS. Employees with a contract of less than 3 months duration can opt to join the LGPS. However, employees with a contract of less than 3 months duration will be automatically enrolled onto the LGPS if they satisfy the automatic enrolment criteria.

A person employed by a community admitted body or a person employed by a transferee admitted body may only be a member if the person, or class of employees to which the person belongs, is designated in the admission agreement by the body as being eligible for membership of the Scheme.

If they satisfy the above statement they should be automatically entered into the LGPS if they have a contract for 3 months or more otherwise they can opt in if they have a contract for less than 3 months.

These employees are not necessarily auto-enrolled at present, depending on the staging date of each employer.

The following table gives details of the various bodies' membership.

Membership Details at 31/03/2014	Active	Deferred	Pensioner	Dependant
Orkney Islands Council	1,564	734	562	90
Orkney Islands Property Development	2	6	1	0
Weyland Farms Limited	0	1	1	0
Orkney Towage Company Limited	14	17	17	1
Pickaquoy Centre Trust	33	15	4	0
Orkney Enterprise	5	4	2	0
Orkney Tourist Board	1	5	2	0
Orkney Ferries Limited	66	43	16	1
D & H Glue	0	2	1	0
Orkney & Shetland Valuation Joint Board	0	0	1	1
Golder Landscapes	0	1	0	0
Summary of Members				
OIC	1,564	734	562	90
Other Scheduled Bodies	0	0	1	1
Admitted Bodies	121	94	44	2
Totals	1,685	828	607	93

22. Scheme Arrangements

The new look LGPS came into force from 1 April 2009. It remains a final salary scheme but there are a number of changes to the benefits package including:

- A change in the accrual rate from 1/80th pension plus 3/80th lump sum to an improved accrual rate of 1/60th for membership from 1 April 2009
- Choice of improved lump sum at retirement
- Introduction of dependent partner's pension
- Increased death in service cover
- Increased flexible retirement options
- Tiered contributions

23. Financial Instruments

Categories of Financial Instruments

The following categories of financial instrument are carried in the Net Assets Statement:

Financial Instruments Balances	31 March 2013	31 March 2014
	£'000	£'000
Investments		
Financial Assets at fair value through profit and loss	199,366	224,263
Loans and receivables	5,061	3,010
Total investments	204,427	227,273
Current assets and liabilities		
Loans and receivables	824	755
Financial liabilities at amortised cost	(563)	(1,001)
Total current assets and liabilities	261	(246)

Income, Expenses, Gains and Losses

Financial Instruments Gains/Losses	2012/13	2013/14
	Financial Assets	
	£'000	£'000
Net gains/losses on financial assets at fair value through profit and loss	26,639	14,699
Investment Income	4,640	4,784
Investment management expenses including taxation	(624)	(702)
Total investment gains and losses	30,655	18,781

Fair Values of Assets and Liabilities

Financial assets represented by investments are carried in the Net Assets Statement at their current market value (bid price), as determined by the investment managers and the global custodian, based upon publicly quoted prices. This provides a close approximation to fair value.

Risk and Risk Management

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

Responsibility for managing the Fund's risk rests with the Investments Sub-Committee.

23.1 Market risk

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

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

Sensitivity analysis

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

Asset Type	Potential Market Movement +/- (%p.a.)
UK Equities	13.86
Global Equities	12.16
Bonds & Index Linked	7.14
Cash	0.02
Diversified Growth	4.70

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

			Potential change in year in the net assets available to pay benefits	
Asset Type	Value	% Change	Favourable Market Movement	Unfavourable Market Movement
	£'000		£'000	£'000
UK Equities	57,711	13.86%	65,710	49,712
Global Equities	105,490	12.16%	118,318	92,663
Bonds & index Linked	34,501	7.14%	36,965	32,038
Cash	3,010	0.02%	3,011	3,009
Diversified Growth*	26,561	4.70%	27,809	25,313
Total Assets	227,273		251,813	202,735

* Diversified Growth % change figure is 3 year volatility figure from Baillie Gifford.

