

Essex Pension Fund

Statement of Investment Principles 2010

as at 1 April 2010



Statement of Investment Principles

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 “**the Regulations**” require local authority pension funds to prepare a Statement of Investment Principles “**SIP**” and to review it annually. They are also required to publish each year a Statement of Compliance with the 6 Principles of Investment Management issued by the Government. The Essex Pension Fund “**the Fund**” first adopted a SIP on 12 May 1999 and has since reviewed it at least once each year.

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Background

Essex County Council is the administering authority “**the Authority**” for the Fund under the Regulations. Responsibilities for its investment functions have been delegated to the Investment Steering Committee “ISC” and the Chief Financial Officer “**the CFO**”. The ISC is composed of 6 county councillors and 2 non-voting observers, one appointed annually by the Essex Local Government Association and representing all Fund Employers and the other by UNISON and representing all Fund Members. The ISC is provided with investment advice by Hymans Robertson, two independent investment advisers, the Executive Director for Finance & Deputy Chief Executive and the CFO.

The Regulations specify that, in investing the Fund’s money, regard must be given to the need for diversification and to proper advice obtained at reasonable intervals. External investment managers have been appointed to make the day-to-day investment decisions.

Set out below are the key investment principles that have been adopted by the Fund.

Objectives

1. The underlying aim of the Fund is to ensure that employers' contribution rates are set at a level to attain 100% funding, as certified by the Fund's Actuary, whilst keeping the employers' contribution rates as stable as possible. With regard to the investments of the Fund the objective is to maximise returns within an acceptable risk profile.
2. In 2001 the Fund adopted a customised benchmark, which sets out the strategic asset allocation for the Fund. This was agreed following the consideration of a detailed asset liability modelling exercise, taking account of the specific characteristics of the Fund. Such a study requires assumptions to be made regarding returns on the Fund's assets and in this connection, in preparation for the 2007 Valuation, Hymans Robertson were asked to update the investment expectations for the Fund. The following is a summary of their findings:

Expected strategic return on assets

At 31 March 2007, Hymans Robertson's assumptions with regard to the long term returns on asset classes were:

UK Equity:	7.9%
Overseas Equity:	7.6%
Fixed Interest Gilts:	4.6%
Index-linked Gilts:	4.3%
Property:	5.8%
Corporate Bonds:	5.4%
Private Equity:	9.3%

Given the Fund's long term strategic allocation of assets at that time (re-weighting for Private equity) of:

%	
26.5	UK Equity
37.2	Overseas Equity
6.0	Fixed Interest Gilts
6.0	Index-Linked Gilts
12.0	Property
6.0	Corporates
6.3	Private Equity (assume inclusion of shareholder activism)

this would imply a long term strategic expected return of 7.06% p.a. on an arithmetic weighted average of these individual returns. This does not take account of any expected return from active management (including currency) or the benefit we might expect from diversification (which we expect to come through as 'bonuses'). Using Hymans Robertson's internal structure model (which, in this case, also does not take account of active management, but does allow for the benefits of diversification) some analysis was performed with respect to various expected returns and the probability of achieving that return. The model (based on the current structure) calculates a central expected return of 7.93% p.a. The overall expected return on a portfolio of assets does not solely reflect the arithmetic weighted average of the returns on the individual asset classes. This is due to diversification i.e. when

you combine a portfolio of assets which are not fully correlated to each other, the expected portfolio return is greater than the arithmetic combination of the individual returns. This reflects the lower volatility of the portfolio compared to the volatility of the sum of the parts. This is sometimes referred to as ‘volatility drag’.

The probability of achieving particular levels of out-performance relative to the liabilities is as follows:

Probability of achieving liabilities

+ 1.0% p.a.= 57%

Probability of achieving liabilities

+ 2.5% p.a.= 53%

Probability of achieving liabilities

+ 3.5% p.a.= 50%

3. In September 2008 the ISC, as part of a comprehensive review of investment strategy and structure, reviewed its approach to investment and set down its core investment beliefs. These are reproduced in full at Appendix A. As part of that same review exercise they then re-examined the asset allocation and investment management structure of the Fund and adopted a revised target structure that was in line with their core investment beliefs. This is set out below with more detail provided in Appendix B.
4. The risks in terms of volatility of funding levels and employers’ contribution rates have been considered in depth by the ISC and the strategic asset allocation has

been set consistent with the liabilities in the Fund, taking full account of the risks involved following the detailed consideration of the asset liability modelling exercise. This was formulated to take account of the ISC’s attitude to risk. The strategic asset allocation, the customised benchmark and the tolerances set on investment managers’ performance are the means by which the ISC aims to achieve the overall fund objective.

