

# **Hermes Group Pension Scheme**

Scheme Registration Number: 10243702

## **Trustee's Annual Report and Financial Statements Year Ended 31 December 2016**

**CONFIDENTIAL**

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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 Willis Towers Watson Limited (formerly 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 (until 21 October 2016) Barings Global Investment Funds 2 plc (from 22 October 2016) M&G Investment Management Limited Insight Investment Funds Management Limited
<b>AVC Investment Managers:</b>	Prudential Assurance Company Limited
<b>Investment Adviser</b>	Hymans Robertson LLP
<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 pleasure to present this report giving you an update on how the Scheme has progressed during the last year.

The total value of the Scheme's assets rose from £144.0m at 31 December 2015 to £181.1m at 31 December 2016. The return on the Scheme assets in 2016 was 24.3%.

In accordance with the Recovery Plan, £7.4m of deficit contributions were paid into the Scheme in 2016.

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 is also included at the end of this Report.

The Trustee continued to review its investment strategy and implemented some de-risking by transferring 10% of Scheme assets from equities and, based on advice from Hymans Robertson, investing the proceeds in the Scheme's existing LDI and multi-credit mandates. The Trustee will look to implement further de-risking as the Scheme matures and opportunities arise.

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 2016.

### 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 2016 is shown on page 2 of the report.

The independent Chairman during 2016 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 2016 the Trustee met a total of 5 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 meets regularly with its advisers and carries out a formal review occurring at least 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 Auditor, Deloitte LLP, does not provide any non-audit work for the Scheme. However, they do undertake 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

### 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 2016 the Committee comprised three Trustee Directors: David Bridges, Ingrid Kirby and Carol Woodley, who is the Chairman.

The Committee generally meets 2 times per 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 Schedules of Contributions dated 16 July 2012 and 24 March 2016 require the Employer to meet the annual cost of the Scheme's administrative expenditure incurred in a financial year.

The Employer pays a contribution of £50,000 per month towards Scheme administrative expenditure, and should this amount, along with other expense related contributions paid to the Scheme, be insufficient to cover the Scheme's annual administrative expenditure, the Employer is required to make an additional one-off expense contribution to cover the shortfall by the end of the following financial year.

For the previous year ended 31 December 2015 the additional one-off contribution payable to the Scheme by 31 December 2016 was reported within current assets (note 18) as £447,000.

Following a review of the calculation of the one-off Employer expense contribution payable, it was determined the Scheme had over-provided for the amount due from the Employer in respect of 2015 by £105,000 due to the incorrect inclusion of investment expenses relating to Legal & General. The Trustee subsequently agreed with the Employer that the previously reported amount payable to the Scheme in respect of 2015 of £447,000 would be reduced to £342,000. The adjusted amount payable of £342,000 was fully settled by the Employer by 31 December 2016 in accordance with the Schedule of Contributions.



## Scheme Management (continued)

### Contributions (continued)

During 2016, the Employer made further expense contributions totalling £715,000, as shown in the Summary of Contributions payable on page 39.

As a result of the adjustment, the reported Employer other expense contributions for the year ended 31 December 2016 of £610,000 as shown in note 3 to the financial statements, is the net of the expense contribution receipts in respect of 2016, and the 2015 over-provided amount of £105,000.

### Financial Statements and Financial Development

The financial statements included in this annual report are the financial statements 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 2016 can be summarised as follows:

	£000's
Contributions receivable and transfers in	7,967
Member related costs	(5,426)
Administrative expenses	(715)
<b>Net additions from dealings with members</b>	<b>1,826</b>
Investment income	832
Change in market value of investments	34,587
Investment management expenses	(168)
<b>Net returns on investments</b>	<b>35,251</b>
<b>Net increase in the fund during the year</b>	<b>37,077</b>
Scheme value as at 1 January 2016	144,045
<b>Scheme value as at 31 December 2016</b>	<b>181,122</b>

Significant developments affecting the financial position of the Scheme during the year included the receipt of employer deficit contributions of £7.4m paid in accordance with the Scheme's Schedules of Contributions.

## Membership and Benefits

### Scheme Membership

The change in membership during the year was as follows:

	Employed deferred members*	Deferred	Pensioners	Totals
At 31 December 2015 - as reported	66	398	155	619
Prior year adjustments	-	(8)	10	2
<b>At 31 December 2015 – as amended</b>	<b>66</b>	<b>390</b>	<b>165</b>	<b>621</b>
<b>Changes in the year:</b>				
Left employment	(8)	8	-	-
Transfers-out	-	(5)	-	(5)
New retirement pensions	(1)	(12)	13	-
Dependant pensions ceased	-	-	(2)	(2)
Deaths	-	-	-	-
<b>At 31 December 2016</b>	<b>57</b>	<b>381</b>	<b>176</b>	<b>614</b>

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

At 31 December 2016, included within total pensioners above are 6 members (2015 as amended: 5 members) who have passed their normal retirement date and who have not yet commenced a drawdown of their pensions.