23.1.1 Interest rate risk

The Fund invests in financial assets for the primary purpose of obtaining a return on investments. These investments are subject to interest rate risks, which represent the risk

that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

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

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

	At 31 March 2013	At 31 March 2014
	£'000	£'000
Cash and cash equivalents	5,061	3,010

Interest rate risk sensitivity analysis

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

The analysis that follows assumes that all other variables, in particular exchange rates, remain constant, and shows the effect in the year on the net assets available to pay benefits of a 1% change in interest rates:

Asset Type	Carrying amount as at 31 March 2014	Potential change in year in the net assets available to pay benefits	
		+1%	-1%
	£'000	£'000	£'000
Cash and Cash Equivalents	3,010	30	(30)
Total change in assets available	3,010	30	(30)

23.1.2 Currency risk

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Fund (£UK). The Fund is invested in equities overseas that are denominated in currencies other than £UK. The Fund also holds a low level of bonds denominated in overseas currencies.

The following table summarises the Fund's currency exposure at 31 March 2014:

Currency exposure - asset type	Asset value at 31 March 2014	
	£'000	
Overseas Quoted Equities	102,421	
Pooled Funds - Global Basket	3,069	
Total	105,490	

Currency risk – sensitivity analysis

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

Currency	Value £'000	Change %	Value on Increase £'000	Value on Decrease £'000
Australian Dollar	1,190	9.80%	1,307	1,074
Brazilian Real	767	12.69%	865	670
Danish Krone	1,921	6.26%	2,041	1,801
EURO	5,407	6.31%	5,748	5,066
Hong Kong Dollar	2,873	7.98%	3,102	2,644
Indonesian Rupiah	389	11.05%	431	346
Japanese Yen	7,044	11.54%	7,857	6,231
Norwegian Krone	1,292	8.79%	1,406	1,179
South African Rand	3,293	11.31%	3,665	2,920
Swedish Krona	5,809	7.03%	6,218	5,401
Swiss Franc	7,266	7.42%	7,805	6,726
US Dollar	65,170	8.07%	70,429	59,910
Pooled Investments - Global Basket	3,069	5.21%	3,229	2,909
Total	105,490		114,103	96,877

23.2 Credit risk

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

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

The Fund believes it has managed its exposure to credit risk, and the Fund has had no experience of default or uncollectable deposits over the past five financial years. The Fund's cash holding under its treasury management arrangements at 31 March 2014, including current account cash, was £0.7m. (31 March 2013: £0.8m). This was held with the following institutions:

	Rating	Balance at 31 March 2014 £'000
Bank current accounts		
Royal Bank of Scotland	A	693

23.3 Liquidity Risk

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

The Council has immediate access to its Pension Fund cash holdings

The Fund defines liquid assets as assets that can be converted to cash within three months. Illiquid assets are those assets which will take longer than three months to convert into cash. As at 31 March 2014, the Fund had no illiquid assets.

24. Funding and Valuation Note

In line with the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008, the Fund's actuary undertakes a funding valuation every three years. The actuarial valuation assesses the health of the fund and provides a check that the funding strategy and assumptions used are appropriate. It also sets the future rates of contributions payable by employers. The most recent full actuarial valuation by the Fund's actuaries Hymans Robertson was to 31 March 2011. The next valuation will take place as at 31 March 2014.

The key elements of the funding policy are:

- To ensure the long-term solvency of the Fund, i.e. that sufficient funds are available to meet all pension liabilities as they fall due for payment
- To ensure that employer contribution rates are as stable as possible
- To minimise the long-term cost of the scheme by recognising the link between assets and liabilities and adopting an investment strategy that balances risk and return
- To reflect the different characteristics of employing bodies in determining contribution rates where the administering authority considers it reasonable to do so
- To use reasonable measures to reduce the risk to other employers and ultimately to the council tax payer from an employer defaulting on its pension obligations

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 over a period of time. Solvency is achieved when the funds held, plus future expected investment returns and contributions are sufficient to meet expected future pension benefits payable.

At the 2011 actuarial valuation, the Fund was assessed as 106.3% funded (86.3% at the March 2008 valuation). This corresponded to a surplus of £9m (2008 valuation: deficit of £18m) at that time.

