

# **Hermes Group Pension Scheme**

Scheme Registration Number: 10243702

## **Trustee's Annual Report and Financial Statements Year Ended 31 December 2015**

**CONFIDENTIAL**

**3 June 2016**

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# Trustee, Principal Employers and their Advisers

<b>Trustee:</b>	Hermes Pension Trustees Limited
<b>Directors of the Trustee Company</b>	C L Woodley (Chairman) D C Bridges I A Kirby M A Simms D P Bradford
<b>Secretary to the Trustee:</b>	Inside Pensions Limited
<b>Principal Employers:</b>	Hermes Fund Managers Limited BT Pension Scheme Trustees Limited
<b>Actuary:</b>	Ms E Palfreyman Towers Watson Limited
<b>Auditor:</b>	Deloitte LLP
<b>Legal Adviser:</b>	Sackers & Partners LLP
<b>Administrator:</b>	Capita Employee Benefits Limited
<b>Investment Managers:</b>	Legal & General Investment Management Limited Hermes Investment Management Limited Hermes Alternative Investment Management Limited Standard Life Investments Limited Babson Capital Global Investment Funds plc M&G Investment Management Limited Insight Investment Funds Management Limited K2 Advisors L.L.C. (Investor Relations Group)
<b>AVC Investment Managers:</b>	Prudential Assurance Company Limited
<b>Investment Adviser</b>	Hymans Robertson LLP
<b>Custodian:</b>	Northern Trust Limited
<b>Banker:</b>	National Westminster Bank plc
<b>Stewardship Adviser:</b>	Hermes Equity Ownership Services

## Trustee's Mission Statement

The Trustee's mission is to manage the Hermes Group Pension Scheme efficiently in the interests of the members, to provide the expected benefits, and to ensure that an excellent quality of service is given to those members.

## Chairman's Statement

It is a great pleasure to write my fourth report and to give you an update on how the Scheme has progressed during the last year.

The total value of the Scheme's assets rose from £138.6m at 31 December 2014 to £144.0m at 31 December 2015. The return on the Scheme's assets in 2015 was 3%.

In accordance with the Recovery Plan in place at the time, £7.1m of deficit contributions were paid into the Scheme in 2015.

The Scheme's triennial valuation process as at 31 December 2014 progressed throughout 2015 and was signed off in Q1 2016. I am pleased to report that the technical provisions funding level had increased from 73.7% in 2011 to 81.2% and a Recovery plan has been put in place which is expected to achieve full funding on this basis by 31 October 2020. Further information on Scheme funding is included in the Report on Actuarial Liabilities on pages 17 and 18. The Actuary's certification of the Schedule of Contributions relating to this valuation is also included at the end of this Report, along with the certificate that was in place during 2015.

The Trustee continued its work with Hymans Robertson in relation to the development and simplification of the investment strategy. The majority of the Scheme's new strategy was implemented over the course of 2015. In light of the changes, a new Statement of Investment Principles was approved in October 2015.

You will notice that there have been some changes to the way the Report is structured and that there is some new information included. This is because of a change to the pension accounting standards, which means we are now required to include more information on investments, particularly how they are valued and their associated risks.

Finally, I would like to thank the members of the Trustee Board for their sterling work for HGPS over the year.

CAROL WOODLEY

# Trustee's Report

The Trustee of the Hermes Group Pension Scheme ("HGPS", or "the Scheme") has pleasure in presenting its annual report together with the investment report, actuarial statement and certification, summary of contributions, compliance statement and financial statements for the year ended 31 December 2015.

## Scheme Management

### The Scheme

The Scheme is a defined benefit pension scheme and its purpose is to provide retirement benefits for Scheme members and, in the event of a member's death, to provide benefits to their spouse and dependents as prescribed in the rules.

The Scheme was set up by the Principal Employers - Hermes Pensions Management Limited, which is now called Hermes Fund Managers Limited ("Hermes"), and the Trustees of the BT Pension Scheme (now BT Pension Scheme Trustees Limited) - by a Deed made on 16 September 1998. However, the only employer of members is Hermes Fund Managers Limited.

Members of HGPS were contracted out of the State Second Pension (S2P) while they contributed to HGPS.

The Scheme is a registered pension scheme under the Finance Act 2004. This means that members, their employer and the Scheme benefit from favourable tax treatment.

### The Trustee

The Trustee is a trustee company limited by guarantee which acts as Trustee for the Scheme, and is independent of the Principal Employers. A list of the Trustee Directors at 31 December 2015 is shown on page 2 of the report.

The independent Chairman during 2015 was Carol Woodley. Two of the Trustee Directors, David Bridges and Douglas Bradford, were elected by the members. Two of the Trustee Directors, Ingrid Kirby and Matthew Simms, were nominated by the Principal Employers. Irrespective of who appoints them, the Directors act collegiately in the best interests of all of the members of the Scheme.

Details of the provisions relating to the power to appoint and remove Trustee Directors and on the normal term of office are included in the Appendix.

In 2015 the Trustee met a total of 7 times. The Trustee has a calendar of business which enables it to carry out its duties and monitor the performance of all aspects of the Scheme.

The Trustee is supported by a secretariat function which is provided by Inside Pensions, whose contact details are: Inside Pensions, Third Floor, 54-56 Victoria Street, St Albans, Hertfordshire, AL1 3HZ.

## Scheme Management (continued)

### **Scheme Advisers**

The names of the professional advisers to the Trustee and other individuals and organisations who have acted for or were retained by the Trustee during the year are listed on page 2.

The Trustee usually meets each of them at least once each year, and a formal review usually occurs triennially. Earlier reviews will be arranged if problems arise or an adviser resigns. At the triennial reviews the Trustee decides if it is necessary to arrange for a tendering process, or if the incumbent adviser is to be retained.

The Trustee has a contract with Hermes Equity Ownership Services Limited ("HEOS") for the provision of share voting services on behalf of HGPS. The Scheme pays HEOS a fee for this service.

The Auditor, Deloitte LLP, does not provide any non-audit work for the Scheme. However, they do undertake audit and non-audit work for the Principal Employers. The Trustee has arrangements in place to enable it to be satisfied about the independence of the Auditor.

### **Scheme Administration**

Capita Employee Benefits Limited ("Capita") maintains the membership records of the Scheme, calculates benefits, and deals with other administrative matters. Capita also provides accounting and pension payroll services.

The administrator's full address is:

Capita Employee Benefits Limited  
PO Box 323  
Whitstable  
CT5 9BY

Telephone number: 01227 771445  
Fax number: 01227 771466  
Email: hermes.pensions@capita.co.uk

### **Changes to the Scheme Rules**

During 2015 there was one amendment to the Scheme's trust documents which was to provide equivalent benefits to dependants arising from same-sex marriages as to those arising from opposite-sex marriages.

### **Scheme Governance**

The Trustee conducts itself in accordance with the Myners principles (as updated in 2008) and Regulatory guidance from The Pensions Regulator.

The Trustee Board meets at least quarterly and all investment decisions are considered by the entire Board. The Trustee has an Audit Committee, a Communication Sub-Group and other ad hoc committees have been established from time to time when necessary.

The Trustee Directors receive training appropriate to their needs, and they continue to assess whether they have the right set of skills both individually and collectively with regular reviews.

The Trustee has a business plan, which it reviews at each meeting.

## Scheme Management (continued)

### **Scheme Governance (continued)**

The benefits administrator for HGPS is Capita Employee Benefits Limited. Its performance is measured against a number of service level targets and the Trustee Board monitors performance regularly.

The Trustee Board, Audit Committee and Communications Sub-Group are supported by a professional secretariat firm, Inside Pensions. The Trustee Board monitors the performance of Inside Pensions regularly.

### **Audit Committee**

An Audit Committee aids the Trustee's oversight of the Scheme's financial controls. For 2015 the Committee comprised three Trustee Directors: David Bridges, Ingrid Kirby and Carol Woodley, who is the Chairman.

The Committee generally meets twice each year. The Committee considers the Annual Report and Financial Statements before it is finally approved by the Trustee Board, and meets with the external auditor and Capita. The Committee regularly considers a number of areas of the Scheme's operations including financial control, risk assessment, and the effectiveness of the audit process, and makes recommendations to the full Trustee Board where necessary. At every meeting, the Committee discusses a risk assessment report for HGPS.