5. Risk associated with investments will be controlled by the diversification of investments over asset classes and the use of a number of investment managers. Regular reports will be made to the ISC.
6. The majority of the Fund’s investments are quoted on major stock markets and are in readily realisable form. The Fund’s strategic allocation to property and partnership investments, which are relatively illiquid, is currently 21.5% of the Fund’s assets. The Fund is relatively immature with almost as many contributors as pensioners, dependants and deferred pensioners. In consequence the Fund has a positive cash flow and is able to pay benefits from contributions received. As the Fund is not in the position of a forced seller, i.e. it does not need to sell assets in order to pay benefits, it is considered appropriate to hold such investments to increase diversification, minimise risk and improve long-term investment performance.

Strategic Asset Allocation

The Fund's strategic asset allocation with effect from 30 July 2009 is as follows:

	%
UK Equities	10.0
Global Equities	28.0
Overseas Equities	25.0
Shareholder Activism	2.0
Private Equity	4.0
UK index-linked	3.8
Fixed interest – UK gilts	1.2
Fixed interest – Sterling non-government	5.5
LIBOR+	5.0
Infrastructure	2.5
Property	12.0
Company Loans	1.0
Total	100.0

More detail is provided at Appendix B.

Investment Management Strategy

The investment management strategy is to appoint expert investment managers with a clear performance benchmark and place maximum accountability for performance against that benchmark on the investment manager. The Fund has recently adopted a growth/income structure, allocating 69% of its assets to asset classes (equities, private equity, activism) that are expected to grow at levels significantly in excess of bonds in the long term and therefore reduce the cost of providing pension provision and 31% of assets to income sectors (bonds, property, infrastructure and company loans) to control overall volatility and provide cash income and liquidity to the Fund.

Investment Managers

The Fund's investment management arrangements now consist of one passive balanced "swing" manager (who also manages a passive currency hedge), four active global equity managers, one active emerging market equity manager, two active bond managers, one private equity manager, one property manager, two active currency managers and holdings in shareholder activism funds, infrastructure and company loans. (See Appendix B for asset allocation and Appendix C for details of individual investment managers' mandates).

Managers' performance against their agreed

targets will be monitored and reviewed each quarter. In addition a detailed review of their performance will be carried out on an annual basis.

1. Managers are required to submit quarterly reports on their performance, their asset holding and their future intentions together with any changes they are planning to make to their portfolios. A statement of their compliance with the SIP is also to be included.
2. Managers are required to attend meetings as requested with officers and advisers and/or the ISC to discuss their performance and future intentions.
3. Managers must comply with all legitimate instructions given to them by the Authority. In the event of any perceived conflict with the law, rules, regulations or the agreement between the manager and the Authority, the manager must consult with the Authority in order to resolve the conflict.
4. Managers must not enter into soft commission arrangements in respect of the funds they manage on behalf of the Fund unless those arrangements have been approved by the Authority.
5. The Authority must be able to terminate the appointment of any manager by giving not more than one months notice.

Responsibilities

ISC Responsibilities

1. To approve and annually review the content of the SIP.
2. To appoint and review investment managers, custodian and advisors.
3. To assess the quality and performance of each investment manager annually in conjunction with investment advisers and the Chief Financial Officer.
4. To set the investment parameters within which the investment managers can operate and review these annually.
5. To monitor compliance of the investment arrangements with the SIP.
6. To assess the risks assumed by the Fund at a global level as well as on a manager by manager basis.
7. To approve and review the asset allocation benchmark for the Fund.
8. To submit quarterly reports on its activities to the Essex Pension Fund Board.

Custodian Responsibilities

1. To safeguard all segregated assets (excluding direct property holdings, unitised holdings and cash held separately with either the Authority or investment managers) within the Fund and ensure that all associated income is collected, including dividends and tax reclaims. Also to ensure that corporate actions affecting the securities are dealt with, including rights issues, bonus issues and acquisitions.
2. To provide regular statements of transactions, corporate actions, income and asset valuations as required by the Authority.
3. To report to the ISC in person on the assets of the Fund if required.
4. To inform the Fund of any areas of concern which arise in its dealings with investment managers.