The deferred prior year adjustment relates to: 2 members who took their benefits in 2016, where their retirement was backdated to prior years; 1 member, who transferred out of the Scheme during 2015, but whose record was not updated until 2016; and, 5 members who had passed their normal retirement date but had yet to drawdown their pension.

The pensioners prior year adjustment relates to: the 2 members referred to above; 3 dependants who were set up in 2016 with their pensions backdated to 2015; and, the 5 members referred to above who are yet to take their benefits.

### 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.

## Membership and Benefits (continued)

### 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.

Members can no longer pay AVCs or any contributions to HGPS. The members who paid AVCs to Prudential, the Scheme's AVC investment manager, 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. As a result, pensions in payment and deferred pensions were not increased from April 2016.

#### 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 0.8% from April 2016.

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 decreased 0.1% 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 decide the basis on which cash equivalent transfer values (CETVs) are calculated. 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 understands that environmental, social and governance considerations are among the factors which the Scheme's active investment managers 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. During the year, a review of the strategic asset allocation was undertaken and a revised SIP reflecting the changes to the allocation was approved by the Trustee in March 2017.

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

The SIP in place as at 31 December 2016 did not reflect the changes to the asset allocation during the year and consequently the asset allocation at the year end, as shown in the table on page 14, represented a departure from that SIP. A revised SIP reflecting these changes was approved by the Trustee in March 2017.

## Employer Related Investment

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 2016 the 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 2016 was £91.5 million.

The remaining funds held by the Scheme at 31 December 2016 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

Over 2016, the Scheme's equity portfolio was partially disinvested as part of strategic changes to the Scheme's assets. The proceeds were reinvested in the existing LDI and diversified credit mandates.

At the end of 2016, 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 Scheme's investment managers and funds regularly.

### 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 previously undertaken by Northern Trust will now be carried out by Capita who operate the sole Trustee bank account to make and receive payments for the Scheme.

## Investment Management (continued)

### 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 24.3% against the benchmark return of 23.2%.

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

#### Comparison with benchmark 2012 - 2016

Annual Rate of Return (%)	2012	2013	2014	2015	2016	2012 to 2016 Annualised*
HGPS	7.8	9.7	12.6	3.0	24.3	11.5
Benchmark	7.5	7.9	13.2	4.5	23.2	11.3
HGPS out/(under) performance of benchmark	0.3	1.8	-0.6	-1.5	1.1	0.2

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

Over 2016, 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 funds (Barings Global High Yield Credit Strategies Fund and the M&G Illiquid Credit Opportunities Fund) delivered positive returns (relative to their respective benchmarks), benefitting from the strong performance of the major asset classes over the year.

In contrast, the Hermes Global Emerging Markets Fund delivered a negative return relative to its benchmark although 12 month performance was strong in absolute terms. The Scheme's property funds (Hermes Property Unit Trust and the Standard Life Long Lease Property Fund) showed a mixed picture in terms of performance relative to their respective benchmarks.

Over the five year period from 2012 to 2016, the Scheme returned 11.3% per annum, outperforming its benchmark return. For background, over the year to 31 December 2016, the Consumer Prices Index rose by a modest amount (1.5%).

## Investment Management (continued)

## Asset Allocation

The table below shows the asset allocation and the long term strategic asset mix as at 31 December 2016 based on the SIP in place at that time. The 2015 comparative numbers have been included to highlight the main changes at Scheme level during 2016.

	Long Term Strategic Asset Allocation (%)	Actual Asset Allocation (%) 31 Dec 2016	Actual Asset Allocation (%) 31 Dec 2015	Notes
Global developed and emerging market equity	30.0	32.0	41.0	1
Absolute Return	0.0	0.0	0.4	2
Multi asset (active)	20.0	16.8	17.2	
Property (active)	10.0	10.8	13.1	
Diversified credit	15.0	15.7	13.6	
LDI (passive)	25.0	24.2	14.1	1
Cash	0.0	0.5	0.6	
	100.0	100.0	100.0	

## Notes:

1. Over 2016, strategic changes were made at the portfolio level, in terms of a switch from equities to LDI, with the target allocation to equities reducing from 40% to 30% and the target allocation to LDI increasing from 15% to 25%, compared to the positions at 31 December 2015.
2. The allocation at the end of 2015 reflects the residual amount (10% of the redemption value) which was expected to be received from K2 Advisors in 2016 following redemption of the K2 Overseas Investors Fund. The money was received in the Trustee Bank Account in mid-June 2016.

