STRATHCLYDE PENSION

Fundnews

February 2004

NEWSLETTER FOR CONTRIBUTORS

WHERE SERVICE COUNTS

Annual Meeting

The Fund held its most successful Annual Meeting to date in the Strathclyde Suite of the Glasgow Royal Concert Hall on Friday 20th June.

Over 150 Employer Representatives attended the meeting, which was chaired by Councillor Ruth Simpson, Glasgow City Council's City Treasurer.

The delegates were treated to a packed agenda, which covered a wide variety of topics. The topics related to various aspects of the Strathclyde Pension Fund Office (SPFO): including Administration, Investments, Communications and Accounts.

Also included on the agenda was an informative presentation of the '2002 Actuarial Valuation' by Donald Fleming, Hymans Robertson, Actuaries and Consultants.

The concluding item on the agenda was an Open Forum, which proved to be a very lively question and answer session. A transcript of the Open Forum can be viewed on the SPFO website, **www.spfo.org.uk**

UNDER NEW MANAGEMENT

SPFO wishes to extend a warm welcome to Lynn Brown, Glasgow City Council's newly appointed Director of Financial Services.

Lynn, former Head of Corporate Finance at The City of Edinburgh Council, took up her appointment on Monday 8th September 2003 replacing George Black, who is now Glasgow City Council's Chief Executive.

Lynn takes responsibility for the entire finance function at Glasgow, including the Strathclyde Pension Fund and SPFO.

In another significant change, subsequent to the May 2003 Council elections, Councillor Ruth Simpson became City Treasurer and Convener of the Strathclyde Pension Fund Sub-Committee.

.....STOP PRESS.....STOP PRESS.....STOP PRESS....

Stocktake of the Local Government Pension Scheme

The "Stocktake" review of the Local Government Pension Scheme, which is currently being carried out by the Office of the Deputy Prime Minister, will lead to some very significant changes to the Scheme.

The aim of the Stocktake is to ensure the sustainability of the Local Government Pension Scheme. Changes will be made via revised Regulations for the Scheme in 2004 and 2005.

A report on the following page details the progress of the review to date. The outcomes of the stocktake, and the implications for LGPS members will become clearer as the year progresses. We therefore intend to produce a special Stocktake edition of Fundnews later in the year.

"Stocktake"

Review of the Local Government Pension Scheme (LGPS).

BACKGROUND

A review of the Local Government Pension Scheme (referred to as the 'Stocktake') was initiated in England & Wales in 2001. The review has progressed through various discussion and consultation stages and will produce revised Regulations in 2 phases during 2004 and 2005.

PHASE 1

The first phase of Scheme amendments (in England and Wales) are contained in draft regulations, on which consultation closed during December 2003. The resultant amended regulations are likely to come into force from April 2004. **The Scottish Executive is responsible for the Regulations in Scotland, but amendments normally follow on directly from the English & Welsh Regulations.**

The main proposals in phase 1 are:

1. To introduce 'immediate vesting', i.e. no refund of contributions available once a member is in the scheme for 3 months;
2. To introduce a requirement for ill-health retirement decisions to be reviewed by employers on a regular basis with reduction, removal or increase of ill-health enhancement possible;
3. A requirement for each Administering Authority to prepare a Funding Strategy Statement by 31st March 2005 in accordance with guidance to be prepared by CIPFA;
4. A requirement for the actuary to take the Funding Strategy Statement into account when setting the common rate of employer's contributions;
5. A requirement for benefit statements to be issued annually by April 2005.

PHASE 2

Phase 2 regulations are due to be implemented a year later (April 2005) and will take into account responses made to the initial stocktake discussion papers and also proposals contained in the Government's June 2003 Green Paper Simplicity, Security and Choice: Working and Saving for Retirement - Action on Occupational Pensions. An initial discussion paper on this phase was issued in November 2003 for response by January 2004. This will lead to draft Regulations later in 2004.

The main proposals in the phase 2 discussion paper are:

1. the equitable phasing out of the "rule of 85";
2. increasing the earliest age at which LGPS benefits can be paid, (other than on the grounds of ill health) from 50 to 55;
3. the introduction of flexible retirement and incentivisation methods to encourage Scheme members to remain in employment;
4. to streamline Internal Dispute Resolution Procedures;
5. further simplification of the regulatory framework;
6. and a thorough assessment of the merits and demerits of options to increase the present level of employee contributions to the Scheme.