When considering the risks to the Scheme, the Audit Committee takes into account both financial and reputational risks and what can be done to reduce them through additional controls. The Committee employs the use of a traffic light system to represent the combination of Impact and Likelihood, for example red indicates risks where both the Impact and Likelihood are high. The latest risk assessment resulted in all the risks being considered "amber" or "green". Although the Trustee Board would wish all the risks to be 'green', there are some that will never be 'green' because any control the Trustee puts in place will not reduce the risk altogether.

### **Contributions**

The Schedule of Contributions dated 11 July 2012 required the Employer to meet the annual cost of Scheme expenditure incurred in a financial year by an additional contribution payment. Under that Schedule, the Employer was required to pay a contribution of £600,000 per year towards Scheme Expenditure, with any shortfall in contributions required to be paid to the Scheme by the end of the following financial year.

As reported in the financial statements for the year ending 31 December 2014, the Scheme was due an additional £125,000 in expenses contribution to be settled by the Employer by 31 December 2015. However, due to an administrative error, payment was not made until 26 April 2016. The auditor's statement about contributions has been qualified in respect of this late payment.

At 31 December 2015, as reported in the financial statements (note 18) the shortfall contribution had increased to £447,000 including the above amount relating to the 2014 financial year.

The new Schedule of Contributions, dated 24 March 2016, has a similar arrangement whereby the Employer is required to pay a total of £600,000 per year towards Scheme Expenditure, with any shortfall in contributions required to be paid to the Scheme by the end of the following financial year.

The Trustee has put in place a process to ensure the Scheme receives full settlement in respect of the 2015 expenses contribution shortfall by 31 December 2016 and in each subsequent year thereafter.



## Scheme Management (continued)

**Financial Statements and Financial Development**

The financial statements included in this annual report are the accounts required by the Pensions Act 1995 and have been prepared and audited in compliance with regulations made under sections 41(1) and (6) of that Act.

The financial development of the Scheme during the year ended 31 December 2015 can be summarised as follows:

	<b>£000's</b>
Contributions receivable and transfers in	9,293
Member related costs	(5,721)
Administrative expenses	(909)
<b>Net additions from dealings with members</b>	<b>2,663</b>
Investment income	729
Change in market value of investments	2,164
Investment management expenses	(153)
<b>Net returns on investments</b>	<b>2,740</b>
<b>Net increase in the Scheme during the year</b>	<b>5,403</b>
Scheme value as at 1 January 2015	138,642
<b>Scheme value as at 31 December 2015</b>	<b>144,045</b>

Significant developments affecting the financial position of the Scheme during the year included the receipt of employer deficit contributions of £7.1m paid in accordance with the Scheme's Schedule of Contributions.

## Membership and Benefits

### Scheme Membership

The change in membership during the year was as follows:

	Employed deferred members*	Deferred	Pensioners	Totals
<b>At 31 December 2014 - as reported</b>	<b>81</b>	<b>401</b>	<b>140</b>	<b>622</b>
Prior year adjustment	(1)	(1)	3	1
<b>At 31 December 2014 – as amended</b>	<b>80</b>	<b>400</b>	<b>143</b>	<b>623</b>
<b>Changes in the year:</b>				
Left employment	(11)	11	-	-
Transfers-out	-	(2)	-	(2)
New retirement pensions	(3)	(10)	13	-
Dependant pension	-	-	1	1
Deaths	-	(1)	(2)	(3)
<b>At 31 December 2015</b>	<b>66</b>	<b>398</b>	<b>155</b>	<b>619</b>

\* When the Scheme closed to future benefit accrual on 31 October 2011 the active members became 'employed deferred members'.

The prior year adjustment relates to three pensioner member movements relating to the prior year where member notifications were received subsequent to the year end. The additional member relates to a pension credit arising from a 2014 pension sharing order completed in 2015.

### Benefits

For active members who joined HGPS from 1 April 1999 onwards, benefits for pensionable service from 1 January 2009 were based on career average revalued earnings. Benefits for these members accrued before 1 January 2009 are based on final salary. All benefits for members who joined prior to 1 April 1999, i.e. former members of the Hermes Pension Scheme, are based on final salary.

Lump sum death benefits payable from HGPS on the death of Employed Deferred Members if they die before taking their benefits is 1.25 times pensionable salary. This is not insured.

### Added Years and Additional Voluntary Contributions

Until 31 October 2011 active members of the Scheme were able to purchase increased benefits in two ways:

- i) by buying added years of pensionable service in the Scheme by paying an additional percentage of salary during their active membership; and
- ii) by making additional voluntary contributions (AVCs) to a with-profits fund managed by Prudential Assurance Company Limited.

From 1 November 2011 these options ceased.

## Membership and Benefits (continued)

### Benefits (continued)

There was also an earlier option to pay AVCs to a Santander deposit account. Members can no longer pay AVCs or any contributions to HGPS. The members who paid AVCs to the Prudential or Santander retain their investment in the fund which can be used to provide additional benefits when they retire. The added years benefit a member purchased up to 31 October 2011 is included in their main HGPS benefits.

### Pension Increases

#### Former Hermes Pension Scheme Members Who Joined Pre-1 April 1999

Pensions in payment and deferred pensions are increased in April each year in line with the Government's pension increase orders, in the same way that public sector pensions are increased. In practice these increases are currently based on Consumer Prices Index (CPI) inflation for the twelve months ending the previous September, and there is no cap on the increases. Pensions in payment and deferred pensions increased by 1.2% from April 2015.

#### Members Who Joined Post-1 April 1999

Pensions in payment are increased each April in line with Retail Prices Index (RPI) inflation for the twelve months ending the previous September, up to a maximum of 5% each year. Pensions in payment increased by 2.3% from April 2015.

Deferred pensions are revalued up to retirement in line with government legislation. In practice these increases in deferment are currently based on CPI inflation for the twelve months ending the previous September. The increases are capped at 5% per annum for benefits earned before 6 April 2009 and at 2.5% per annum for benefits earned on or after 6 April 2009. The cap is applied cumulatively across the whole period of deferment not in respect of each individual year. The CPI increased 1.2% in the year from September 2014 to September 2015.

No discretionary increases were awarded during the year.

### Transfers

It is the responsibility of the Trustee to take the decisions on which the calculation of cash equivalent transfer values (CETVs) is based. Transfer values represent fair value in relation to the alternative benefits payable. No allowance is made for any discretionary increases to pensions. When the Scheme closed to future benefit accrual on 31 October 2011 the Trustee ceased to accept transfers-in of benefits from other pension schemes. However, the Trustee and the Employer did agree that Employed Deferred Members may transfer in benefits from the Hermes Group Stakeholder Pension Plan if they take their pension when they retire, if employed by Hermes at that time. The transfer amount from the stakeholder plan can then be used to increase the defined benefit pension and / or cash payable from HGPS on terms determined by the Trustee in agreement with the Employer.

## Investment Management

### Overview

The Trustee, with the assistance of its appointed investment adviser, determines the overall investment strategy for the Scheme and sets out the broad policy to be adopted by each of the appointed fund managers.

### Investment Managers

The names of those who have managed the Scheme's investments during the year are listed on page 2. The Trustee has delegated the day-to-day management of investment to its appointed fund managers. A written agreement between the Trustee and each manager sets out the terms on which the manager will act.

The Trustee believes that environmental, social and governance considerations are among the factors which the Scheme's active investment managers should take into account, where relevant, when selecting investments. The Trustee expects that the extent to which these considerations may have a fundamental impact on the portfolio will be taken into account by the investment managers as part of their delegated duties. The Trustee's policy is to consider the managers' policy as part of the manager selection process, and then to leave implementation to their discretion.

### Investment Principles

In compliance with Section 35 of the Pensions Act 1995, the Trustee maintains a Statement of Investment Principles ("SIP"), which sets out its policy for investing the assets of the Scheme. Any member of the Scheme who would like a copy of the current SIP should contact the Scheme Secretary, at the address on page 19. A copy is also available on the HGPS website at [www.hermes.co.uk/hgps/investment.htm](http://www.hermes.co.uk/hgps/investment.htm).

### Departures from SIP

To the best of its knowledge, the Trustee can report that there have been no departures from the SIP by the Scheme's investment managers during the year ended 31 December 2015.

### Employer Related Investment

Other than the late contributions referred to in the Summary of Contributions on page 39, which under applicable regulations constituted employer related investments for the period under which they remained unpaid past due, there have been no employer related investments during the year.

### Investment Strategy

All of the Scheme's assets are held in pooled investment vehicles to improve diversification.