Audit Responsibilities

1. The Fund is subject to review by both the County Council's External Auditors (The Audit Commission) and internally by Internal Audit.
2. The Pension Fund financial statements contained in the Council's Annual Statement of Accounts present fairly:
 - the financial transactions of its Pension Fund during the year; and
 - the amount and disposition of the Fund's assets and liabilities, other than liabilities to pay pensions and other benefits after the end of the scheme year.

The External Auditor audits the Pension Fund financial statements and gives their opinion, including:

- whether they present fairly the financial position of the Pension Fund and its expenditure and income for the year in question; and
- whether they have been prepared properly in accordance with relevant legislation and applicable accounting standards;

In carrying out their audit of the financial statements, auditors will have regard to the concept of materiality.

Additionally the Council must prepare a Pension Fund annual report which should contain the Pension Fund account and net asset statement with supporting notes and disclosures. External Audit will review the annual report as a whole and the accounts contained in it and then report:

- whether the accounts contained in the annual report are consistent with the financial statements on which the audit opinion was given; and
- that other information in the annual report is not inconsistent with the financial statements on which the audit opinion was given.

3. Internal Audit carry out a programme of work designed to reassure the Section 151 Officer that Fund investment systems and records are properly controlled to safeguard the Fund's assets
4. Investment Managers and Custodians are subject to regulation by the Financial Services Authority and are required to provide their customers with Internal Financial Controls reports which have been prepared by their auditors. These reports form part of the overall assurance and control mechanism for the Fund.

Investment Limits

The overriding limits that apply for the different types of pension fund investments are set out in the Regulations. These regulations allow an administering authority to increase some of those limits up to specified amounts. When deciding to increase or review limits, the administering authority must:

- take account of proper advice and of the factors in Regulation 9 (3) of the Regulations (the advisability of investing fund money in a wide variety of investments and the suitability of

particular investments and types of investments); and

- the decision must specify certain matters and those matters must be published in a revised statement of investment principles before they can take effect.

Having taken proper advice, from both external investment advisers and its own officers, and having taken account of the factors in Regulation 11(2) of the Regulations, the ISC has decided to increase the following investment limits as set out below:

a. the description of the investment	all contributions to any single partnership	all contributions to partnerships	investment in any single insurance contract
b. the limit on the amount of the investment	limit increased from 2% of total fund to 3% of total fund	limit increased from 5% of total fund to 15% of total fund	from 25% of the total fund to 35% of the total fund
c. the reason for the decision	to permit up to 3% of the total fund to be invested in a single infrastructure fund organised as a partnership	to permit additional investment in private equity, infrastructure, shareholder activism and property partnerships	to permit additional investment in the pooled funds of the Fund's passive index tracking manager
d. the period for which the decision will apply;	for a period of 10 years from 31 March 2008.	for a period of 10 years from 31 March 2008.	for a period of 10 years from 27 July 2005

The above decisions comply with the Regulations.

General Fund Investment Restrictions

The Fund is subject to the overall restrictions specified in the Regulations, modified in certain instances by the Administering Authority as set out above. In addition the Council has determined that the following restrictions should be applied:-

A. For the Fund as a whole

1. Asset allocation benchmarks will be set by the ISC to ensure that the Fund's assets are adequately diversified.
2. Cash held in house by the Authority on behalf of the Fund shall not normally exceed £5 million unless in line with investment policy.
3. The cash holdings of individual investment managers will be monitored and reported upon.

B. For each individual Investment Manager

1. Approval must be sought by each individual investment manager for any new investments in the unlisted securities of companies, in-house unit trusts, open-ended investment companies or insurance contracts, including sub-underwriting contracts.
2. Individual investment managers must not hold more than 5% of equity capital of an individual company on behalf of the Fund. However, in exceptional circumstances, the CFO may increase this limit to 10%, but details of these must be reported

to the next ISC meeting. Managers are responsible for reporting any possible exceptions before they occur.

3. The use of derivatives is restricted to efficient portfolio management in circumstances where the impact on any mandate or on the fund overall is tightly controlled by explicit limits on risk that have been explicitly agreed by the ISC. A cap of 10% of the total value of each investment manager's portfolio on the total economic exposure to derivatives must not be exceeded without the prior consent of the CFO.
4. Hedging of the overseas currency exposure of the Fund is permitted for the purpose of protecting against possible adverse fluctuations in the pounds sterling values of investments or cash in the Fund denominated otherwise than in pounds sterling. Managers will be allowed some latitude to use forward currency contracts to implement active currency views, provided that the aggregate risks across the portfolio remain within the limits explicitly agreed by the ISC under the terms of the mandate.
5. Underwriting of shares can only be undertaken for investment purposes and must not be entered into for short term trading.