COMMENTARY

- The Government view stated clearly in a letter dated 7 November 2003 from the Office of the Deputy Prime Minister is that "it is simply not the case that the LGPS can remain as it is" and that "the ever-changing social and political context of pensions, in both the public and private sectors, makes some change in the LGPS inevitable".
- However, any move to Defined Contribution seems to have been taken off the agenda (at least for just now). The current proposals are described as necessary "if the LGPS is to retain its status as a funded, final salary public service pension scheme". (By implication, if the current proposals are not accepted, a shift to DC could be back on the agenda).
- Whilst falling equity markets have been the most visible cause of the "pensions crisis" over the last couple of years, increased life expectancy has been an equally significant factor. Proposals regarding increasing the retirement age (and therefore the working life) of Scheme members are aimed broadly at restoring the work/retirement balance. This is not just a feature of Local Government but is in line with the Government's overall pensions policy.
- Similarly, proposals to increase the employee contribution rate are aimed at restoring the balance between employers' and employees' share of the cost of pensions provision. Employee contributions have been fixed at 5% or 6% of salary since 1922. In the interim, scheme benefits have improved and the cost of pensions has risen inexorably as life expectancy has increased. To date, increasing costs have been borne solely by the employer.
- The discussion paper outlines a number of options for employee contribution rates, as follows:
  - increase rates for new members only by 1% (i.e. to 7% of salary);
  - increase for all scheme members by 1%;
  - increase for all scheme members by 2%;
  - amend the benefits package (e.g. to improve benefits for a higher contribution);
  - introduce a more flexible tariff (e.g. so that higher earners pay more).

CONCLUSION

The Local Government Pension Scheme still looks very attractive when compared to private sector schemes, particularly as so many of them have moved to Defined Contribution arrangements where the employee bears all the investment risk, and typically a larger share of the costs.

Ironically, this comparison does bring pressure for change. The latest Stocktake discussion paper cites **"...increasingly adverse press coverage when comparisons are made with recent experiences in private sector occupational schemes"** as one of the drivers in the argument for increasing employee contribution rates.

Investment Report

2003 Performance

LONG TERM PERFORMANCE

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	Annualised 3yrs	5yrs	10yrs
Inflation*	1.9%	2.9%	3.2%	2.5%	3.6%	2.8%	1.8%	2.9%	0.7%	2.9%	2.2%	2.2%	2.5%
Fund Return	31.3%	-3.6%	16.9%	10.4%	14.8%	13.0%	28.2%	-2.5%	-9.7%	-15,4%	-9.4%	1.5%	7.3%
WM All Funds**	28.2%	-3.9%	19.1%	10.7%	16.8%	14.0%	21.3%	-1.3%	-8.9%	-13.9%	-8.2%	1.4%	7.3%
Percentile Ranking 2003 ***	22	18	91	68	73	57	7	64	43	35	48	28	46

At the time of going to press, fully audited 2003 investment returns are not available. But the indications are that it will have been a very strong year. It did not start well. In the first quarter, equity markets continued the slide which had characterised the previous 3 years. The bottom of the cycle seems to have been reached in mid-March however, and through the remainder of the year markets recovered steadily. The Fund is likely to have returned as much as 15% for the year. Approximate asset value at 31st December 2003 is £5,934 million, a huge improvement on the 31st March figure of £4,823 million which appears in the 2002/03 accounts.

MEDIUM TERM PERFORMANCE

1974 was worse, but 2002 was still one of the poorest years on record for equity investors, particularly as the 2 preceding years had also yielded negative returns. Over this period the Strathclyde Fund has fallen a little behind the average UK pension fund. The distinguishing feature of the Fund's investment strategy is that it invests more in equities (company shares as opposed to safer investments such as cash or bonds) than the average fund. The expectation is that equity will produce better returns over the long term. But this will not always be the case in the shorter term. On the plus side, the Fund has maintained a relatively high exposure to property which has performed particularly well.

The table above illustrates how difficult the last few years have been. Annualised returns over 3 years are negative and even over 5 years are only marginally positive. The 10-year average return of 7.3% is more in line with long term expectations.

When the table is updated to include 2003 returns, the longer term figures will improve a little, but they remain sensitive to any further market downturn.

The Fund ranking (out of 100) means that the Strathclyde Fund has finished in the top half of the UK pension funds "league table" over 3, 5 and 10 years.

INVESTMENT STRATEGY

Background

Following the actuarial valuation in 2002, a review of the Fund's investment arrangements was carried out during 2003. Revised arrangements were agreed during a series of meetings of the Strathclyde Pension Fund Sub-Committee during August, and implemented towards the end of the year.

Investment Strategy

The Fund's investment strategy has been revised as follows.