While it is correct for accounting purposes to treat the pooled investment vehicles in the financial statements as a single line, the Trustee nevertheless considers that for asset-mix purposes the values of the underlying funds should be used to determine sector exposure and the following tables and charts have been drawn up on that basis.

A significant proportion of the exposure is obtained via a Legal & General unitised insurance policy whose value is determined by the performance of the underlying funds.

## Investment Management (continued)

### Investment Strategy (continued)

At the end of 2015 HGPS had investments in the following funds managed by Legal & General:

- World Developed Equity Index
- FTSE RAFI All World 3000 Equity
- A mixture of leveraged gilt funds and leveraged index-linked gilt funds (together, the 'Liability Driven Investment' (LDI) funds).

The value of the Legal & General funds held on behalf of the Scheme at 31 December 2015 was £67.2 million.

The remaining funds held by the Scheme at 31 December 2015 were as follows:

<b>Asset Class</b>	<b>Fund</b>
Equities:	Hermes Global Emerging Markets Fund
Multi asset:	Insight Broad Opportunities Fund
Diversified credit:	Babson Global High Yield Strategies Fund and M&G Illiquid Credit Opportunities Fund
Property:	Hermes Property Unit Trust and Standard Life Long Lease Property Fund

By the end of 2015, the Scheme's investments in the following funds had been fully divested in order to fund the new investments in line with the Scheme's long-term strategic asset allocation:

- Legal & General UK Equity Index Fund
- Legal & General World Emerging Market Equity Index Fund
- Legal & General Active Corporate Bond – Over 10 Year Fund
- BlackRock UK Property Fund
- K2 Overseas Investors Fund

Note that in relation to the redemption of the K2 Overseas Investors Fund, 90% of the expected proceeds has been distributed to the Scheme (with the remainder expected to be received around June 2016), in accordance with the investment manager's disinvestment policy.

At the end of 2015, the Hermes Group of Companies were involved in managing two HGPS portfolios, with Hermes Alternative Investment Management Limited managing the Hermes Property Unit Trust and Hermes Investment Management Limited managing the Hermes Global Emerging Markets Fund.

The Trustee reviews the performance of all the investment managers and funds regularly.

## Investment Management (continued)

### Custodial Arrangement

The Trustee considers that it is important to keep the investment management of its assets separate from their custody, to minimise the risk of the assets being misused. For pooled funds it is the responsibility of the fund manager to appoint and monitor custodians. Northern Trust previously acted as custodian for non-pooled arrangements but its services were terminated as at 31 December 2015 reflecting the fact that there were no longer any segregated assets. The services undertaken by Northern Trust will now be carried out by Capita who operate the Trustee bank account to make and receive payments for the Scheme.

### Investment Performance

The Trustee continues to monitor investment performance against Scheme benchmarks. The overall benchmark return is obtained by combining the strategic asset allocation of the Scheme with the asset class returns of appropriate market indices.

Over the year the overall investment return for HGPS was 3.0% against the benchmark return of 4.5%

The Scheme's performance in the last five years is shown in the table below:

#### Comparison with benchmark 2011 - 2015

Annual Rate of Return (%)	2011	2012	2013	2014	2015	2011 to 2015 Annualised
<b>HGPS</b>	<b>-0.8</b>	<b>7.8</b>	<b>9.7</b>	<b>12.6</b>	<b>3.0</b>	<b>6.4</b>
Benchmark	-0.5	7.5	7.9	13.2	4.5	<b>6.4</b>
HGPS out/(under) performance of benchmark*	-0.3	0.3	1.8	-0.6	-1.5	<b>0.0</b>

\*The differences in this table are based on an arithmetic approach

Over 2015, the Scheme's passively managed funds (the liability driven investments and equities held with Legal & General) broadly tracked their benchmarks, as expected. The Insight Broad Opportunities Fund and the two diversified credit mandates (the Babson Global High Yield Credit Strategies Fund and the M&G Illiquid Credit Opportunities Fund) delivered negative returns (relative to their respective benchmarks), reflecting the difficult conditions experienced within these markets. Further, as these mandates each have an "absolute return" target to outperform cash, relative returns can be volatile when viewed over the short term.

Offset against this, the Scheme's property funds (Hermes Property Unit Trust and the Standard Life Long Lease Property Fund) delivered positive relative returns, reflecting strong portfolio management initiatives.

Over the five year period from 2011 to 2015, the Scheme returned 6.4% per annum, in line with the benchmark return. For background, over the year to 31 December 2015, the Consumer Prices Index rose by a modest amount (0.2%).

## Investment Management (continued)

**Asset Allocation**

By the end of 2015, the Trustee had completed all of the main transition activity required to implement the long term investment strategy. The long term strategy, expressed through the strategic asset allocations, represents a simplification of the portfolio which is intended to deliver more efficient diversification and to help to meet the Trustee's long term funding targets.

The table below shows the asset allocation at 31 December 2015 and the long term strategic asset mix. The 2014 comparative numbers have been included to highlight the main changes at Scheme level during 2015.

	<b>Long Term Strategic Asset Allocation (%)</b>	<b>Actual Asset Allocation (%) 31 Dec 15</b>	<b>Actual Asset Allocation (%) 31 Dec 2014</b>	<b>Notes</b>
Global developed and emerging market equity	40.0	41.0	44.0	<b>1</b>
Absolute Return	-	0.4	4.0	<b>2</b>
Multi asset (active)	20.0	17.2	-	<b>3</b>
Property (Active)	10.0	13.1	14.0	
Diversified credit	15.0	13.6	15.0	
LDI (passive)	15.0	14.1	16.0	
Cash	-	0.6	7.0	
	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	

**Notes:**

1. The reorganisation of the Scheme's equity portfolio was completed during 2015. Following the reorganisation, the Scheme has a target allocation of 8% to an emerging market equity mandate with Hermes (actively managed) and a target allocation of 32% to a global equity mandate with Legal & General (passively managed).
2. The allocation at the end of 2015 reflects the residual amount (10% of the redemption value) expected to be received from K2 Advisors around June 2016 following redemption of the K2 Overseas Investors Fund.
3. The initial investment in multi asset was completed in 2015. It is intended that the actual holding will be brought closer to its long term target allocation of 20% using available cashflows in accordance with the Trustee's Cashflow Policy.

## Compliance Matters

The purpose of this Statement is to provide information, which is required to be disclosed in accordance with Schedule 3 of The Occupational Pension Schemes (Disclosure of Information) Regulations 1996 or voluntarily by the Trustee. The information deals with matters of administrative routine.

### **Transfer Values**

Transfer values are calculated and verified as required under the provisions of the Pensions Act 1993.

### **Internal Dispute Resolution Procedure**

The Trustee has found that most queries or requests for information about the Scheme are capable of being answered satisfactorily by Capita Employee Benefits Limited or the Scheme Secretary.

Nevertheless the Trustee has a procedure to resolve disputes, which gives a member the means of having a grievance considered at the highest level.

The Internal Dispute Resolution Procedure (IDRP) is in two stages. At stage 1, the dispute/complaint is considered by the Secretary to the Trustee. A member not satisfied with the decision can ask at stage 2 for the matter to be reconsidered by the Trustee Board.

A member of the Scheme who has a query or complaint which is likely to prove difficult to resolve is given a copy of the IDRP. A copy of the procedure can be obtained from the Secretary to the Scheme at the address shown on page 21 of this report.

### **The Pensions Advisory Service (“TPAS”)**

TPAS is available to assist members and beneficiaries of the Scheme in connection with difficulties which they have failed to resolve with the Trustee or Administrator of the Scheme. TPAS may be contacted at 11 Belgrave Road, London, SW1V 1RB

### **Pensions Ombudsman**

The Pensions Ombudsman may investigate and determine any complaint or dispute of fact or law in relation to an occupational pension scheme and can be contacted at 11 Belgrave Road, London, SW1V 1RB.

### **Pensions Regulator**

The Pensions Regulator is able to intervene in the running of schemes where trustees, Employers or Professional Advisers have failed in their duties.

The Pensions Regulator may be contacted at Napier House, Trafalgar Place, Brighton, BN1 4DW.