## 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 19 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 on 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 Trustee 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 on 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 deficit 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 at the valuation date 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.

### Funding Update

Following the last formal triennial actuarial valuation reported above as at 31 December 2014, the Scheme's overall funding position on a Technical Provisions basis was rolled forward in the actuarial annual update report as at 31 December 2015. While the 2015 report is not as formal as the 2014 report, it shows that the funding position had improved by £0.8m from a deficit of £32.1m to a deficit of £31.3m. This was a result of the payment of employer deficit reduction contributions to the Scheme, offset by interest on the deficit, lower investment returns than assumed, and a change in actuarial basis to reflect economic conditions at 31 December 2015. The actuarial annual update report as at 31 December 2016 will be finalised after these Report and Accounts are signed off, following which the associated Summary Funding Statement will be issued to Scheme members.

## 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

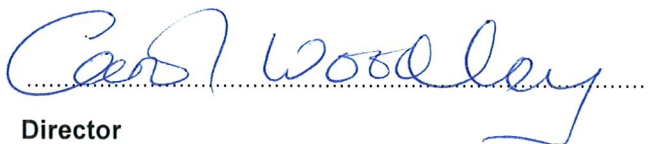
Email: rachael.fortescue@insidepensions.com

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.

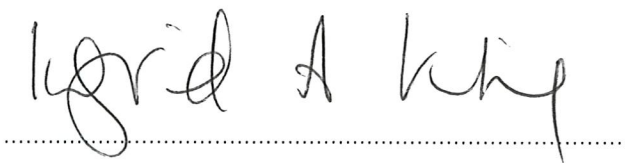
## Approval of the Trustee's Report

The Trustee's Report was approved by the Trustee Board on 11 May 2017 and signed on its behalf by:

  
.....

Director

Date: 11/5/17

  
.....

Director

Date: 11/5/17

# 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 2016 which comprise the Fund Account, the Statement of Net Assets and the related notes 1 to 23. 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) including FRS102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland".

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 2016, 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**  
Chartered Accountants and Statutory Auditor,  
London,  
United Kingdom

Date: 11 May 2017

# Fund Account

## For the Year Ended 31 December 2016

		2016 £'000	2015 £'000
<b>Contributions and benefits</b>			
Employer contributions		7,967	8,550
<b>Total contributions</b>	3	<u>7,967</u>	<u>8,550</u>
Transfers in	4	-	743
		<u>7,967</u>	<u>9,293</u>
Benefits paid or payable	5	(3,396)	(4,189)
Transfers	6	(2,030)	(1,532)
Administration expenses	7	(715)	(909)
		<u>(6,141)</u>	<u>(6,630)</u>
<b>Net additions from dealings with Members</b>		<u>1,826</u>	<u>2,663</u>
<b>Net returns on investments</b>			
Investment income	8	832	729
Change in market value of investments	9	34,587	2,164
Investment management expenses	10	(168)	(153)
<b>Net returns on investments</b>		<u>35,251</u>	<u>2,740</u>
<b>Net increase in the fund during the year</b>		<u>37,077</u>	5,403
Net assets of the Scheme at start of year		<u>144,045</u>	138,642
<b>Net assets of the Scheme at end of year</b>		<u><u>181,122</u></u>	<u><u>144,045</u></u>

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

## Statement of Net Assets

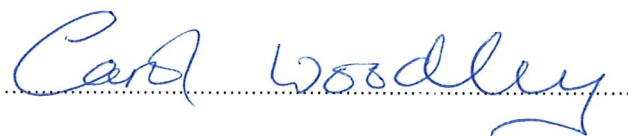
Available for Benefits as at 31 December 2016

	Note	2016 £'000	2015 £'000
<b>Investment assets:</b>			
Pooled investment vehicles	13	180,304	140,710
AVC investments	14	7	10
Cash deposits		-	934
Other investment balances		162	607
<b>Total investments</b>	9	<b>180,473</b>	<b>142,261</b>
<b>Current assets</b>	18	<b>906</b>	<b>2,203</b>
<b>Current liabilities</b>	19	<b>(257)</b>	<b>(419)</b>
<b>Net assets of the Scheme at end of year</b>		<b>181,122</b>	<b>144,045</b>

