

LONDON BOROUGH OF HAMMERSMITH & FULHAM PENSION FUND STATEMENT OF INVESTMENT PRINCIPLES – MARCH 2010

1. BACKGROUND

1.1. Legal

Regulation 12(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 requires administering authorities, after consultation with such persons as they consider appropriate, to prepare, maintain and publish a written statement of the principles governing their decisions about the investment of fund money. The purpose of this document is to satisfy the requirements of the regulations.

1.2. Scheme

The Local Government Pension Scheme (“the Scheme”) was established in accordance with statute to provide death and retirement benefits for all eligible employees. The Scheme is a contributory, defined benefit occupational pension scheme. It is funded by employee contributions and by variable employer contributions, which are set every three years, following an actuarial valuation of the assets and liabilities of the scheme.

The benefits of the Scheme are defined by statute and they are inflation proofed in line with annual increases in the Retail Price Index for September. The Scheme is operated by designated administering authorities, of which the London Borough of Hammersmith and Fulham is one such authority. Each administering authority maintains a Pension Fund (“the Fund”) and invests monies not required immediately to meet benefits.

1.3. Pensions Fund Investment Panel

The Council has delegated the investment arrangements of the scheme to the Pensions Fund Investment Panel (“The Panel”) who decide on the investment policy most suitable to meet the liabilities of the Scheme.

The Panel is made up of elected members of the Council who each have voting rights and invites representatives from the admitted and scheduled bodies within the Fund and from trade unions, as observers. The Panel reports to the full Council.

1.4. Advice

The Panel obtains and considers advice from the Director of Finance and Corporate Services, and as necessary from the Fund’s appointed actuary, investment managers and advisors.

1.5. Investment Management

The Panel has delegated the management of the Fund’s investments to professional investment managers, appointed in accordance with the Scheme’s regulations, whose activities are specified in detailed investment management agreements and regularly monitored.

2. INVESTMENT RESPONSIBILITIES

2.1. The Pensions Fund Investment Panel is responsible for:

- Determining overall investment strategy and ensuring that investments are sufficiently diversified, are not over concentrated in any one type of investment, and that the Fund is invested in suitable types of investments, as required by relevant regulations,
- Appointing the investment manager(s), custodian, actuary and any independent external advisors felt to be necessary for the good stewardship of the Fund,
- Monitoring the performance of the investment managers, custodians, actuary and external advisors to ensure that they remain suitable.
- Preparing, publishing and maintaining the Statement of Investment Principles, and reviewing its contents,
- Preparing, publishing and reviewing the Funding Strategy Statement, the Governance Compliance Statement and the Communications Policy and Practice Statement,
- Receiving actuarial valuations of the Fund regarding the level of employers' contributions necessary to balance the Fund.
- Reviewing policy on corporate and social responsibility and on the exercise of rights, including voting rights,
- Approving the final accounts and balance sheet of the Fund.
- Approving the Business Plan of the Fund.

2.2. The Investment Managers are responsible for:

- The investment of the Pension Fund assets in compliance with prevailing legislation and the detailed Investment Management Agreements,
- Tactical asset allocation and security selection around the strategic benchmark set by the Panel,
- Preparation of quarterly reports including a review of investment performance,
- Attending meetings of the Panel as required,
- Voting shares in accordance with the Council's policy except where the Council has made other arrangements.

2.3. The Custodian (*Northern Trust.*) is responsible for:

- Its own compliance with prevailing legislation,
- Providing valuations and accounting data summarizing details of all investment transactions within the fund,

- Safe custody and settlement of all investment transactions, collection of income, tax reclaims, and the administration of corporate actions.
- Providing a performance measurement service of the investment managers against their specific benchmarks
- Voting the Fund's shares in accordance with the investment manager's instructions.

2.4. The External Advisor (*P-Solve Asset Solutions.*) is responsible for:

- Advising and assisting the Director of Finance and Corporate Services and the Panel on the investment objective and investment strategy of the Fund and its implementation,
- Assisting the Director of Finance and Corporate Services and the Panel in their regular monitoring of the investment managers' performance,
- Assisting the Director of Finance and Corporate Services and the Panel in the selection and appointment of investment managers and custodians,
- Advising and assisting the Director of Finance and Corporate Services and the Panel on other investment related issues, which may arise from time to time,
- Providing continuing education and training to the Panel and Officers.