	Existing	Revised
UK Equity	46%	38%
Small Companies	4%	3%
Overseas Equity	28%	29%
North America	6.8%	9.75%
Europe (ex UK)	7.7%	9.75%
Japan	5.3%	3.25%
Pacific	5.0%	3.25%
Emerging Markets	3.2%	3%
Private Equity	3%	5%
Total Equity	81%	75%
Property	8%	10%
Index Linked	4%	3%
UK Gilts	2.5%	3%
Corporate Bonds	2.5%	6%
Overseas Bonds	2%	3%
Total	**100%**	**100%**

The principal features are an increased allocation to property and corporate bonds, and a consequent reduction in equity exposure. Within the equity allocation there was a further shift from UK to overseas, consistent with previous revisions to the Fund's strategy.

Structure

As part of the investment review the Fund tendered a number of large investment mandates during the year. The appointments subsequently made represented a significant step towards more specialist management.

A newly created global bond portfolio will be managed by **Western Asset**, a dedicated bond house with its origins, and much of its present operations, in California. The Western mandate will be a little more aggressive than the fund's existing specialist bond mandate for which **Henderson Global Investors** were retained. Both mandates represent around 5% of total fund assets.

An equity manager search concluded with 3 appointments. **Baillie Gifford**, **Capital International** and **Schroder** will all run global equity mandates but with different regional allocations. Each mandate represents around 15% of total fund value. All 3 managers were already running mandates for the Fund.

The Fund retains **Legal & General** as its passive manager together with **JP Morgan Fleming** and **Gartmore** (small companies), **Aberdeen** (property), **Pantheon** (private equity) and **Genesis** (emerging markets).

A multi-asset portfolio managed by **JP Morgan Fleming** was deleted from the Fund's structure.

OTHER DEVELOPMENTS

Since 1990 the Fund has employed a global custodian - effectively a specialist bank for the Fund's stocks and shares. The expiry of the existing contract at the end of 2002 prompted a full review and open tender for global custody services. The review culminated with the re-appointment of the existing provider, **Northern Trust**.

* Retail Price Index
** Average UK Pension Fund
*** Within the WM All Funds Universe of over 1,000 UK Pension Funds.

STRATHCLYDE PENSION FUND

FUND ACCOUNTS

The Pension Fund's accounts for the year ended 31st March 2003 are presented below.

2001/02 £000	FUND ACCOUNT	2002/2003 £000
68,142	Contributions Receivable from Employees	73,019
142,109	Contributions Receivable from Employers	159,913
8,647	Additional Contributions from Employers	15,093
23,658	Transfers In	24,859
339	Other Income	301
242,895	**Total Member Income**	**273,185**
	FUND PAYMENTS	
180,534	Pensions	186,473
26,169	Lump Sums	33,760
666	Refund of Contributions	791
12,831	Transfers Out	14,275
2,566	Administrative and Other Expenses	2,696
222,766	**Total Member Payments**	**237,995**
20,129	**Net Addition from Dealings With Members**	**35,190**

Pensions and other payments during the year were met from current income, so there was no need to draw down cash from investment portfolios.

	RETURN ON INVESTMENTS	
138,876	Investment Income	138,334
-10,834	Investment Management Expenses	-8,494
-1,218	Overseas Tax	-1,289
-156,195	Change in Market Value of Investments	-1,379,550
-29,371	**Net Returns on Investments**	**-1,250,999**
-9,242	**Net Decrease in the Fund during the year**	**-1,215,809**
	ASSETS STATEMENT	
6,048,441	Opening Net Assets of the Scheme	6,039,199
-9,242	Asset Movement during the Year	-1,215,809
6,039,199	**Closing Net Assets of the Scheme**	**4,823,390**

Anther year of poor investment returns saw a significant fall in the fund's value.

Pension Liberation

SHORT-TERM GAIN EQUALS LONG-TERM MISERY!!!

Pension Liberation or "Trust busting", as it is sometimes referred to, is a practice that some unscrupulous companies are offering as a way to lure members out of their occupational pensions schemes.

The companies offer to convert pension benefits into tax free lump sums which can be paid out immediately. They achieve this by manipulating the common pensions practice of transfer values. Transfer values are part of the normal run of the mill pensions administration. If you transfer your pension rights to a new pension provider, a cash value is calculated and the monetary value is then used by the new provider as a set-up investment or to purchase service credit in your new pension scheme. The companies offering Pension Liberation services arrange a transfer to a fictitious pension scheme, and on receipt of the transfer value, manipulate the rules and allow the bogus pension scheme to release a lump sum payment for a percentage of the long term pension. It all sounds very attractive to people who need ready cash; give up part of a pension which you won't receive until you retire to receive a cash lump sum now.