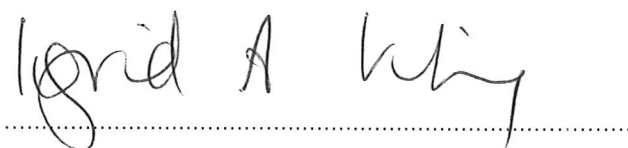
The financial statements summarise the transactions of the Scheme and deal with the net assets at the disposal of the Trustee. They do not take account of obligations to pay pensions and benefits which fall due after the end of the Scheme year. The actuarial position of the Scheme, which takes into account 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 11 May 2017 and signed on its behalf by:**



C L Woodley (Chairman)



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). 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

	2016 £'000	2015 £'000
Employer contributions		
Deficit funding	7,357	7,138
Augmentation	-	350
Other - expenses	610	1,062
	<u>7,967</u>	<u>8,550</u>

In order to improve the Scheme's funding position, 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, and £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.

In addition, the previous Schedule of Contributions certified 16 July 2012, required the Employer to pay deficit contributions of £1.8m for the period 1 January 2016 to 31 March 2016.

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

As reported on page 7 of the Trustee Report, following a review of the calculation of the one-off Employer expense contribution payable, it was determined the Scheme had over-provided for the amount due from the Employer in respect of 2015 by £105,000 due to the incorrect inclusion of investment expenses relating to Legal & General. The Trustee subsequently agreed with the Employer that the previously reported amount payable to the Scheme in respect of 2015 of £447,000 would be reduced to £342,000. The adjusted amount payable of £342,000 was fully settled by the Employer by 31 December 2016.

During 2016, the Employer made further expense contributions totalling £715,000, as shown in the Summary of Contributions payable on page 39.

As a result of the adjustment, the reported Employer other expense contributions for the year ended 31 December 2016 of £610,000 is the net of the expense contribution receipts in respect of 2016, and the 2015 over-provided amount of £105,000.

## 4. Transfers In

	2016 £'000	2015 £'000
Individual transfers in from other schemes	-	743
	<u>-</u>	<u>743</u>

## Notes to the Financial Statements (continued)

## 5. Benefits Paid or Payable

	2016 £'000	2015 £'000
Pensions	3,065	2,817
Commutations of pensions and lump sum retirement benefits	331	1,195
Purchase of annuities	-	2
Lump sum death benefits	-	175
	<u>3,396</u>	<u>4,189</u>

## 6. Transfers Out

	2016 £'000	2015 £'000
Individual transfers out to other schemes	<u>2,030</u>	<u>1,532</u>

## 7. Administration Expenses

	2016 £'000	2015 £'000
Administration and processing	444	541
Actuarial fees	174	264
Trustee Director fees	97	104
	<u>715</u>	<u>909</u>

Trustee Director's fees were paid as follows:

	2016 £'000	2015 £'000
Mr D P Bradford	8	8
Mr D C Bridges	8	8
Mrs I A Kirby	8	8
Mr M Simms	11	4
Mrs C L Woodley (Chairman)	62	76
	<u>97</u>	<u>104</u>

Trustee Director fees in respect of Mrs C L Woodley show a decrease of £14,000 compared to 2015. This decrease is attributable to the inclusion in 2015 of a prior year under accrual in respect of fees for the quarter ended 31 December 2014, which were paid to Mrs Woodley in January 2015. Therefore, of Mrs Woodley's prior year fees above of £76,000, only an amount of £62,000 related to 2015.

All other Trustee Directors each receive a payment of £8,000 per annum. The 2016 fees reported in respect of Mr M Simms include a £3,000 under accrual of his 2015 fees.

## Notes to the Financial Statements (continued)

## 8. Investment Income

	2016 £'000	2015 £'000
Income from pooled investment vehicles	829	727
Interest on cash deposits	3	2
	<u>832</u>	<u>729</u>

## 9. Investment Reconciliation

	Value at 1 January 2016 £'000	Purchases at cost £'000	Sales proceeds £'000	Change in market value £'000	Value at 31 December 2016 £'000
Pooled investment vehicles	140,710	40,658	(35,627)	34,563	180,304
AVC investments	10	-	(3)	-	7
	<u>140,720</u>	<u>40,658</u>	<u>(35,630)</u>	<u>34,563</u>	<u>180,311</u>
Cash deposits	934			8	-
Other investment balances	607			16	162
	<u>142,261</u>			<u>34,587</u>	<u>180,473</u>

At 1 January 2016, the Scheme held cash deposits with Northern Trust, the Scheme's former custodian for non-pooled arrangements, of £934,000. Following a termination of its services at 31 December 2015, the cash deposit balance with Northern Trust was wholly transferred to the Scheme's bank account held with Capita. The 31 December 2016 bank balance held on behalf of the Trustee by Capita is reported as a current asset (note 18) as it is held for operational rather than investment purposes.