2.5. The Actuary (*Barnett Waddingham*) is responsible for:

- Undertaking a triennial valuation of the Fund's assets and liabilities and interim valuations as required,
- Providing advice as to the maturity of the Fund and its funding level in order to aid the Panel in balancing the short term and long term objectives of the Fund,
- Providing advice on the admission of new bodies to the Fund.

2.6. The Director of Finance and Corporate Services is responsible for:

- Day to day administration of the Fund
- Monitoring compliance with statutory requirements and the investment principles set out in this document.
- Ensuring that this document is regularly reviewed and updated in accordance with the Regulations.
- Ensuring proper resources are available to meet the Council's responsibilities.

3. PENSION FUND LIABILITIES

3.1 Overview

The Hammersmith and Fulham Pension Fund is broadly similar to other funds of comparable size in terms of its maturity. The actuary determined that the funding level was 70% at the 31st March 2007 valuation. The Panel has agreed with the actuary for the Council to make additional employer contributions over a period of 25 years to bring the funding level back to 100%.

The Fund's liabilities are sensitive to inflation via pension and pay increases, to interest rates and to mortality rates. The assets that would most closely match the liabilities are a combination of index-linked gilts and fixed interest gilts.

However, the Fund's assets are invested in a broad range of asset classes which are expected to produce returns above the investment objective of the Fund over the long term albeit with greater volatility.

Following the revised liability information from the 31st March 2007 actuarial valuation, the overall investment objective of the Fund was reviewed. Defining an investment objective that is directly related to the Fund's liabilities is crucial in allowing the Panel to recognise the risks inherent in the Fund's liabilities and in monitoring the performance of the investment managers and overall strategy relative to this target.

The overall investment objective, the Liability Benchmark Portfolio ("LBP") was defined as the return on a portfolio of index-linked gilts with an average duration of 18 years in line with the Fund's liabilities and was updated as follows:

Asset	Allocation	Duration (years)
2½% Index-linked Treasury Stock 2024	27%	13.5
1¼% Index-linked Treasury Gilt 2027	63%	17.2
1¼% Index-linked Treasury Gilt 2055	10%	37.4
Total	100%	18.2

To meet the funding plan for the Fund and to bring the funding level back to 100%, an investment return of at least LBP + 1.75% p.a. is required over the next 25 years, the recovery period, in addition to the employers' and employees' contributions. It is expected that the current overall investment strategy (see paragraph 4.2) for the Fund will generate a return of around 2.3% p.a. over the LBP in order to provide a buffer against future adverse experience.

3.2 Scheme Benefits.

The Scheme is a defined benefit scheme. Each member's pension is specified in terms of a formula based on salary and service and is unaffected by the investment return achieved on the Fund's assets.

Full details of Scheme benefits are set out in the regulations. The Council has also published a guide for members of staff who are eligible to join the Scheme.

3.3 Funding the Benefits

As defined in the Scheme regulations, all active members of the Scheme are required to contribute a percentage of their pensionable pay to the Fund on a sliding scale based upon their level of earnings.

The Council and other employers in the Fund are responsible for meeting the balance of costs necessary to finance the benefits payable from the Fund. Employer's contribution rates are determined triennially based on the advice of the Fund's actuary and are subject to inter-valuation monitoring.

3.4 Actuarial Valuation

The Fund is valued by the actuary every three years in accordance with the Local Government Pension Scheme Regulations and monitored each year by the Director of Finance and Corporate Services.

The next valuation will be based on the value and position of the Fund as at 31st March 2010 and any changes in the contribution rate payable by the Council due to that valuation will take place from 1st April 2011.

4. INVESTMENT STRATEGY

4.1 Aims and Purpose of the Fund

The aims of the Fund are to:

- Enable employer contribution rates to be kept as nearly constant as possible and at reasonable cost to the taxpayers and admitted bodies,
- Manage employers' liabilities effectively,
- Ensure that sufficient resources are available to meet all liabilities as they fall due,
- Maximise the returns from investments within reasonable risk parameters.