The assessed common contribution rate (i.e. the rate which employers in the Fund pay) was 16.5%.

Owing to volatility in the financial markets in the year following the actuarial review, it was decided to hold the pooled contribution rate at its previous level of 21.4%.

In accordance with the Funding Strategy Statement the administering authority has adopted employer contributions from 2012/13 to 2014/15 of 21.4%. The valuation of the Fund has been undertaken using the projected unit method under which the salary increase for each member is assumed to increase until they leave active service by death, retirement or withdrawal from service. The principal assumptions were:

Financial Assumptions

Financial Assumptions	31 March 2008	31 March 2011	
	Funding basis (% p.a.)	Funding basis (% p.a.)	Gilts basis (% p.a.)
Discount rate	6.1%	5.9%	4.3%
Price inflation	5.1%	5.1%	5.1%
Pay increases	3.6%	2.8%	2.8%
Pension increases:			
in excess of GMP	3.6%	2.8%	2.8%
post-88 GMP	2.8%	2.8%	2.8%
pre-88 GMP	0.0%	0.0%	0.0%
Revaluation of deferred pension	3.6%	2.8%	2.8%
Expenses	0.6%	0.8%	0.8%

* GMP = guaranteed minimum pension

Mortality assumptions

The mortality assumptions used and applied to all members are based on the Self-Administered Pension Schemes year of birth tables with improvements from 2008 in line with the Medium Cohort and a 1% p.a. underpin.

25. Post Balance Sheet Events

There were no adjusting post balance sheet events.

26. Additional Voluntary Contributions

Under Inland Revenue rules, scheme members are permitted to make contributions towards retirement and death in service benefits in addition to those which they are required to make as members of the Local Government Pension Scheme. These contributions are known as Additional Voluntary Contributions and are treated separately from the scheme's assets under arrangement with Prudential Assurance Company Limited.

During the year, member contributions amounted to £0.322m (2012/13: £0.357m).

Members contributions are invested in a "with profits" Fund or a "deposit" Fund. During the year the value of AVC investments increased by £0.147m to £2.119m as at 31 March 2014 (2013: £1.972m) excluding the final bonus.

GOVERNANCE ARRANGEMENTS

Orkney Islands Council Pension Fund

Introduction

This Statement outlines the governance arrangements in place for administering the pension scheme administered by Orkney Islands Council.

1. Administering Authority

- 1.1 Orkney Islands Council (the Council) is the Administering Authority for the Local Government Pension Scheme (LGPS) set up for the Orkney Islands Council geographic area.
- 1.2 The Council has delegated the management of the investment of the Pension Fund to the Investments Sub-Committee.

2. Regulatory Framework

- 2.1 The Scottish Public Pensions Agency (SPPA) is responsible for regulating the LGPS in Scotland and the Council administers the pension scheme in accordance with these regulations.
- 2.2 The Orkney Islands Council scheme is open to all employees of scheduled bodies except for those whose employment entitles them to belong to another statutory pension scheme (e.g. Teachers). Employees of admitted bodies can join the scheme subject to those bodies meeting the statutory requirements and on such terms and conditions as the Council (as Administering Authority) may require. A list of scheduled and admitted bodies is attached in Annex 1.
- 2.3 The Investments Sub-Committee (the Sub-Committee) is a formal sub-committee of Orkney Islands Council's Policy and Resources Committee. The Scheme of Administration for the Council refers to the Investments Sub Committee all matters relating to the management of investments of the Council's Pension Fund.
- 2.4 Financial affairs are conducted in compliance with the Council's Financial Regulations which were formally adopted by the Pension Fund in 2011.
- 2.5 Funds are invested in compliance with the Council's Statement of Investment Principles.