### **Pension Tracing**

A pension tracing service is carried out by the Department for Work and Pensions. The Pension Tracing Service can be contacted at The Pension Service 9, Mail Handling Site A, Wolverhampton, WV98 1LU



## Statement of Trustee's Responsibilities

### **Trustee Responsibilities in Respect of the Financial Statements**

The financial statements, which are prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including the Financial Reporting Standard applicable in the UK and Republic of Ireland ("FRS102"), are the responsibility of the Trustee. Pension scheme regulations require the Trustee to make available to Scheme members, beneficiaries and certain other parties, audited financial statements for each Scheme year which:

- show a true and fair view of the financial transactions of the Scheme during the Scheme year and of the amount and disposition at the end of that year of the assets and liabilities, other than liabilities to pay pensions and benefits after the end of the Scheme year;
- state whether applicable United Kingdom Accounting Standards, including FRS 102, have been followed, subject to any material departures disclosed and explained in the financial statements; and
- contain the information specified in Regulations 3 and 3A of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996.

The Trustee has supervised the preparation of the financial statements and has agreed suitable accounting policies, to be applied consistently, making any estimates and judgements on a prudent and reasonable basis.

The Trustee is also responsible for making available certain other information about the Scheme in the form of an Annual Report.

The Trustee also has a general responsibility for ensuring that adequate accounting records are kept and for taking such steps as are reasonably open to it to safeguard the assets of the Scheme and to prevent and detect fraud and other irregularities including the maintenance of an appropriate system of internal control.

### **Trustee Responsibilities in Respect of Contributions**

The Trustee is responsible under pension legislation for ensuring that there is prepared, maintained and from time to time revised a Schedule of Contributions showing the rates of contributions payable towards the Scheme by or on behalf of the Employer and the active members of the Scheme and the dates on or before which such contributions are to be paid.

The Trustee is also responsible for keeping records in respect of contributions received in respect of any active member of the Scheme and for monitoring whether contributions are made to the Scheme by the Employer in accordance with the Schedule of Contributions. Where breaches of the Schedule occur, the Trustee is required by the Pensions Acts 1995 and 2004 to consider making reports to The Pensions Regulator and the members.

## Report of Actuarial Liabilities

As required by Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" (FRS102), the financial statements do not include liabilities in respect of promised retirement benefits.

Under Section 222 of the Pensions Act 2004, every scheme is subject to the Statutory Funding Objective, which is to have sufficient and appropriate assets to cover its technical provisions. The technical provisions represent the present value of the benefits members are entitled to based on pensionable service to the valuation date, assessed using the assumptions agreed between the Trustees and the Employer and set out in the Statement of Funding Principles, which is available to Scheme members on request.

The most recent full actuarial valuation of the Scheme was carried out as at 31 December 2014. This showed that on that date:

The value of the Technical Provisions was: £170.7 million

The value of the assets at that date was: £138.6 million

The method and significant actuarial assumptions used to determine the technical provisions are as follows (all assumptions adopted are set out in the Appendix to the Statement of Funding Principles):

### Method

The actuarial method to be used in the calculation of the technical provisions is the Projected Unit Method.

### Significant actuarial assumptions

**Discount interest rate:** 4.6% per annum pre-retirement and 3.05% per annum post-retirement at 31 December 2014.

The discount rate for liabilities prior to retirement differs from the discount rate for liabilities after retirement to reflect the expected change in the investment strategy as the Scheme matures. For liabilities pre-retirement the discount rate assumes a notional portfolio of assets which is heavily weighted in return seeking assets. For liabilities post-retirement the discount rate assumes a notional portfolio of assets which is heavily weighted in matching assets.

The expected return on the return seeking assets in the discount rate assumptions was set based on a realistic asset return model at a level of prudence deemed appropriate. The expected returns on the matching assets in the discount rate assumptions was set with reference to the yields on matching assets expected to be held.

**Future Retail Price inflation (RPI):** 3.3% per annum at 31 December 2014. The RPI assumption takes into account information available in respect of bond markets at the effective date of the actuarial valuation and data published by the Bank of England.

**Future Consumer Price inflation (CPI):** 2.3% per annum at 31 December 2014. The assumption for future CPI is set by reference to the RPI assumption and allows for a prudent view of the expected long term gap between RPI and CPI (at 31 December 2014, this long term gap was set at 1.0% per annum).

**Pension increases:** derived from the rates for future retail and consumer price inflation allowing for the caps and floors on pension increases according to the provisions in the Scheme's rules.

## Report of Actuarial Liabilities (continued)

### Significant actuarial assumptions (continued)

**Pay increases:** general pay increases of 2.5% for the first year and in line with consumer price inflation each year thereafter.

**Mortality:** SAPS Light ("S2 Light normal health pensioner tables") series with a 95% multiplier for males and SAPS ("S2 Normal health pensioner tables") with a 90% multiplier for females, based on member's year of birth and projected from 2007 in line with the CMI 2014 Core Projections model with a long term trend of 1.5% pa.

### Recovery Plan

The valuation of the Hermes Group Pension Scheme as a continuing Scheme revealed a past service deficit as at 31 December 2014 of £32.1 million. To eliminate this deficit, the Employer is making a series of additional contributions, as set out in the Schedule of Contributions, which are targeted to eliminate the deficit by 31 October 2020.

Taken in conjunction with the assumed rate of investment return on the invested assets, Ms Palfreyman certified that she expected the target of full funding against the ongoing valuation assumptions to be achieved on payment of the above contributions.

The Employer has also agreed to make further special contributions, if applicable, to meet the strains which arise on account of redundancies or early retirements of active-deferred members.

In the unlikely event that the Employer ceased paying contributions to the Scheme ("discontinuance"), the Trustee could seek to meet benefits payments either by winding up the Scheme or by continuing it as a closed fund. The terms available from insurance companies at 31 December 2014 were such that, based on the Scheme's assets and liabilities at that date, the premiums charged to secure accrued rights in full would have exceeded the value of the Scheme's assets.

### Actuarial Valuation

The next actuarial valuation of the Scheme will be carried out with an effective date no later than 31 December 2017. It is anticipated that the results will be available in 2018 or early 2019.

## Contact for Further Information

Members who have a general query about this report or HGPS in general, should contact Inside Pensions at the following address:

The Secretary of the Hermes Group Pension Scheme  
Inside Pensions  
54-56 Victoria Street  
St Albans  
AL1 3HZ

Telephone: 01727 733150

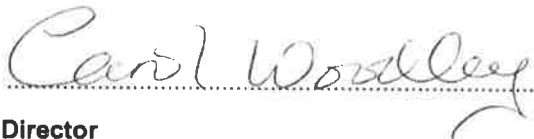
Email: [rachael.fortescue@insidepensions.com](mailto:rachael.fortescue@insidepensions.com)

Further information on HGPS is available on the Scheme's website [www.hermes.co.uk/hgps](http://www.hermes.co.uk/hgps).

Members seeking information about their own benefits are referred to the Scheme's Administrators, Capita. Their contact details can be found on page 6.


## Approval of the Trustee's Report

The Trustee's Report was approved by the Trustee Board on 10 JUNE 2016 and signed on its behalf by:

  
.....

Director

Date: 10 JUNE 2016  
.....

  
.....

Director

Date: 10 JUNE 2016  
.....

# Independent Auditor's Report

## To the Trustee of the Hermes Group Pension Scheme

We have audited the financial statements of Hermes Group Pension Scheme for the year ended 31 December 2015 which comprise the Fund Account, the Statement of Net Assets and the related notes 1 to 24. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the Trustee, as a body, in accordance with regulation 3 of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 made under the Pensions Act 1995. Our audit work has been undertaken so that we might state to the Trustee those matters we are required to state to it in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Trustee as a body, for our audit work, for this report, or for the opinions we have formed.

### **Respective Responsibilities of the Trustee and the Auditor**

As explained more fully in the Trustee's Responsibilities Statement, the Scheme's Trustee is responsible for the preparation of financial statements which give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### **Scope of the Audit of the Financial Statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Scheme's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Trustee; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Independent Auditor's Report  
To the Trustee of the Hermes Group Pension Scheme (continued)

**Opinion on Financial Statements**

In our opinion the financial statements:

- show a true and fair view of the financial transactions of the Scheme during the year ended 31 December 2015, and of the amount and disposition at that date of its assets and liabilities, other than the liabilities to pay pensions and benefits after the end of the year;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- contain the information specified in Regulations 3 and 3A to the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, made under the Pensions Act 1995.