But as the old expression states, "You get nothing for nothing". The catch is the exorbitant fees that these companies charge for arranging the Pension Liberation. The commission can be as high as 30% of the value of your transfer, and you could also be liable for tax on the total amount. The Occupational Pension Regulatory Authority (OPRA), the pension scheme watchdog, has issued a warning that people may suffer personal losses of up to 70% of the value of their pensions because of these scams, through commission fees to the company and tax payments to the Inland Revenue.

Be very wary if you are approached by any company offering to liberate your pension, and if you are tempted by the promise of short-term gain remember it could lead to long-term misery in retirement.

DO YOU HAVE A SHORTFALL IN YOUR PENSION SERVICE?

Are you aware that 40 years pensionable service with the Local Government Pension Scheme (LGPS) will allow you to retire on half salary?

But don't despair if you can't attain 40 years membership, as there are 2 methods available in the LGPS by which you can make up the shortfall in your pension. The methods are detailed below:-

1. **PURCHASE OF ADDED YEARS**

   You can elect to pay an additional percentage contribution, subject to medical fitness, and purchase service credit with the LGPS. The amount of service you would be allowed to purchase is governed by the amount of service you would attain at your earliest retiral date, your age, and the Inland Revenue restriction of a maximum contribution rate of 15% for pension provision. For further details or a quotation please contact the Strathclyde Pension Fund Office. Contact details are listed on the back page.

2. **ADDITIONAL VOLUNTARY CONTRIBUTIONS (AVC's)**

   You can pay additional contributions to our in-house AVC provider, Prudential, which Prudential will invest on your behalf. On your retirement you would receive details of the value of your accrued AVCs to allow you to purchase an annuity, basically an additional pension. You will have the option at retiral to accept an annuity with Prudential, or to use the 'open-market' option and purchase an annuity from another insurance company. You also have a third option which is to bring your AVC fund into the main scheme, the LGPS, and have it converted into service credit i.e. Years and Days. For further details or a quotation please contact Prudential's 'Pension Connection' number on **0845 607 0077**.

Actuarial Valuation

Results of the 2002 actuarial valuation were better than anticipated....a strong fund with a healthy surplus.

But while the valuation was being carried out, the situation deteriorated as equity markets fell....

In accordance with the Local Government Pension Scheme Regulations, the Fund commissions an actuary to carry out a "health check" every 3 years. The actuary assesses whether the assets of the Fund are sufficient to meet its liabilities (future pensions payments) and how much employers will need to pay into the Fund in future.

The latest valuation was carried out as at 31st March 2002. Results of the valuation were confirmed during February 2003, and a copy of the valuation report was issued to all participating employers. The report is summarised as follows.

RESULTS

Funding Level

As at 31st March 2002 the funding position was as follows.

Fund Assets	£6,050m
Fund Liabilities	£5,594m
Surplus	£456m

This is a very positive result - a funding level of **108%**, broadly unchanged from the last valuation in 1999 when the Fund also had a surplus of around **8%**.

Post Valuation Events

But the actuary was at pains to stress that the funding position had deteriorated between the valuation date and completion of the valuation process, as investment markets fell throughout the remainder of 2002.

Future Service Funding Rate

The Future Service Funding Rate is the cost to employers of pensions benefits which will be earned after the valuation date. The actuary calculated the Future Service Funding Rate as 245% of employee contributions (i.e. for every £1.00 paid by an employee, their employer would need to contribute £2.45). This had reduced a little from the 1999 valuation when the Future Service Rate was 260%.

Employer Contribution Rates

Ordinarily, the existence of a surplus at the valuation date would allow actual employer contribution rates to be set below the Future Service Funding Rate. However, because of the post-valuation fall in the funding level, the actuary recommended that no account should be taken of the surplus. (Reliance on the surplus could leave a funding gap if investment markets failed to recover before the next valuation in 2005).

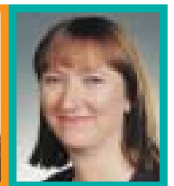
This implied that employers should pay the Future Service Rate. The actuary proposed that the resultant increase should be phased over the period up to the next valuation. The following common contribution rates for employers were agreed.

Year to	Rate (as % of employee contributions)
31st March 2004	230%
31st March 2005	240%
31st March 2006	250%

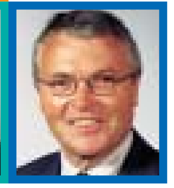
The next actuarial valuation will be carried out as at 31st March 2005.