6. Investments of cash by investment managers must be in line with their individual management agreements which limit the amount that can be invested in any single institution.
7. Controls have been agreed on the extent of the positive positions which a manager can take on individual UK equities relative to the proportion which that stock represents in the Index. Where the market weighting of an individual stock exceeds 10% of the Index, exposure to that stock is limited to 2% more than the market weighting as a proportion of the overall UK equities in the mandate. The monitoring of holdings is the responsibility of the individual investment managers.

Partnership Investments

The ISC will scrutinise proposed partnership agreements and only enter into them if the terms of the agreements are appropriate and the purpose of the partnership supports the asset allocation strategy. The amount invested in any single partnership at the time of commitment must not exceed 3% of the Fund. Total investment in all partnerships at the time of commitment must not exceed 15% of the Fund.

Socially Responsible Investments

1. The ISC does not place restrictions on investment managers in choosing investments in quoted companies except in limiting the size of single investments. We expect the companies in which we invest to adopt and pursue socially responsible business practices.
2. The ISC will intervene if investments are made in companies whose behaviour is seen as unacceptable because of environmental considerations and other social implications. Intervention is likely to be extremely rare as companies are aware of the increasing sensitivity of investors.

Corporate Governance

1. The Fund fully supports the principles of responsible share ownership and requires investment managers who hold shares on its behalf to act as responsible share owners.

2. UK Shares

The National Association of Pension Funds “NAPF” has produced a Corporate Governance Policy that the Fund believes encapsulates the principles of responsible share ownership. The Fund recommends that its investment managers should follow NAPF Corporate Governance Policy in managing the UK shares they hold on the Fund’s behalf. However where for whatever reason they do not deem this to be appropriate they are required to report back to the ISC to obtain agreement to alternative arrangements.

3. Overseas Shares

The Organisation for Economic Co-operation and Development (OECD) has produced a set of Corporate Governance Principles and the International Corporate Governance Network (ICGN) a set of Global Corporate Governance Principles which provide widely accepted standards for corporate governance in many countries and which the Fund believes are suitable principles to apply to achieve responsible share ownership.

The Fund recommends that its investment managers should follow OECD Corporate Governance Principles and ICGN Global Corporate Governance Principles in managing the overseas shares they hold on the Fund’s behalf. However where for whatever reason they do not deem this to be appropriate they are required to report back to the ISC to obtain agreement to alternative arrangements.

Stock Lending

1. Segregated Investments

The Fund does not participate in stock lending schemes nor allow its stock to be lent.

2. Pooled Investments

In regard to the Fund's pooled investments, where the Fund is buying units in a pooled vehicle, stock lending is outside the control of the Fund and undertaken at the discretion of the pooled fund manager.

Appendix A

Essex Pension Fund Investment Steering Committee Core Investment Beliefs

1. Long term approach

- a. Local authority funds take a long term view of investment strategy*

This is largely based on covenant. Unlike the private sector, the covenant underlying the Fund is effectively gilt-edged. This means that short term volatility of returns can be acceptable in the pursuit of long term gain. Whilst there is a need to consider stability of contributions, at current maturity levels and with deficits spread over 20 years, it is largely the future service rate which is expected to drive instability. One of the best ways to avoid this is to build in margins over the long term.

- b. Over the long term, equities are expected to outperform other liquid asset classes, particularly bonds*

Given 1. a. above, there is a preference for a significant allocation to equities in the Fund as over the long-term as they are expected (but not guaranteed) to outperform other asset classes.

- c. Allocations to asset classes other than equities and bonds expose the Fund to other forms of risk premium*

Investors with a long term investment horizon and little need for immediate liquidity can use this to their benefit as it offers the ability to capture the

illiquidity premium on many asset classes, such as private equity and infrastructure.

2. Diversification

- a. Diversification into alternative asset classes (including property) is also expected to reduce overall volatility of the Fund's funding level*

Given that the returns from different asset classes are expected to be delivered in different cycles (i.e. not be directly correlated with equity returns), the use of alternative assets can reduce overall volatility in the delivery of Fund returns without leading to a significant reduction in overall expected return, therefore increasing efficiency.