The purpose of the Fund is to:

- Receive monies in respect of contributions, transfer values and investment income, and
- Pay out monies in respect of scheme benefits, transfer values, costs, charges and expenses, as defined in the Local Government Pension Scheme Regulations

4.2 Investment Management Strategy

The Panel, after advice from P-Solve, the Fund's advisor, has agreed an investment strategy consisting of having four portfolios, UK Equity, Global (ex UK) Equity, Dynamic Asset Allocation and a Matching Fund (to match some of the Fund's liabilities). Each portfolio represents 25% of the total Fund. The investment strategy

is designed to give diversification and specialisation and achieve optimum return against acceptable risk.

Within the four portfolios the Panel has appointed external investment managers with clear strategic benchmarks which place maximum accountability for performance against that benchmark on the investment manager.

The UK Equity portfolio is managed by Majedie Asset Management, the Global (ex UK) portfolio by MFS International (UK) Ltd, the Dynamic Asset Allocation portfolio is split 75% to Baring Asset Management Ltd and 25% to Ruffer LLP and the Matching Fund is split equally between Goldman Sachs Asset Management and Legal and General Investment Management.

In addition, £15 million is committed to private equity, through an investment of £7.5million with each of two fund of funds managers, Unigestion and Invesco.

4.3 Strategic Benchmarks and Performance Targets

Each investment manager has been set a strategic benchmark in order to achieve the overall investment objective for the Fund. The current benchmarks and performance targets for each investment manager are set out below:

- UK Equity - Majedie Asset Management to produce a return of 2% after fees above the FTSE All Share index returns over rolling three-year periods.
- Global (ex UK) Equity - MFS International (UK) Ltd to produce a return of 2% after fees above the FTSE World (ex UK) index returns over rolling three-year periods.
- Dynamic Asset Allocation – Baring Asset Management Ltd and Ruffer LLP to produce an absolute return of 4% in excess of cash based on the 3 month sterling LIBOR over rolling three-year periods.
- Matching Fund - Goldman Sachs Asset Management to produce an absolute return of 2% in excess of cash based on the 3 month sterling LIBOR over rolling three-year periods and Legal and General Investment Management to produce a return of two times the FTSE over 15 years Gilts index minus 3 month sterling LIBOR over rolling three-year periods.

Investment management performance is reviewed quarterly and annually upon receipt of independent data from Northern Trust, the Fund's custodian.

4.4 Reporting

The investment managers' performance is reported quarterly to the Panel. The Panel publishes this Statement of Investment Principles, a Funding Strategy Statement, a Governance Compliance Statement, a Communications Policy and Practice Statement and minutes of their meetings.

4.5 Review

Investment strategy and performance is reviewed regularly.

5. INVESTMENTS

The powers and duties of the council to invest monies are set out in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. The council is required to invest any monies which are not required immediately to pay pensions and any other benefits and, in so doing, take account of the advisability of investing fund money in a wide variety of investments and the suitability of particular investments and types of investments. In doing so the council must obtain and consider the advice of persons properly qualified on investment matters.

5.1 Types of Investment

Investment can be made in accordance with the regulations in a broad spectrum of investments such as equities, fixed interest and other bonds, private equity fund of funds and property, both in the UK and overseas.

The regulations also specify other investment instruments that may be used such as bank deposits, stock lending, financial futures, hedge funds, traded options, insurance contracts, sub underwriting contracts and a contribution to a limited partnership in an unquoted securities investment partnership. The limits on the amount of monies that can be invested in each individual type of investment are specified in schedule 1 of the Regulations.

5.2 Investment Management

The Panel has appointed external investment managers under the terms of the Regulations whose roles are described in the Investment Strategy above. The managers are paid fees (some with a performance related element) based on percentage rates applied to the market value of the assets under management.

The Panel has appointed P-Solve Asset Solutions as the Fund's advisor. They are paid fees based on an agreed schedule of work. A fee is agreed with the advisor in advance for any additional work over and above the agreed schedule.

The Panel has appointed Northern Trust as global custodian. They are paid fees based on the market value of the funds under management and the number of transactions made by the investment managers.