3. Investments Sub-Committee

- 3.1 The members of the Sub-Committee act as quasi-trustees and oversee the management of the Orkney Islands Council Pension Fund (the Fund).
- 3.2 Their overriding duty is to ensure the best possible outcomes for the Fund, its participating employers and scheme members.
- 3.3 The members' knowledge is supplemented by professional advice from Officers of the Council, professional advisers and external experts.
- 3.4 The Sub-Committee is comprised of seven members of the Council:

Convenor (Chair of Policy & Resources Committee)

Vice Convenor (Vice Chair of Policy & Resources Committee)

Five other elected members of the Council

- 3.5 The Independent Investment Consultant, the Director of Corporate Services, Head of Finance, and Corporate Finance Service Manager also attend the Sub-Committee meetings as advisers.
- 3.6 The Sub-Committee meets at least quarterly. Additional meetings are called as appropriate.
- 3.7 The Sub-Committee papers and minutes are publicly available on the Council's website, unless they have been considered as private business in terms of Schedule 7A to the Local Government (Scotland) Act 1973. Minutes of the Sub-Committee are presented to the Policy and Resources Committee of the Council.

4. Administration and Management of the Fund

4.1 Head of Finance

4.1.1 The Council's Head of Finance is the Officer with responsibility to ensure proper administration of the Council's financial affairs in terms of Section 95 of the Local Government (Scotland) Act 1973.

4.1.2 He is responsible for:

- the financial accounting of the Fund,
- the preparation of the Pension Fund Annual Report, and
- being the principal advisor on investment management to the Council in its capacity as Trustee to the Fund and as the Fund's Administering Authority.

4.2 The day-to-day management of the investment activities of the Fund is managed by the Corporate Finance Section within Corporate Services.

4.3 The pension benefits policy oversight and day-to-day administration for the Fund is managed by the Pensions Section within Corporate Services.

5. Professional Advisers and External Service Providers

5.1 Hymans Robertson has been appointed to act as Actuary to the Fund. The services provided include advice on funding and actuarial valuations.

5.2 Hymans Robertson is the Independent Investment Consultant employed by the Council to advise the Sub-Committee on investment strategy.

5.3 The Fund has appointed investment managers who have responsibility for the selection, retention and realisation of individual investments. Where appropriate, they also implement the Sub-Committee's policy in relation to corporate socially responsible investment and corporate governance.

5.4 Bank of New York Mellon is the global custodian for the Fund and is responsible for the safekeeping of the assets including transaction processing and making tax claims.

5.5 WM Performance Services provides independent performance services for the Fund. They have responsibility for measuring and reporting on the performance of individual portfolios and the overall Fund.

6. Internal and External Review

- 6.1 The annual financial statement of the Fund is subject to external audit. The auditors are appointed by Audit Scotland, as part of the process to ensure that public funds are properly safeguarded and accounted for.
- 6.2 The Council provides internal audit arrangements to the Fund both as a tool of management and with direct reporting to the Council's Monitoring and Audit Committee.

7. Risk Management

- 7.1 The Council has a corporate risk management policy which includes the maintenance and regular review of a risk register. The Fund does not maintain its own risk register; however no specific risks facing the pension fund have been identified at the Council level.
- 7.2 Risk awareness is embedded into the investment performance management process.

8. Access to Information

- 8.1 Sub-Committee papers and minutes are available via the Council website www.orkney.gov.uk.
- 8.2 The Fund's Annual Report and Accounts is available via the Council's website www.orkney.gov.uk.

9. Compliance with Best Practice

- 9.1 The Local Government Pension Scheme (Administration) (Scotland) Regulations 2008 require Administering Authorities to measure their governance arrangements set out against standards set by Scottish Ministers. These standards are established via a number of best practice principles. The Governance Compliance Statement details the Fund's status against these standards.

GOVERNANCE COMPLIANCE STATEMENT

The Regulations that govern the management of LGPS funds in Scotland require that a Governance Compliance Statement is published. The following compliance statement sets out the extent to what governance arrangements comply with best practice.