- b. In the context of LA funds (open, long duration, not maturing quickly and with high equity content), an allocation to bonds does not offer a match to liabilities, but additional diversification.*

Where bonds are not used for liability matching purposes, an allocation to these assets can be beneficial from an overall risk/return perspective improving the overall efficiency of the Fund. The corollary to this is that bond benchmarks do not necessarily have to reflect the nature and duration of the liabilities (see benchmark section

below), but should be set to provide managers with the sufficient scope to add value.

- c. *The overweight to UK equities in most UK pension funds is historic and loosely based on currency exposures, rather than a preference for the UK market*

Although historically the UK may have benefited from better corporate governance, and therefore a higher return, increasingly the rest of the world is catching up and UK equities are not expected to outperform overseas equities over the long term. Given the concerns over market concentration in the UK market and an increased opportunity set overseas a move towards increased overseas allocation relative to the UK seems appropriate. Concerns about currency risk can be addressed by a separate currency hedging programme.

- d. *Benchmarks*

Where appropriate, benchmarks should represent the full opportunity set.

For example, for a global equity mandate, a market capitalisation (“market cap”) weighted benchmark reflects a passive allocation to the market (analogous to investing in a passive equity mandate and investing in each stock according to its size). It therefore reflects the investable universe of stocks available and represents the starting point for an equity benchmark.

- e. *To some extent market cap weighted indices reflect past winners, so should be treated with caution*

The regional exposures in the World Index are a function of the relative market cap of the regional stockmarkets. In turn, these are a function of the size of the economy as a whole and how well companies have performed in that economy. One measure of the size of the economy could be its overall contribution to global GDP. However, as has been seen in the UK, many companies in the market have little exposure to the domestic economy and, again, this should not be adhered to too slavishly. At the total fund level a fixed weights regional benchmark is therefore preferred in order to maintain an appropriate level of diversification across markets. This is particularly the case when the allocations are maintained by a passive “swing” manager.

- f. *Emerging market economies may be expected to outperform over the long term as the economy develops and the risk premium falls*

As emerging markets develop both politically and economically, become more robust and less dependent on the fortunes of a small number of developed economies (such as the US), the risk of investing in these countries should decrease. The return demanded by investors for investing in these ‘riskier’ countries will therefore

fall reflecting the increased security. This reduction in required return would tend to lead to a systematic increase in stock prices. As a result, a strategic allocation to emerging markets of at least the market cap weight if not slightly above is favoured.

g. Bond benchmarks do not need to reflect the nature and duration of the liabilities

As discussed in the diversification section above, if bonds are not held for liability matching purposes, benchmarks should be set in order to maximise the scope for adding value.

3. Active versus passive management

a. Passive management is appropriate for obtaining a low cost allocation to efficient markets

Where markets offer little scope for adding value through active management (such as individual allocations to UK equities, US equities and gilts) passive management is preferred as a low cost way of accessing the market. This does not include emerging markets where the risk inherent in the market (although improving as stated above) and inefficiency of the market lends itself to active management.

b. Active management is appropriate where a market is relatively inefficient offering opportunities for active managers to add value

Where markets offer substantial scope

for added value active management would seem appropriate as a way of increasing overall expected return (after fees) without significantly increasing the overall level of volatility in the funding level.

c. Constraints on active managers reduce their ability to add value

Active managers should not be unnecessarily constrained (within appropriate risk limits) and should be given the maximum scope to implement their active views. There is therefore a preference for unconstrained mandates e.g. unconstrained global equity mandates and unconstrained bond mandates such as M & G's LIBOR plus approach. This also suggests that, within reason, managers' requests for additional scope should be acceded to.

d. A degree of diversification of managers improves the efficiency of the overall structure (i.e. improves the expected return per unit of risk)

Active manager performance is expected to be cyclical and therefore by appointing a number of managers the delivery of returns is expected to be less volatile. However, too much diversification can lead to expensive index tracking.

e. A rigorous approach to active manager selection improves the chance of appointing an active manager who will add value over the long-term

An active manager must outperform their benchmark after fees to add value. The selection of an active manager must assess more than just past performance and look into the infrastructure supporting the performance including; business and ownership, philosophy and process, people, risk controls and fees.

- f. The Fund does not have the governance structure in place to take tactical views and market timing is very difficult*

Both timing investments into the market and taking tactical views are very difficult given the governance structure in place and the time taken to agree and implement decisions. Where possible these decisions are left to professional investment managers who are closer to the market and can implement tactical views in a more timely fashion. This highlights the importance of not unnecessarily constraining active managers and providing them with appropriate scope.