*Deloitte LLP*

Deloitte LLP  
Chartered Accountants and Statutory Auditor,  
London,  
United Kingdom

Date: *10 June 2016*

## Fund Account

### For the Year Ended 31 December 2015

		2015 £'000	2014 £'000
<b>Contributions and benefits</b>			
Employer contributions		8,550	8,806
<b>Total contributions</b>	3	<u>8,550</u>	<u>8,806</u>
Transfers in	4	743	66
		<u>9,293</u>	<u>8,872</u>
Benefits paid or payable	5	(4,189)	(3,098)
Payments to and on account of leavers	6	(1,532)	-
Administration expenses	7	(909)	(820)
		<u>(6,630)</u>	<u>(3,918)</u>
<b>Net additions from dealings with Members</b>		<u>2,663</u>	<u>4,954</u>
<b>Net returns on investments</b>			
Investment income	8	729	922
Change in market value of investments	9	2,164	14,486
Investment management expenses	10	(153)	(223)
<b>Net returns on investments</b>		<u>2,740</u>	<u>15,185</u>
<b>Net increase in the fund during the year</b>		<u>5,403</u>	<u>20,139</u>
Net assets of the Scheme at start of year		<u>138,642</u>	118,503
<b>Net assets of the Scheme at end of year</b>		<u>144,045</u>	<u>138,642</u>

The accompanying notes on pages 24 to 38 are an integral part of these financial statements.

## Statement of Net Assets

### Available for Benefits as at 31 December 2015

	Note	2015 £'000	2014 £'000
<b>Investment assets:</b>			
Pooled investment vehicles	13	140,710	129,200
AVC investments	14	10	11
Cash deposits		934	9,033
Other investment balances		607	115
<b>Total investments</b>	9	<b>142,261</b>	<b>138,359</b>
<b>Current assets</b>	18	<b>2,203</b>	<b>649</b>
<b>Current liabilities</b>	19	<b>(419)</b>	<b>(366)</b>
<b>Net assets of the Scheme at end of year</b>		<b>144,045</b>	<b>138,642</b>

The financial statements summarise the transactions of the Scheme and deal with the net assets at the disposal of the Trustee. They do not take account of obligations to pay pensions and benefits which fall due after the end of the Scheme year. The actuarial position of the Scheme, which takes into account such obligations for the defined benefit section, is dealt with in the Report on Actuarial Liabilities on pages 17 and 18 of the Annual Report and these financial statements should be read in conjunction with this report.

The notes on pages 24 to 38 form an integral part of these financial statements.

**These financial statements were approved by the Trustee on 10 JUNE 2016 and signed on its behalf by:**

*Carl Woodley*

**C L Woodley (Chairman)**

*Igrid A Kirby*

**I A Kirby (Trustee Director)**



# Notes to the Financial Statements

## 1. Basis of Preparation

The financial statements have been prepared in accordance with the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, Financial Reporting Standard 102 – The Financial Reporting Standard applicable in the UK and Republic of Ireland, the Amendments to FRS 102 – Fair Value Hierarchy Disclosures (March 2016) issued by the Financial Reporting Council and with guidance set out in the Statement of Recommended Practice (Revised November 2014). This is the first year FRS 102 and the Revised SORP have applied to the Scheme's financial statements. The Trustee has elected to early-adopt the changes proposed by the FRC in Amendments to FRS 102 – Fair Value Hierarchy Disclosures to align the reporting standards more consistently with International Financial Reporting Standards (IFRS).

## 2. Accounting Policies

The principal accounting policies of the Scheme, which have been applied consistently in the current and preceding year, are as follows:

### Contributions

Employer deficit funding contributions and other employer contributions payable in respect of Scheme expenses are accounted for on the due dates on which they are payable under the Schedule of Contributions or on receipt if earlier with the agreement of the employer and Trustee.

Employer augmentation contributions are accounted for in accordance with the agreement under which they are payable.

### Payments to Members

Benefits are accounted for in the period in which the member notifies the Trustees of his decision on the type or amount of benefit to be taken, or if there is no member choice, on the date of retiring or leaving.

Pensions in payment are accounted for in the period to which they relate.

Individual transfers in or out of the Scheme are accounted for when member liability is accepted or, discharged which is normally when the transfer amount is paid or received.

### Expenses

Expenses are accounted for on an accruals basis.

### Investment Income

Income from cash and short term deposits is accounted for on an accruals basis.

Income from pooled investment vehicles which distribute income is accounted for on an accruals basis on the date stocks are quoted ex-dividend.

Income from pooled investment vehicles which is reinvested within the funds and is therefore not directly paid to the Scheme, is included within change in market value.

## Notes to the Financial Statements (continued)

### 2. Accounting Policies (continued)

#### Valuation and Classification of Investments

Investment assets and liabilities are included in the financial statements at fair value. Where separate bid and offer prices are available, the bid price is used for investment assets and the offer price for investment liabilities. Otherwise, the closing single price, single dealing price, or most recent transaction price is used.

The methods of determining fair value for the principal classes of investments are:

*Certain pooled investment vehicles* which are traded on an active market are included at the quoted price, which is normally the bid price.

*Unitised pooled investment vehicles* which are not traded on an active market but where the manager is able to demonstrate they are priced daily, weekly or at each month end, and are actually traded on substantially all pricing days, are included at the latest price provided by the manager at or before the year end.

Where the value of a pooled investment vehicle is primarily driven by the fair value of its underlying assets, the net asset value advised by the fund manager is normally considered a fair approximation to fair value unless there are restrictions or other factors which prevent realisation at that value, in which case adjustment is made.

The change in market value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

#### Presentation Currency

The Scheme functional and presentation currency is pounds sterling. Monetary items denominated in foreign currency are translated into sterling using the closing exchange rates at the Scheme year end. Foreign currency transactions are recorded in sterling at the spot exchange rate at the date of the transaction.

## Notes to the Financial Statements (continued)

**3. Contributions**

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
<b>Employer contributions</b>		
Deficit funding	<b>7,138</b>	6,925
Augmentation	<b>350</b>	838
Other - expenses	<b>1,062</b>	1,043
	<b>8,550</b>	8,806

Deficit funding contributions of £7,138,000 per annum were being paid by the Employer into the Scheme for a period of one year in accordance with a recovery plan dated 16 July 2012 in order to improve the Scheme's funding position. For the period 1 January 2016 to 31 March 2016, further deficit contributions of £1.8m were payable.

A new Schedule of Contributions, certified on 24 March 2016, requires the Employer to pay £5.5m in the period 1 April 2016 to 31 December 2016, £7.0m in the year ending 31 December 2017, followed by £5.0m in the years ending 31 December 2018 and 2019. For the period 1 January 2019 to 31 October 2020, a further payment of £4.2m is payable.

Other contributions relate to amounts receivable in respect of the Scheme expenses under the Schedule of Contributions.

Employer augmentation contributions are payable by agreement under the terms of redundancy or in certain cases of early retirement.

**4. Transfers In**

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Individual transfers in from other schemes	743	66
	<b>743</b>	66

**5. Benefits Paid or Payable**

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Pensions	<b>2,817</b>	2,563
Commutations of pensions and lump sum retirement benefits	<b>1,195</b>	535
Purchase of annuities	<b>2</b>	-
Lump sum death benefits	<b>175</b>	-
	<b>4,189</b>	3,098

## Notes to the Financial Statements (continued)

**6. Payments to and on Account of Leavers**

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Individual transfers out to other schemes	<b>1,532</b>	<b>-</b>

**7. Administrative Expenses**

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Administration and processing	<b>541</b>	597
Actuarial fees	<b>264</b>	141
Trustee Director fees	<b>104</b>	82
	<b>909</b>	820

Trustee Director's fees were paid as follows:

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Mr D P Bradford	8	2
Mr D C Bridges	8	8
Ms K Graham	-	2
Mrs I A Kirby	8	8
Mr M Simms	4	-
Mrs C L Woodley (Chairman)	76	62
	<b>104</b>	82

Trustee Director fees in respect of Mrs C L Woodley show an increase of £14,000 compared to 2014. This increase is primarily attributable to an under accrual in the previous year in respect of fees for the quarter ending 31 December 2014, which were paid to Mrs Woodley in January 2015. Of Mrs Woodley's fees stated above of £76,000, an amount of £62,000 relates to 2015.