Strathclyde Pension Fund Sub-Committee Members


Convener Ruth Simpson

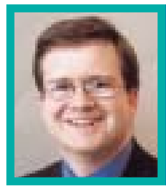

Aileen Colleran


Malcolm Cunning


Eamon Fitzgerald


John Lynch


John Mason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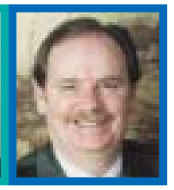
John McKenzie


Malcolm McLean


James McNally

The new Sub-Committee was convened after the May 2003 Council Elections.

WHERE SERVICE COUNTS

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SPFO website......a hit!

The SPFO website is proving to be a firm favourite with members.

From it's introduction in June 2001 to the date of writing the website has had 20,671 "Hits" (Internet terminology for a visitor to a website). After it featured in the last issue of Fundnews the hit count rose dramatically. We are now experiencing more than 200 hits per week, which reflects the level of interest that Pensions are currently generating.

The website contains information on various aspects of the Scheme; online member guides; a ready reckoner benefit calculator; details of fund investments; fund accounts; investment principles; and copies of all reports considered by the Pension Fund Sub-Committee.

The SPFO has been in consultation with scheme Employers regarding hyperlinks from their sites to the SPFO website to allow members easier access. Other planned enhancements to the site include hyperlinks to other pension related sites, such as OPAS, OPRA and LGPS. A facility for online member enquiries and form completion is under development.

So if you haven't already visited the website set your browser to **www.spfo.org.uk** and see what a store of information is available.

Benefit Statement

The provision of Benefit Statements to scheme members has now become an established form of communication from the SPFO. All unitary authority members have received at least one statement, and work is progressing on the production of statements for all other members within the next '3 yearly cycle'.

The latest batch of statements has just been issued to the employees of the employers listed below:-

- Argyll & Bute
- East Ayrshire
- North Ayrshire
- South Ayrshire
- West Dunbartonshire
- East Dunbartonshire
- Inverclyde
- Scottish Enterprise
- Scottish Water
- Strathclyde Police
- Strathclyde Fire

The primary function of the statement is to advise you of the current value of your pension benefits in the LGPS, and to illustrate your future benefits at your retirement based on your current pay.

The statement also has a secondary function as it provides members with the opportunity to identify any erroneous information held on their pension record, and this then allows us to update our database accordingly.

We would therefore ask members to check all their details on receipt of their statement, and if there appears to be any inaccuracies to advise the SPFO by completing the tear off page attached to their statement.

If you are employed by any of the employers listed and did not receive a benefit statement, please contact the SPFO.

Moving House?

If you have moved house recently did you notify the Strathclyde Pension Fund Office?

As the Pension Fund Office is committed to keeping you fully informed about your Pension Rights, we need to have your current home address on file.

All changes of address should be notified to:-

**Strathclyde Pension Fund Office,
Charlotte House, Floor 2,
78 Queen Street, Glasgow G1 3DN**

Alternatively you can e-mail the Pension Fund Office at

spfo@fs.glasgow.gov.uk

PLEASE REMEMBER TO QUOTE YOUR NATIONAL INSURANCE NUMBER ON ANY CORRESPONDENCE, AS THIS IS THE KEY TO YOUR PENSION RECORD.

Help us improve

If you have any comments or suggestions that you feel will help improve the content of our newsletter please let us know. Feedback from Fund members is very important to us and will enable us to shape future issues of Fund News to your requirements.

Please write to:

**Alistair Gray
Senior Communications Officer,
Strathclyde Pension Fund Office,
Charlotte House, Floor 2,
78 Queen Street, Glasgow G1 3DN**

or e-mail **alistair.gray@fs.glasgow.gov.uk**

Any Questions?

If so please contact the Strathclyde Pension Fund Office.

To try to prevent you being passed from one phone extension to another please use the phone number listed for your employer. If none is shown then use the General Enquiries number.

☎ **0141 287 7420**

If you work in:

- Glasgow City Council
- East Dunbartonshire Council
- East Renfrewshire Council
- Strathclyde Fire Brigade
- Strathclyde Buses
- Scottish Water

☎ **0141 287 7341**

If you work in:

- South Lanarkshire Council
- North Ayrshire Council
- South Ayrshire Council
- West Dunbartonshire Council
- Strathclyde Police

☎ **0141 287 7342**

If you work in:

- North Lanarkshire Council
- Argyll & Bute Council
- East Ayrshire Council
- Renfrewshire Council
- Inverclyde Council
- Strathclyde Passenger Transport

☎ **0141 287 7343**