- g. The assessment of active management performance should be taken with a long-term view and take account of the market environment in which returns are delivered*

Active management is cyclical and periods of underperformance from investment managers should be expected so the structure should be such that when the market cycle is unfavourable for some managers it is

favourable for others and vice versa. This is expected to deliver added value over the long-term whilst smoothing the overall performance at the total Fund level. Churning of managers leads to additional costs; however, where the ISC no longer views an investment manager's prospects as positive over the long-term, action should be implemented as soon as possible due to the potential downside risk.

Appendix B

Essex Pension Fund – Target Structure as at 30 July 2009

	Effective Benchmark	Passive Balanced (swing)	Equities					Bonds		Alternatives					
			L&G	Fidelity	Marathon	Baillie Gifford	Alliance Bernstein	First State	GSAM	M&G	Property	Activism	Currency	Infra-structure	Private Equity
Fund Weighting	100.0	33.0	7.0	7.0	7.0	7.0	4.0	5.5	5.0	12.0	2.0	3.0	2.5	4.0	1.0
UK equities	10.0	25.5										50.0			
Global equities	28.0	0.0	100.0	100.0	100.0	100.0									
North America	7.9	19.5										50.0			
Europe	6.4	19.5													
Japan	4.5	13.6													
Pacific ex-Japan	2.2	6.8													
Emerging markets	4.0						100.0								
Total Equities	63.0	84.8	100.0	100.0	100.0	100.0	100.0				100.0				
UK index linked	3.8	11.4													
UK Gilts	1.2	3.8													
UK Corps	5.5							100.0							
Libor+	5.0								100.0						
Total bonds	15.5	15.2						100.0	100.0						
Infrastructure	2.5											100.0			
Shareholder activism	2.0									100.0					
Private equity	4.0													100.0	
Company loans	1.0														100.0
Property	12.0									100.0					
Total alternatives	21.5									100.0	100.0		100.0	100.0	100.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Growth															69.0%
Income															31.0%

Appendix C

Mandates: Performance Objectives

Manager	Mandate Type	Benchmark Indices	Before fees	Performance Target After fees	Period for measurement	Target tracking error* <i>Note 1</i>
Legal & General	Passive Equities Swing	Multi-index* <i>Note 2</i>	To track the index* <i>Note 3</i>		Ongoing	
Legal & General	Passive Bonds Swing	Multi-index* <i>Note 2</i>	To track the index* <i>Note 3</i>		Ongoing	
Fidelity	Global Equities	MSCI World Index	Benchmark + 2.0%		Rolling 3-5 year periods	
Marathon	Global Equities – segregated	FTSE All World Index		Benchmark + 3.0%	Rolling 3 year periods	Ex-post 9.0% or less p.a.* <i>Note 4</i>
Marathon	Global Equities – pooled	MSCI World Index		To exceed the benchmark	Rolling 5 year periods	
Baillie Gifford	Global Equities	MSCI AC World Index	Benchmark + 3.0%		Rolling 5 year periods	
Alliance Bernstein	Global Equities	MSCI World Index	Benchmark + 3.0%		Full market cycle* <i>Note 5</i>	4% to 9% p.a.
First State	Emerging Markets Equities	MSCI Emerging Markets Free Index Unhedged (in UK Sterling)		Benchmark + 4.0%	Rolling 3 year periods	Ex-post 12.0% or less p.a.* <i>Note 4</i>
GSAM	Bonds	iBoxx Sterling nonGilts index		Benchmark + 1.25%	Investment cycle* <i>Note 6</i>	2.25% p.a.
M & G	Bonds	One-month sterling LIBOR		Benchmark + 1.0%	Rolling 3 year periods	3.0% or less p.a.
Aviva	Property	Multi-index* <i>Note 2</i>	Benchmark + 1.0%		Rolling 3 year periods	
Mellon	Active Currency	FTSE 100 Index		Benchmark +20.0%	Rolling 3 year periods	
Record	Active Currency	S & P 500 Index		Benchmark +18.0%	Rolling 3 year periods	

Explanatory Notes

*Note 1: Target tracking error - the range of returns likely in the portfolio relative to its benchmark/index

*Note 2: Multi-index - a separate index is applied to each sub-asset class

*Note 3: To track the index - Seeks to attain performance equal to the specified index returns. Invest in the same shares and in the same proportions as those in the index being tracked.