5.3 Investment Risk

The investment strategy has been set with the objective of controlling the risk that the assets will not be sufficient to meet the liabilities of the Fund while achieving a good return on investment. The Panel has adopted in its investment strategy an approach to investment that involves the full range of permitted asset classes.

The return from the investment strategy is measured each quarter and over longer time periods against the investment objective of "Liability Benchmark Portfolio +1.75%" (see paragraph 3.1 above).

Risk is further controlled by having a number of investment managers. Strategic benchmarks have been set for each manager and performance is monitored relative

to the benchmarks. This is to ensure the investment manager does not deviate from the Panel's investment strategy.

5.4 Realisation of Investments

Investments will be realised at the discretion of the investment managers. The Fund has a positive cash flow and there is no current requirement to realise investments to meet pensions and other benefits.

The vast majority of the Fund's investments are readily marketable and may be easily realised if required. Some investments, such as private equity and limited partnership schemes are less easy to realise in a timely manner but the total value of these types of investments is not considered to have any adverse consequences for the Fund.

5.5 Stock Lending

The council does not engage in the lending of stocks or other securities from its pension fund.

6. CORPORATE SOCIAL RESPONSIBILITY

This statement is an outline of the Fund's approach to shareholder engagement. It provides the basis for the broad policies which the Fund believes constitute best practice and provides the framework within which it will enter into engagement with companies in which it invests.

The Fund recognises that the neglect of corporate governance and corporate social responsibility (CSR) may lead to poor or reduced shareholder returns.

The Panel has considered how the Fund may best implement a corporate social responsibility policy, given the current resources available to the Fund. Accordingly, the Panel has delegated CSR (social, environmental and ethical) policy to the appointed investment managers. The council believes this is the most efficient approach whilst ensuring the implementation of policy by each manager is consistent with current best practice and there is appropriate disclosure and reporting of actions taken.

Authority has been delegated to the investment managers to exercise voting rights on behalf of the Fund. The investment managers are required to report how they have voted in their quarterly reports.

7. COMPLIANCE WITH THIS STATEMENT

The Panel will review the Fund's compliance with this Statement of Investment Principles and issue a revised version following any material change in the Council's policy.

8. COMPLIANCE WITH THE SIX MYNERS PRINCIPLES OF INVESTMENT DECISION MAKING

Regulation 12(3) of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 requires an administering authority to report on its compliance with the six Myners Principles, in accordance with guidance given by the Secretary of State. The guidance for the Local Government Pension Scheme is set out in the publication by CIPFA called "Investment Decision Making and Disclosure in the Local Government Pension Scheme: A guide to the application of the Myners Principles".

The principles, together with the council's position on compliance are set out below:

Principle 1 - Effective decision-making,

Administering authorities should ensure that:

- ***Decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to make them effectively and monitor their implementation; and***
- ***Those persons or organizations have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.***

Fully Compliant - The council has delegated the management and administration of the pension fund to the Pensions Fund Investment Panel ("The Panel") which meets quarterly. The responsibilities of The Panel are described in paragraph 2.1 above.

The Panel is made up of elected members of the council who each have voting rights and has representatives from the admitted and scheduled bodies within the Fund and from trade unions, as observers. The Panel has specific terms of reference which are reviewed and agreed annually, standing orders and operational procedures and reports to the full council. Members are not paid specifically for these duties.

The Panel obtains and considers advice from the Director of Finance and Corporate Services, and as necessary from the Fund's appointed actuary, investment managers and advisors. The Panel is supported by the Business Support and Pension sections of the Finance and Corporate Services Department. Training is provided to members as required.

The Panel has delegated the management of the Fund's investments to professional investment managers, appointed in accordance with the scheme's regulations, whose activities are specified in detailed investment management agreements and regularly monitored.

Principle 2 - Clear objectives

An overall investment objective(s) should be set for the fund that takes account of the scheme's liabilities, the potential impact on local tax payers, the strength of the covenant for non-local authority employers, and the attitude to

risk of both the administering authority and scheme employers, and these should be clearly communicated to advisors and investment managers.