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 Orkney Islands Council as administering authority has delegated all pension scheme matters to the Policy and Resources Committee (PRC) and the Investments Sub Committee (ISC) which comprises of 7 elected members.
	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.	No	<p>On 15 April 2014, the PRC agreed to establish a LGPS Pension Fund Forum (PFF) which once operational will report to the ISC.</p> <p>There are however no admitted bodies or deferred members represented on the PRC or ISC at present.</p> <p>The existing membership of the ISC includes both active and pensioner members of the Orkney Island Council Pension Fund.</p>
	That where a secondary committee of panel has been established, the structure ensures effective communication across both levels.	Partial	The agreed terms of reference for operation of the PFF includes the requirement to produce a formal minute of all Forum meetings and which will then act to inform the decision making process for meetings of the ISC.
	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.	N/A	Membership of the PFF will include all 7 elected members of the ISC.
Representation	a) 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 	Partial	<p>Members of the PRC and ISC are selected from the membership of the Council.</p> <p>In accordance with the terms of reference for the operation of the PFF, membership will comprise 7 elected members, 1 trade union representative, 1 member</p>

Principle		Full Compliance	Comments
	<p>bodies;</p> <ul style="list-style-type: none"> • Scheme members including deferred and pensioner scheme members • Where appropriate, independent professional observers, and • Expert advisors (on an ad-hoc basis). 		<p>nominated by admitted bodies, 1 pensioner or deferred member and 1 active member of the scheme.</p> <p>Input from Hymans Robertson as expert advisors to the Pension Fund is routinely sought on policy matters.</p>
	b) 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.	N/A	In accordance with the terms of reference, all members of the PFF will be treated equally.
Selection and Role of Lay Members	a) 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.	No	<p>The current arrangements whereby training is provided to members of the ISC on an ad-hoc basis, or where a specific needs has been identified, is under review.</p> <p>The CIPFA framework will be used to identify gaps in knowledge.</p> <p>Training for ISC members includes presentations from investment managers, actuary and investment advisors.</p> <p>Attendance at meetings and training is monitored and reported as appropriate.</p>
	b) 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 the ISC, MAC, PRC and HRC.
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	Full voting rights are given to all members of the PRC.
Training/	a) That in relation to the way	Yes	Members' training is funded from

Principle		Full Compliance	Comments
Facility Time/ Expenses	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.		the Council's Pension Fund.
	b) 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.
	c) That the administering authority considers the adoption of annual training plans for committee members and maintains a log of all such training.	No	Annual training plans will be developed in the future. A log is maintained of all training provided to members and this is monitored and reported as appropriate.
Meeting Frequency	a) That an administering authority's main committee or committees meet at least quarterly	Yes	The PRC and ISC are scheduled to meet four times a year.
	b) 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.	Partial	The proposed PFF will meet a minimum of 2 times per annum.
	c) That an administering authority that does not include lay members in their formal governance arrangements must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	Partial	On 15 April 2014, the PRC agreed to establish a LGPS Pension Fund Form (PFF) which once operational will report to the ISC.
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 are treated equally.

Principle		Full Compliance	Comments
Scope	That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Yes	The PRC and ISC deal with all matters relating to both the administration and investment of the Pension Fund.
Publicity	That administering authorities have published details of their governance arrangements in such a way that stakeholders, can express an interest in wanting to be part of those arrangements.	Yes	The Orkney Islands Council Pension Fund governance documents are available upon request. The Council as administering authority communicates regularly with employers and scheme members.

INDEPENDENT AUDITOR'S REPORT

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

I certify that I have audited the financial statements of Orkney Islands 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 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 Head of Finance and auditor

As explained more fully in the Statement of Responsibilities for the Statement of Accounts, the Head 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 Head 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 fund during the 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 matter

In my opinion the information given in the Foreword by Head of Finance, the Operating and Financial Review and the Governance Arrangements 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 (Audit Services)
Audit Scotland
4th Floor, South Suite
The Athenaeum Building
8 Nelson Mandela Place
Glasgow
G2 1BT

25 September 2014

ANNEX 1 - Scheduled and Admitted Bodies

Orkney Islands Council Pension Fund

Scheduled Bodies

- Orkney Islands Council
- Assessors

Admitted Bodies

Active Admitted Bodies

- Orkney Tourist Board (Visit Scotland)
- Orkney Towage Company Limited
- Orkney Ferries Limited
- Orkney Enterprise
- Pickaquoy Centre Trust
- Orkney Islands Property Development Limited

Admitted bodies with Deferred or Retired Members only

- D & H Glue
- Weyland Farms Limited
- Golder Landscapes

ANNEX 2 – Actuarial Statement for 2013/14

Orkney Islands Council Pension Fund (the Fund)