*Note 4: ex-post – projected possible range of future returns

*Note 5: Full market cycle – A rising and a falling market taken together. An average market cycle is 3-5 years.

*Note 6: Investment cycle – Rolling 3 year periods

Investment Decision Making and Disclosure in the LGPS Statement of Compliance

The position of the Essex Pension Fund “the Fund” in relation to the statutory guidance issued by CIPFA is set out below.

Principle	Extent of compliance		
	Full	Partial	Not
1. Effective Decision Making		✓	
Areas of non compliance and explanation			
<p>While the roles of some officers are set down clearly in the Constitution this needs to be extended to all officers.</p> <p>While the Essex County Council appointments to the committee have been based on consideration of relevant skills, experience and continuity it needs to be confirmed with other nominating authorities if the same is true of their appointments.</p> <p>The SIP needs to be amended to provide a complete differentiation and specification for members, officers, external advisors and managers.</p> <p>The training arrangements which are well developed need to be reviewed in the light of the issuance of the CIPFA knowledge and skills framework.</p> <p>Consideration needs to be given to including standing orders in the Member handbook.</p> <p>Provision of the training plan for members is currently a shared responsibility.</p> <p>While the allowances paid to Essex County Council elected members are set out in a published allowances scheme, regularly reviewed in the way described and have regard to the types of matters mentioned, it needs to be confirmed with other nominating authorities if the same is true of their allowances. No additional allowances are paid by Essex County Council for attendance at the meetings of the Essex Pension Board or ISC.</p> <p>The issue of whether the single UNISON representative is allowed adequate time off from their normal duties to attend meetings and to read the papers has to be referred to UNISON as he is not an Essex County Council employee.</p> <p>While the business plan arrangements are in place some aspects of performance measurement and financial estimating are still under development and it does not currently detail external resources used.</p> <p>The Fund does not currently have an administration strategy.</p>			
Action to be taken			
<p>The regulations and guidance have been issued at such short notice and are so voluminous that it has not proved possible in the time allowed to carry out the actions necessary to achieve full compliance. However the following actions are planned to be</p>			

carried out in 2010/11 and are expected to bring the Fund into full compliance with the guidance:

- The rules of conduct for the Pension Board and ISC and the standing orders will be included in the Member Handbook.
- The basis of nominations to the Pension Board and ISC and the approach to member allowances will be clarified with nominating bodies.
- It will be clarified with UNISON whether their nominee is allowed adequate time for preparation for meetings.
- A section will be added to the SIP on the role of external advisers.
- Provision of the training plan for members will be added to the CFO's responsibilities (this work has already been commissioned from the Independent Governance and Administration Adviser). A training statement describing actions taken and progress made will be included in the annual report.
- The business plan will be further developed to include a medium term perspective and the use of external resources.
- A comprehensive administration strategy will be drawn up and put out to consultation.

Principle	Extent of compliance		
	Full	Partial	Not
2. Clear Objectives		✓	
Comment/Justification			
<p>The range of asset classes considered at the annual review of investment strategy is very broad but may not include all asset classes available to investors.</p> <p>Although value for money and efficiency are important priorities for the Fund, its business plan does not currently highlight that aim in its objectives and all aspects of its operations. The Fund does not have in place clear performance objectives and a performance measurement framework for its advisers.</p> <p>Fully compliant in regard to transaction related costs in transition management contracts and in monitoring normal investment management contracts but not compliant in regard to letting contracts for normal investment management.</p>			
Action to be taken			
<p>The regulations and guidance have been issued at such short notice and are so voluminous that it has not proved possible in the time allowed to carry out the actions necessary to achieve full compliance. However the following actions are planned to be carried out in 2010/11 and are expected to bring the Fund into full compliance with the guidance:</p> <ul style="list-style-type: none"> • The process used to determine the Fund's asset allocation will be reviewed to ensure that the decision making process is transparent. • The inclusion of appropriate performance objectives and a performance measurement framework in contracts will be discussed with investment advisers and built into the next contract with investment consultants. • We will consider with investment advisers and consultants the extent to which transaction-related costs should be a consideration in letting and monitoring investment management contracts. 			