**8. Investment Income**

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Income from bonds	-	78
Income from pooled investment vehicles	<b>727</b>	835
Interest on cash deposits	<b>2</b>	9
	<b>729</b>	922

## Notes to the Financial Statements (continued)

**9. Investment Reconciliation**

	Value at 1 January 2015 £'000	Purchases at cost £'000	Sales proceeds £'000	Change in market value £'000	Value at 31 December 2015 £'000
Pooled investment vehicles	129,200	41,057	(31,814)	2,267	140,710
AVC investments	11	-	(1)	-	10
	<u>129,211</u>	<u>41,057</u>	<u>(31,815)</u>	<u>2,267</u>	<u>140,720</u>
Cash deposits	9,033			(105)	934
Other investment balances	115			2	607
	<u>138,359</u>			<u>2,164</u>	<u>142,261</u>

**10. Investment Management Expenses**

	2015 £'000	2014 £'000
Administration, management and custody	<u>153</u>	<u>223</u>

Investment management fees are in respect of the funds managed by Legal & General Investment Management Limited (LGIM), and Hermes Real Estate Investment Management Limited. There are no direct fees payable to other funds

Investment expenses included fees paid to HEOS of £470 (2014: £11,281) in respect of Scheme governance services.

**11. Transaction Costs**

Transaction costs are included in the cost of purchases and sale proceeds. Indirect costs are incurred through the bid-offer spread on investments within pooled investment vehicles and charges made within those vehicles. There are no separately identifiable direct costs incurred.

**12. Taxation**

The Scheme is a registered Pension Scheme under Chapter 2 of Part 4 of the Finance Act 2004 and is therefore exempt from income tax and capital gains tax. Tax charges are accrued on the same basis as the investment income to which they relate.

## Notes to the Financial Statements (continued)

**13. Pooled Investment Vehicles**

The Scheme's investments in pooled investment vehicles at the year end comprised:

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Equity	120,371	105,429
Bonds	1,823	4,833
Property	18,516	18,938
	<u>140,710</u>	<u>129,200</u>

**14. Additional Voluntary Contributions (AVC) Investments**

Members' additional voluntary contributions, when received, are invested separately from the main Scheme fund in the form of insurance policies and deposits securing additional benefits on a money purchase basis for those members electing to pay additional voluntary contributions. Members participating in this arrangement each receive an annual statement made up to 31 December confirming the amounts held in their account and the movements in the year. The aggregate amounts of money purchase AVC investments are as follows:

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Santander UK PLC	-	1
Prudential Assurance Company Limited	10	10
	<u>10</u>	<u>11</u>

## Notes to the Financial Statements (continued)

**15. Investment Fair Value**

The fair value of financial instruments has been determined using the following fair value hierarchy:

Level 1	The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date.
Level 2	Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly.
Level 3	Inputs are unobservable for the asset or liability.

The Scheme's investment assets and liabilities have been fair-valued using the above hierarchy categories as follows:

As at 31 December 2015	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
<b>Pooled Investment Vehicles</b>				
Insight - Broad Opportunities	-	-	24,447	24,447
Babson Capital - Global High Yield Credit Strategies	-	-	9,447	9,447
Hermes – Global Emerging Markets	-	11,238	-	11,238
Hermes – Property Unit Trust	-	-	12,130	12,130
Legal & General – FTSE RAFI	-	21,147	-	21,147
Legal & General – Leveraged Index Linked Gilts	-	20,079	-	20,079
Legal & General – World Developed Equity	-	25,950	-	25,950
M&G – Illiquid Credit	-	-	9,886	9,886
Standard Life – Long Lease Property	-	-	6,386	6,386
<b>Total Pooled Investment Vehicles</b>	-	<b>78,414</b>	<b>62,296</b>	<b>140,710</b>
<b>AVC Investments</b>	-	-	<b>10</b>	<b>10</b>
<b>Cash Deposits</b>	<b>934</b>	-	-	<b>934</b>
<b>Other Investment Balances</b>	<b>607</b>	-	-	<b>607</b>
	<b>1,541</b>	<b>78,414</b>	<b>62,306</b>	<b>142,261</b>

## Notes to the Financial Statements (continued)

## 15. Investment Fair Value (continued)

As at 31 December 2014	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
<b>Pooled Investment Vehicles</b>				
Babson Capital - Global High Yield Credit Strategies	-	-	9,331	9,331
Hermes – Property Unit Trust	-	-	10,607	10,607
BlackRock – Property Active	-	-	2,405	2,405
Standard Life – Long Lease Property	-	-	5,927	5,927
Legal & General – FTSE RAFI	-	20,994	-	20,994
Legal & General – Leveraged Index Linked Gilts	-	22,819	-	22,819
Legal & General – UK Equity	-	6,757	-	6,757
Legal & General – World Developed Equity	-	22,207	-	22,207
Legal & General – Corporate Bonds Active	-	1,775	-	1,775
Legal & General – World Emerging Market	-	11,674	-	11,674
M&G – Illiquid Credit	-	-	9,500	9,500
K2 Advisers – Absolute Return	-	5,204	-	5,204
<b>Total Pooled Investment Vehicles</b>	<b>-</b>	<b>91,430</b>	<b>37,770</b>	<b>129,200</b>
<b>AVC Investments</b>	<b>-</b>	<b>-</b>	<b>11</b>	<b>11</b>
<b>Cash Deposits</b>	<b>9,033</b>	<b>-</b>	<b>-</b>	<b>9,033</b>
<b>Other Investment Balances</b>	<b>115</b>	<b>-</b>	<b>-</b>	<b>115</b>
	<b>9,148</b>	<b>91,430</b>	<b>37,781</b>	<b>138,359</b>



## Notes to the Financial Statements (continued)

### 16. Investment Risks Disclosures

FRS 102 requires the disclosure of information in relation to certain investment risks. These risks are set out by FRS 102 as follows:

**Credit risk:** this is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

**Market risk:** this comprises currency risk, interest rate risk and other price risk.

- **Currency risk:** this is the risk that the fair value of future cash flows of a financial asset will fluctuate because of changes in foreign exchange rates.
- **Interest rate risk:** this is the risk that the fair value of future cash flows of a financial asset will fluctuate because of changes in market interest rates.
- **Other price risk:** this is the risk that the fair value of future cash flows of a financial asset will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The Trustee determines its investment strategy after taking advice from a professional investment adviser. The Scheme has exposure to these risks because of the investments it makes in following the investment strategy as detailed below. The Trustee manages investment risks, including credit risk and market risk, using monitoring reports produced by its investment adviser and taking into account the Scheme's strategic investment objectives. Investment objectives and risks are also managed through the investment management agreements in place with the Scheme's investment managers and monitored by the Trustee by regular reviews of the investment portfolio.

Further information on the Trustee's approach to risk management is set out below.

#### **Investment Strategy**

The investment objective of the Scheme is to maintain a portfolio of suitable assets of appropriate liquidity which will generate investment returns to meet, together with future contributions, the benefits of the Scheme payable under the trust deed and rules as they fall due.

The Trustee sets the investment strategy for the Scheme taking into account considerations such as the strength of the employer covenant, the long term liabilities of the Scheme and the funding agreed with the Employer. The investment strategy is set out in its SIP.

The current strategy is to hold:

- a. 15% in investments that move in line with the long term liabilities of the Scheme. This is referred to as Liability Driven Investment (LDI) and comprises gilt and leveraged index-linked gilt funds held with Legal & General, the purpose of which is to hedge against the impact of interest rate and inflation movement on long term liabilities.
- b. 85% in return seeking investments comprising UK and overseas equities (including emerging market equities), investment property, multi-asset / absolute return funds and diversified credit funds.

Notes to the Financial Statements (continued)

16. Investment Risks Disclosures (continued)

Risk Exposures

As the Scheme’s economic exposure to its investments is obtained via pooled funds, it has exposure to the credit and market risks arising from the pooled investment vehicles as well as indirect exposure to the credit and market risks arising from the underlying investments within the pooled investment vehicles.

The Scheme’s pooled investment vehicles comprise the following:

- Unit-linked long term insurance policies;
- Unit trusts; and
- Open ended investment companies.

Each type of arrangement has different regulatory and legal structures, for example whether governed by trust or company law and, therefore, the underlying investments will have differing degrees of protection in the event of insolvency of the pool manager.

The Trustee has considered the extent, if any, to which each of the Scheme’s funds are affected by the direct and indirect risks set out under FRS 102. This is captured pictorially in the table below, which is based on the opinion of the Trustee’s investment adviser:

Pooled investment vehicles	Credit risk		Market risk					
	Direct	Indirect	Currency risk		Interest rate risk		Other price risk	
			Direct	Indirect	Direct	Indirect	Direct	Indirect
Liability Driven Investments	●	●	○	○	○	●	○	○
Equity	●	○	○	●	○	○	○	●
Multi asset	●	◐	○	●	○	◐	○	●
Diversified credit	●	●	○	●	○	◐	○	○
Property	●	○	○	○	○	○	○	●

In the above table, the risk noted affects the vehicle or asset class (●) significantly, (◐) partially or (○) hardly / not at all.