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 Orkney Islands Council's Funding Strategy Statement (FSS). In summary, the key funding principles are as follows:

- to ensure the long-term solvency of the Fund as a whole and of the share of the Fund attributable to each individual employer;
- to ensure that sufficient funds are available to meet all benefits as they fall due for payment;
- not to restrain unnecessarily the investment strategy of the Fund, so that the Administering Authority can seek to maximise investment returns (and hence minimise the cost of the benefits) for an appropriate level of risk;
- to help employers recognise and manage pension liabilities as they accrue;
- to minimise the degree of short-term change in the level of each employer's contributions where the Administering Authority considers it reasonable to do so;
- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations; and
- to maintain the affordability of the Fund to employers as far as is reasonable over the longer term.

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 as at 31 March 2011. This valuation revealed that the Fund's assets, which at 31 March 2011 were valued at £160 million, were sufficient to meet 106% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting surplus at the 2011 valuation was £9 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 my valuation report dated 30 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 value.

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

Financial assumptions	31 March 2011	
	% p.a. Nominal	% p.a. Real
Discount rate	5.9%	3.1%
Pay increases *	5.1%	2.3%
Price inflation/Pension increases	2.8%	-

* plus an allowance for promotional pay increases. Short term pay growth was assumed to be 1% p.a. for 2011/12 and 2012/13, reverting to 5.1% p.a. thereafter.

The key demographic assumption was the allowance made for longevity. As discussed in the accompanying report, life expectancy is based on the SAPS year of birth tables with improvements from 2008 in line with the Medium Cohort and a 1% p.a. underpin. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	23.0 years	25.8 years
Future Pensioners	24.9 years	27.7 years

Copies of the 2011 valuation report and Funding Strategy Statement are available on request from Orkney Islands Council, administering authority to the Fund.

Experience over the period since April 2011

The Administering Authority monitors the funding position on a regular basis as part of its risk management programme. An estimate of the funding position as at 31 March 2014 shows that the funding level (excluding the effect of any membership movements) has worsened since the 2011 valuation due to falling real bond yields.

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



Barry McKay

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

ANNEX 3 - Glossary of Terms

ACTIVE MANAGEMENT

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

ASSET ALLOCATION

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

BALANCED MANAGEMENT

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

GROWTH MANAGER

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

MANDATE

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

PASSIVE MANAGEMENT

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

POOLED FUND

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

RETURN

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

RISK

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

SEGREGATED FUND

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

SPECIALIST MANAGEMENT

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

VALUE MANAGER

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

VESTED/NON VESTED OBLIGATIONS

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

PENSION FUND STRAIN

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

OPERATING SURPLUS/DEFICIT

The surplus/deficit arising from dealing with members, employers and others directly involved in the scheme.

ADDITIONAL INFORMATION

Key Documents Online

You can find further information on our website www.orkney.gov.uk/Council/P/pension-fund-annual-reports.htm, including the following documents:

- Annual Report and Accounts

Fund Advisers

Actuaries:	Hymans Robertson
Auditors:	Audit Scotland
Bankers:	Royal Bank of Scotland
Investment Advisors:	Hymans Robertson
Investment Custodians:	Bank of New York Mellon
Investment Managers:	Baillie Gifford & Co
Performance Measurement:	WM Company
Additional Voluntary Contributions (AVC) Managers:	Prudential

Contact Details

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

Bryan Hay	Telephone 01856 873535	Ext 2108
Pensions Manager	E-mail bryan.hay@orkney.gov.uk	

Scheme members should have a copy of the "Employees' Guide to the Local Government Pension Scheme Administered by the Orkney Islands Council", and can obtain their own copy of an Annual Report on request.

or visit Orkney Islands Council Pension Fund website at: www.orkney.gov.uk.

For further information on the Fund's Investments, please contact:

Gareth Waterson	Telephone 01856 873535	Ext 2103
Head of Finance	E-mail gareth.watson@orkney.gov.uk	
Colin Kemp	Telephone 01856 873535	Ext 2106
Corporate Finance Senior Manager	E-mail colin.kemp@orkney.gov.uk	