Principle	Extent of compliance		
	Full	Partial	Not
3. Risk and Liabilities		✓	
Comment/Justification			
<p>Investment management agreements generally show the range of returns likely rather than acceptable.</p> <p>A description of the risk assessment framework used for potential and existing investments does not appear in the Fund's SIP.</p> <p>The Fund has adopted a customised (scheme specific) benchmark. Although it is formulated having regard to the level of risk, both active and market, considered acceptable the actual level of risk being taken is not clearly quantified.</p> <p>Although some aspects of the risk assessment undertaken by the Fund appear in the annual report under the Funding Strategy Statement, no overall risk assessment is included.</p>			
Action to be taken			
<p>The regulations and guidance have been issued at such short notice and are so voluminous that it has not proved possible in the time allowed to carry out the actions necessary to achieve full compliance. However the following actions are planned to be carried out in 2010/11 and are expected to bring the Fund into full compliance with the guidance:</p> <ul style="list-style-type: none"> • The SIP will be revised to show a formal risk assessment framework which makes clear the actual level of risk being taken. • The business plan now includes a requirement for a report on risk management to be brought to each meeting of the Pension Board. • A risk assessment will be included in the Fund's annual report. 			

Principle	Extent of compliance		
	Full	Partial	Not
4. Performance Assessment		✓	
Comment/Justification			
<p>The Fund does not have in place a formal performance framework against which to measure the cost, quality and consistency of advice received from its actuaries.</p> <p>The Fund does not have in place a formal performance framework against which to measure its consultants on issues such as the appropriateness of asset allocation recommendations (bearing in mind the nature of the liabilities), the quality of advice in choosing benchmarks and any related performance targets and risk profiles, the quality and appropriateness of the investment managers that are recommended, and the extent to which advisors are proactive and consistent in recommending subsequent changes.</p> <p>The business plan is constructed to show expected progress and performance standards against a number of detailed areas but not the specific matters highlighted in the guidance.</p>			
Action to be taken			
<p>The regulations and guidance have been issued at such short notice and are so voluminous that it has not proved possible in the time allowed to carry out the actions</p>			

necessary to achieve full compliance. However the following actions are planned to be carried out in 2010/11 and are expected to bring the Fund into full compliance with the guidance:

- An appropriate performance measurement framework will be discussed with advisers and built into the next contracts for investment consultancy, investment advice and actuarial services.
- The business plan provides for an annual assessment of the effectiveness of the Pension Board and the services supplied to it. The exercise will be extended to include the areas recommended and the assessment included in the annual report.

Principle	Extent of compliance		
	Full	Partial	Not
5. Responsible Ownership		✓	
Comment/Justification			
<p>ESG issues have not been a prominent feature of the investment manager selection process to date.</p> <p>The Fund has not ensured that its investment managers have an explicit strategy on intervention in place.</p> <p>The Fund has not ensured that its investment consultants have adopted the Institutional Shareholders’ Committee statement of practice in regard to consultants.</p> <p>It is not known if the Fund’s Investment managers comply with the Institutional Shareholders’ Committee Statement of Principles on the responsibilities of shareholders and agents.</p>			
Action to be taken			
<p>The regulations and guidance have been issued at such short notice and are so voluminous that it has not proved possible in the time allowed to carry out the actions necessary to achieve full compliance. However the following actions are planned to be carried out in 2010/11 and are expected to bring the Fund into full compliance with the guidance:</p> <ul style="list-style-type: none"> • The ISC will discuss ESG and responsible ownership issues and consider if further action is appropriate. • Adoption by investment consultants of the Institutional Shareholders’ Committee statement of practice will be considered in the current investment consultancy tendering exercise. 			

Principle	Extent of compliance		
	Full	Partial	Not
6. Transparency and Reporting		✓	
Comment/Justification			
<p>The Fund does not have a single clear policy statement on the matters on which stakeholders will be consulted or informed.</p> <p>The Fund does not currently publish information on fee structures in the SIP</p>			
Action to be taken			
<p>The regulations and guidance have been issued at such short notice and are so voluminous that it has not proved possible in the time allowed to carry out the actions necessary to achieve full compliance. However the following actions are planned to be carried out in 2010/11 and are expected to bring the Fund into full compliance with the guidance:</p> <ul style="list-style-type: none"> • The Fund’s Communication Policy Statement will be revised to provide a single clear policy statement on the matters on which stakeholders will be consulted or informed. • The information published in regard to investment management fee structures will be reconsidered when the SIP is next reviewed. 			

This information is issued by **Essex County Council**

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**The information contained in this document can be translated,
and/or made available in alternative formats, on request.**

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