The following section provides further details on the risk exposures and the steps taken by the Scheme to mitigate these risks.

## Notes to the Financial Statements (continued)

**16. Investment Risks Disclosures (continued)****Credit Risk**

The Scheme has direct credit risk in so far as it is dependent on the pooled arrangements to deliver the cashflows which support the units in them held by the Scheme. As the Scheme is wholly invested in pooled investment vehicles, direct credit risk affects all of the Scheme's funds.

Direct credit risk is mitigated by the underlying assets of the pooled arrangements being, in part, ring-fenced from the pooled manager, the regulatory environments in which the pooled managers operate and diversification of investments amongst a number of pooled arrangements. Through the use of its adviser, the Trustee carries out due diligence checks on the appointment of any new pooled investment manager and on an ongoing basis monitors any changes to the regulatory and operating environment of the pooled manager.

The Scheme is also indirectly exposed to credit risks arising on the financial instruments within the pooled arrangements which have credit risk. For example, the Scheme's diversified credit mandate and, to a lesser extent the multi asset strategy, are invested in a range of credit instruments, such as investment grade and non-investment grade debt, and therefore, the Scheme is indirectly exposed to the risk of default of the underlying issuers. In addition, the Scheme is also exposed to the credit risk arising from the financial instruments the manager of the liability driven investment uses in the efficient management of that portfolio; this mostly concerns the use of derivative investments.

The Trustee has considered the indirect credit risk through the choice of funds it uses to carry out the investment strategy and will have an expectation that the investment managers, through their approach to investment, will seek to diversify their holdings on an ongoing basis to minimise the impact of default by any one issuer. The risk is further mitigated by the types of investments held. For example, the Scheme's liability driven investments invests in gilts. Further, the credit risk of the assets within the multi asset and diversified credit mandates is mitigated by the investment managers' continuous analysis of the credit quality of the securities held within these mandates.

**Currency risk**

The Scheme does not have direct currency risk as its interest in the pooled investment vehicles is predominately priced in sterling, the same currency as the Scheme's liabilities.

The Scheme is, however, subject to indirect currency risk as some of the Scheme's investments are held in overseas markets and priced in the local currency. As such the value of the Scheme's assets may be affected favourably or unfavourably by fluctuations in currency rates, relative to sterling. Further, currency risk may arise from investment in derivative instruments exposed to non-sterling currencies. This mainly applies to the Scheme's equity, diversified credit and multi asset mandates.

The Trustee expects that the Scheme's underlying investment managers will review the impact of currency movements in their investment decision making as part of their ongoing management of the portfolios. Where applicable, the investment managers have discretion over whether or not to hedge underlying currency risk based on their views of financial markets.

## Notes to the Financial Statements (continued)

**16. Investment Risks Disclosures (continued)****Interest Rate Risk**

The Scheme's interest in pooled investment vehicles is largely unaffected by movements in interest rates and therefore there is no direct interest rate risk. However, some of the underlying investments within the pooled investment vehicles are exposed to interest rates detailed below and therefore the Scheme has indirect interest rate risk.

The Scheme invests via the liability driven investment portfolio in leveraged fixed interest and index-linked gilts which broadly move in line with the Scheme's liabilities as a consequence of changing interest rates and inflation. The Trustees have set a target allocation to liability driven investments of 15% of the overall portfolio, which is intended to hedge around 30% of the Scheme's interest rate and inflation risk.

In addition, the Scheme is subject to an element of interest rate risk on the underlying holdings within the diversified credit and multi asset mandates. However, the bond assets within these mandates typically have short duration and therefore are less sensitive to changes in interest rates. Further, the investment managers are tasked with taking into account interest rate risk as part of the mandates' holistic risk management approach.

**Other Price Risk**

The Scheme has indirect exposure to other price risk, principally in relation to its return seeking portfolio which includes equities, multi asset and investment property held in pooled vehicles.

The Scheme manages this exposure to overall price movements by constructing a diverse portfolio of investments across various markets. According to the Scheme's Statement of Investment Principles, each investment manager is expected to manage broadly diversified portfolios and to spread assets across a number of individual shares and securities.

## Notes to the Financial Statements (continued)

**17. Concentration of Investments**

The following holdings represented more than 5% of the net assets of the Scheme as at 31 December 2015 and the prior year:

	<b>2015 Market value £000</b>	<b>2015 % of net assets</b>	<b>2014 Market value £000</b>	<b>2014 % of net assets</b>
Legal & General World Developed Equity Index	25,949	18.0	22,207	16.0
Legal & General World Emerging Markets Equity Index	-	-	11,674	8.4
Insight Absolute Broad Opportunities	24,448	17.0	-	-
Legal & General FTSE RAFI All World 3000 Index	21,147	14.7	20,994	15.1
Hermes Property Unit Trust	12,130	8.4	10,606	7.7
Hermes Global Emerging Markets	11,238	7.8	-	-
M&G Illiquid Credit Opportunities Fund	9,886	6.9	9,500	6.9
Babson Capital Global High Yield Credit Strategies Fund	9,447	6.6	9,331	6.7

**18. Current Assets**

	<b>2015 £'000</b>	<b>2014 £'000</b>
Contributions due from employer in respect of:		
Employer other – expense contributions	<b>447</b>	125
Cash balances	<b>1,738</b>	520
Other debtors	<b>18</b>	4
	<b>2,203</b>	649

Employer's other expense contributions represent the shortfall of employer contributions payable towards the expenses incurred by the Scheme in the year. In accordance with the Schedule of Contributions these are payable during the following year.

Of the £447,000 expense contributions due to the Scheme, an amount of £322,000 is payable in respect of the year ended 31 December 2015, with the balance of £125,000 payable in respect of the year ended 31 December 2014.

The Schedule of Contributions requires the 2015 expense contribution debtor of £322,000 to be paid to the Scheme by 31 December 2016.

The 2014 expense contribution debtor of £125,000 was required to be paid to the Scheme by 31 December 2015, but was not received until 26 April 2016, 117 days later than the due date set out in the Schedule of Contributions. Processes have been implemented by the Trustee to ensure that such instances do not reoccur.

## Notes to the Financial Statements (continued)

**19. Current Liabilities**

	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Accrued expenses	182	211
Amounts due to Employer related companies:		
Hermes Fund Managers Limited	4	5
HEOS	-	2
Accrued benefits	175	97
Other creditors	58	51
	<u>419</u>	<u>366</u>

**20. Related Party Transactions**

One Trustee Director earned fees of £76,000 (2014: £62,000) for their services to the Scheme as disclosed in note 7. Of this amount £14,000 (2014: Nil) was payable at the year end date.

Other Trustee Director fees of £28,000 (2014: £20,000) were recharged to the Scheme by Hermes Fund Managers Limited during the year as disclosed in note 7. Of this amount £4,000 (2014: £5,528) was payable at the year end date as disclosed in note 19.

During the year fees of £470 (2014: £11,281) were payable to HEOS in respect of Scheme governance services. Of this amount £nil (2014: £1,800) was payable at the year end date as disclosed in note 19.

At 31 December 2015, the Scheme held investments, on an arm's length basis, with Hermes Investment Management Limited of £11.2m (2014 - £Nil) and with Hermes Alternative Investment Management Limited of £12.1m (2014 - £10.6m).

Hermes Fund Managers Limited, HEOS, Hermes Investment Management Limited and Hermes Alternative Investment Management Limited are related to the Scheme as all form part of the same corporate group as the Principal Employers.

**21. Employer Related Investments**

Other than the late contributions referred to in note 18, on page 36, which under applicable regulations constituted employer related investments for the period under which they remained unpaid past due, there have been no employer related investments during the year.

**22. Contingencies and Commitments**

At 31 December 2015 in the opinion of the Trustee, the Scheme had no contingent liabilities or undrawn commitments (2014: nil).

## Notes to the Financial Statements (continued)

**23. Subsequent Events**

There were no subsequent events requiring disclosure in the financial statements.

**24. Transition to FRS102**

This is the first year that FRS 102 and the Revised SORP have applied to the Scheme's financial statements. The effective date of transition to FRS102 and the Revised SORP was 1 January 2014. There were no transitional adjustments required to be disclosed in respect of the change in accounting policy.