Fully Compliant - The Panel has agreed in conjunction with its advisor an investment objective that is directly related to the Fund's liabilities (See paragraph 3.1 above). The investment objective aims to enable employer contribution rates to be kept as nearly constant as possible and at reasonable cost to the taxpayers and admitted bodies,

The investment strategy has been set with the objective of controlling the risk that the assets will not be sufficient to meet the liabilities of the Fund while achieving a good return on investment (see paragraphs 4 and 5 above).

The approach taken reflects the Fund's liabilities and was decided upon without reference to any other funds. The Fund's performance is measured against the investment objective on a quarterly basis.

Principle 3 – Risk and liabilities

In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of liabilities.

These include the implications for local tax payers, the strength of the covenant for participating employers, the risk of their default and longevity risk.

Fully Compliant - The Panel has agreed in conjunction with its advisor an investment Strategy that is directly related to the Fund's liabilities. The investment strategy is described in paragraphs 4 and 5 above and was set following the actuarial valuation at 31st March 2007. An actuarial valuation of the fund takes place every three years.

The investment strategy is designed to give diversification and specialisation and achieve optimum return against acceptable risk (see paragraph 5.3 above).

Principle 4 – Performance Assessment

Arrangements should be in place for the formal measurement of performance of the investments, investment managers and advisors

Administering authorities should also periodically make a formal assessment of their own effectiveness as a decision-making body and report on this to scheme members

Partially compliant - The Panel has appointed investment managers with clear index strategic benchmarks (see paragraph 4.3 above) within an overall Investment objective which place maximum accountability for performance against that benchmark on the manager.

The managers are monitored at quarterly intervals against their agreed benchmarks, and independent detailed monitoring of the Fund's performance is carried out by P-Solve Asset Solutions, the Fund's advisor and by Northern Trust, the Fund's custodian who provide the performance figures.

The advisor is assessed on the appropriateness of asset allocation recommendations and the quality of advice given (see paragraph 2.4 above). The actuary is assessed on the quality and consistency of the actuarial advice received (see paragraph 2.5 above). Both the advisor and the actuary have fixed term contracts which when expired are tendered for under the OJEU procedures.

The Panel does not periodically make a formal assessment of its own effectiveness as a decision-making body but does receive quarterly reports as to how the Fund has performed against the investment objective set by the panel. The performance figures are included in the extract from the accounts which is sent to stakeholders annually.

Principle 5 – Responsible Ownership

Administering authorities should:

- ***Adopt, or ensure their investment managers adopt, the Institutional Shareholders Committee Statement of Principles on the responsibilities of shareholders and agents***
- ***Include a statement of their policy on responsible ownership in the statement of investment principles***
- ***Report periodically to scheme members on the discharge of such responsibilities***

Partially compliant –

Majedie our UK Equity investment manager has adopted the Institutional Shareholders Committee Statement of Principles and MFS our overseas equity investment manager are signatories of the United Nations Principles of Responsible Investment (UNPRI).

Barings and Ruffer who manage our Dynamic Asset Allocation portfolios which have some equity exposure have not adopted the principles but have corporate governance and socially responsible investment policies which are broadly in line with the principles.

The Fund believes in using its influence as a shareholder to promote corporate social responsibility and high standards of corporate governance in the companies in which it invests (see paragraph 6 above). Authority has been delegated to the investment managers to exercise voting rights on behalf of the Fund. The investment managers are required to report how they have voted in their quarterly reports.

This Statement of Investment principles is included in the Pension Fund Annual Report which is available to all scheme members.

Principle 6 – Transparency and reporting

Administering authorities should:

- ***Act in a transparent manner, communicating with stakeholders on issues relating to their management of investments, its governance and risks, including performance against stated objectives***

- ***Provide regular communications to scheme members in the form they consider most appropriate.***

Fully compliant - The Governance Compliance Statement, the Statement of Investment Principles, the Funding Strategy Statement and the Communications Statement are all included in the Pensions Fund Annual Report which is published and is accessible to stakeholders of the Fund on the Council's web site and internal intranet. Monitoring results of the fund's performance are also included. An extract from the accounts is sent to stakeholders annually.

For further information on this statement contact-

Pat Gough, Assistant Director of Finance and Corporate Services, Finance Department,

Town Hall, King Street, Hammersmith, London, W6 9JU

Phone: 020-8753 2542 E-mail: Pat.Gough@lbhf.gov.uk