## Summary of Contributions Payable For the Year Ended 31 December 2015

During the year ended 31 December 2015 the contributions payable to the Scheme under the Schedule of Contributions were as follows:

	<b>2015 £000's</b>
Employer's deficit funding contributions	7,138
Additional Employer other contributions in respect of 2015 Scheme expenses:	
- Amounts received	740
- Shortfall due	322
Additional Employer other contributions due in respect of 2014 Scheme expenses	125
Employer's augmentation	350
<b>Contributions required by the Schedule of Contributions as Reported on by the Scheme auditor</b>	<b>8,675</b>
Less: Additional Employer other contributions due in respect of 2014 Scheme expenses and accounted for in the year ended 31 December 2014	(125)
<b>Contributions as per Note 3 of the Financial Statements</b>	<b>8,550</b>

The Schedule of Contributions dated 11 July 2012 required the Employer to meet the annual cost of Scheme expenditure incurred in a financial year by an additional contribution payment. Under that Schedule, the Employer was required to pay a contribution of £600,000 per year towards Scheme Expenditure, with any shortfall in contributions required to be paid to the Scheme by the end of the following financial year.

As reported in the financial statements for the year ended 31 December 2014, the Scheme was due an additional £125,000 in expense contributions to be settled by the Employer by 31 December 2015 in accordance with the Schedule of Contributions dated 12 July 2012. However, due to an administrative error, payment was not made until 26 April 2016, 117 days after the due date.

The auditor's statement about contributions has been qualified in respect of this late payment.

The Trustee has put in place a process to ensure the Scheme receives full settlement in respect of the 2015 expenses contribution shortfall by 31 December 2016 and in each subsequent year thereafter.

Approved by the Trustee on 10 JUNE 2016 and signed on its behalf by:



C L Woodley, Chairman



## Independent Auditor's Statement about Contributions To the Trustee of the Hermes Group Pension Scheme

We have examined the summary of contributions to the Hermes Group Pension Scheme for the Scheme year ended 31 December 2015 on page 39.

This statement is made solely to the Trustee, as a body, in accordance with regulation 4 of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 made under the Pensions Act 1995. Our work has been undertaken so that we might state to the Trustees those matters we are required to state to them in an auditor's statement about contributions and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Trustees as a body for our work, for this statement, or for the opinion we have formed.

### Respective Responsibilities of the Trustee and the Auditor

As explained more fully in the Trustee's Responsibilities Statement, the Scheme's Trustee is responsible for ensuring that there is prepared, maintained and from time to time revised a Schedule of Contributions showing the rates and due dates of certain contributions payable towards the Scheme by or on behalf of the employer and the active members of the Scheme. The Trustee is also responsible for keeping records in respect of contributions received in respect of active members of the Scheme and for monitoring whether contributions are made to the Scheme by the employer in accordance with the Schedule of Contributions.

It is our responsibility to provide a Statement about Contributions paid under the Schedule of Contributions and to report our opinion to you.

### Scope of Work on Statement about Contributions

Our examination involves obtaining evidence sufficient to give reasonable assurance that contributions reported in the attached summary of contributions have in all material respects been paid at least in accordance with the Schedule of Contributions. This includes an examination, on a test basis, of evidence relevant to the amounts of contributions payable to the Scheme and the timing of those payments under the Schedule of Contributions.

### Basis for Qualified Statement about Contributions

As explained on page 39, additional Employer expense contributions relating to the 2014 financial year amounting in total to £125k that were payable by 31 December 2015 were paid on 28 April 2016, 117 days later than the due date set out in the Schedule of Contributions.

### Qualified statement about contributions payable under the Schedule of Contributions

In our opinion, except for the effects of the departure from the Schedule of Contributions described in the Basis for Qualified Statement about Contributions above, contributions for the Scheme year ended 31 December 2015 as reported in the summary of contributions and payable under the Schedule of Contributions have in all material respects been paid at least in accordance with the Schedule of Contributions certified by the actuary on 12 June 2012.



Deloitte LLP

Chartered Accountants and Statutory Auditor  
London, United Kingdom

Date: 10 June 2016

# Actuary's Certification of the Schedule of Contributions

**Name of scheme** Hermes Group Pension Scheme

## **Adequacy of rates of contributions**

1. I certify that, in my opinion, the rates of contributions shown in this schedule of contributions are such that the statutory funding objective could have been expected on 31 December 2011 to be met by the end of the period specified in the recovery plan.
2. I also certify that the rates of contributions shown in this schedule are not lower than I would have provided for had I had responsibility for preparing or revising the schedule, the statement of funding principles and any recovery plan.

## **Adherence to statement of funding principles**

3. I hereby certify that, in my opinion, this schedule of contributions is consistent with the Statement of Funding Principles dated 22 June 2012.

The certification of the adequacy of the rates of contributions for the purpose of securing that the statutory funding objective can be expected to be met is not a certification of their adequacy for the purpose of securing the scheme's liabilities by the purchase of annuities, if the scheme were to be wound up.

**Judith Dingle**

**Fellow of the Institute and Faculty of Actuaries  
Towers Watson Limited**

**21 Tothill Street  
London  
SW1H 9LL**

**16 July 2012**

# Actuary's Certification of the Schedule of Contributions

**Name of scheme: Hermes Group Pension Scheme**

## **Adequacy of rates of contributions**

1. I certify that, in my opinion, the rates of contributions shown in this Schedule of Contributions are such that the Statutory Funding Objective could have been expected on 31 December 2014 to be met by the end of the period specified in the Recovery Plan.
2. I also certify that the rates of contributions shown in this schedule are not lower than I would have provided for had I had responsibility for preparing or revising the schedule, the Statement of Funding Principles and any Recovery Plan.

## **Adherence to statement of funding principles**

3. I hereby certify that, in my opinion, this Schedule of Contributions is consistent with the Statement of Funding Principles dated 24 March 2016.

The certification of the adequacy of the rates of contributions for the purpose of securing that the Statutory Funding Objective can be expected to be met is not a certification of their adequacy for the purpose of securing the Scheme's liabilities by the purchase of annuities, if the Scheme were to be wound up.

**Emma Palfreyman**

**Fellow of the Institute and Faculty of Actuaries  
Towers Watson Limited**

**71 High Holborn  
London  
WX1V 6TP**

**24 March 2016**

# Appendix

## Trustee Arrangements

1. The main provisions relating to the appointment and retirement of Trustee Directors are as follows:
  - there is a minimum of five Trustee Directors, but a sixth Director may be appointed from time to time;
  - two of the Directors are nominated by the Principal Employers, who can also remove them from office;
  - two of the Directors are member-nominated Directors, elected by the active members, deferred pensioners and pensioners;
  - they can be removed from office by the Principal Employers, at the request of the members;
  - in addition there is a Chairman who is appointed by the Principal Employers after consultation with and the agreement of the member-nominated Directors;
  - the Principal Employers fix the Chairman's period of office;
  - the Chairman can be removed from office as Trustee Director and Chairman by the Principal Employers and has to be so removed by the Principal Employers at the request of the member-nominated Directors; and
  - the Principal Employers may from time to time appoint a sixth Trustee Director, who will be "independent", with the consent of the other five Directors. The sixth Director will not be a member of the Scheme, or an employee or ex-employee of any of the Employers participating in the Scheme.
2. A Trustee Director's normal term of office is four years:
  - a Trustee Director can be appointed for a second term giving a normal maximum period of eight years, unless the Principal Employers and the other Trustee Directors agree to a third term;
  - a member-nominated Director who has completed a term of office will be required to seek re-election if he/she wishes to serve for a second or third term;
  - the Chairman's term of office is normally three years with a normal maximum of two terms (i.e. six years), unless the Principal Employers and the other Trustees agree to a third term;
  - for a Trustee Director who subsequently becomes Chairman, the term is limited to a normal maximum of eleven years unless the Principal Employers and other Trustee Directors agree to an extension;
  - Carol Woodley's term of office as Chairman of HGPS was due to expire on 21 December 2015. Both the Principal Employers and the Trustee Board agreed to an extension of her term of office for a further two years to 20 December 2017 under the same terms as the contract previously in place. The extension has arisen as a result of project work being carried out in relation to the Scheme; and

## Trustee Arrangements (continued)

- David Bridges' term of office as a Member-Nominated Director (MND) is due to expire in September 2016. The Trustee Board, along with the Principal Employers, agreed to extend Mr Bridges' term for one year beyond the normal four year term of an MND. The extension has arisen as a result of project work being carried out in relation to the Scheme.