## 10. Investment Management Expenses

	2016 £'000	2015 £'000
Administration, management and custody	215	153
Fee rebates	(47)	-
	<u>168</u>	<u>153</u>

## Notes to the Financial Statements (continued)

## 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.

## 13. Pooled Investment Vehicles

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

	2016 £'000	2015 £'000
Equity	58,881	58,334
Bonds	61,136	29,526
Property	19,326	18,516
Illiquid credit	10,636	9,886
Diversified Growth	30,325	24,448
	<u>180,304</u>	<u>140,710</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:

	2016 £'000	2015 £'000
Prudential Assurance Company Limited	<u>7</u>	<u>10</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 have been fair-valued using the above hierarchy categories as follows:

As at 31 December 2016	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
<b>Pooled Investment Vehicles</b>				
Insight – Broad Opportunities	-	30,324	-	30,324
Barings Capital – Global High Yield Credit Strategies	-	17,617	-	17,617
Hermes – Global Emerging Markets	-	10,914	-	10,914
Hermes – Property Unit Trust	-	-	12,653	12,653
Legal & General – FTSE RAFI	-	24,186	-	24,186
Legal & General – Leveraged Index Linked Gilts	-	43,519	-	43,519
Legal & General – World Developed Equity	-	23,782	-	23,782
M&G – Illiquid Credit	-	-	10,636	10,636
Standard Life – Long Lease Property	-	6,673	-	6,673
<b>Total Pooled Investment Vehicles</b>	-	157,015	23,289	180,304
<b>AVC Investments</b>	-	-	7	7
<b>Other Investment Balances</b>	162	-	-	162
	162	157,015	23,296	180,473

## Notes to the Financial Statements (continued)

## 15. Investment Fair Value (continued)

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
Barings 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
Total Pooled Investment Vehicles	-	118,694	22,016	140,710
AVC Investments	-	-	10	10
Cash Deposits	934	-	-	934
Other Investment Balances	607	-	-	607
	1,541	118,694	22,026	142,261

\* The fair value hierarchy allocations previously reported in 2015 have been reviewed in the current year in accordance with recent industry guidance. As a result, certain pooled investments, previously reported as level 3 type investments, have been deemed to be more appropriately allocated as level 2 investments in the opinion of the Trustee.

To aid comparability, the presentation of the 2015 investment fair values above has been aligned with the reported 2016 fair value allocations shown on the previous page.



## 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 strategy at 31 December 2016 was to hold:

- a. 25% 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 leveraged gilt funds 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. 75% 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 table above, the risk noted affects the 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 cash flows 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 LDI portfolio 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. Indirect currency risk 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 LDI 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 LDI of 25% of the overall portfolio, which is intended to hedge close to 50% of the Scheme's interest rate and inflation risk on a Technical Provisions basis.

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, with the exception of UK government securities, represented more than 5% of the net assets of the Scheme as at 31 December 2016 and the prior year:

	<b>2016 Market value £000</b>	<b>2016 % of net assets</b>	<b>2015 Market value £000</b>	<b>2015 % of net assets</b>
Legal & General World Developed Equity Index	<b>23,782</b>	<b>13.1</b>	25,949	18.0
Insight Absolute Broad Opportunities	<b>30,324</b>	<b>16.7</b>	24,448	17.0
Legal & General FTSE RAFI All World 3000 Index	<b>24,186</b>	<b>13.4</b>	21,147	14.7
Barings Capital Global High Yield Credit Strategies Fund	<b>17,617</b>	<b>9.7</b>	9,447	6.6
Hermes Property Unit Trust	<b>12,653</b>	<b>7.0</b>	12,130	8.4
Legal & General 2062 Leveraged Index-Linked Gilt	<b>12,239</b>	<b>6.8</b>	4,806	3.3
Hermes Global Emerging Markets	<b>10,914</b>	<b>6.0</b>	11,238	7.8
M&G Illiquid Credit Opportunities Fund	<b>10,636</b>	<b>5.9</b>	9,886	6.9

## Notes to the Financial Statements (continued)

## 18. Current Assets

	2016 £'000	2015 £'000
Contributions due from employer in respect of:		
Employer other – expense contributions	-	447
Cash balances	877	1,738
Other debtors	29	18
	<u>906</u>	<u>2,203</u>

Employer's other expense contributions receivable represent the shortfall of employer contributions to meet the administrative expenses incurred by the Scheme in each year. In accordance with the Schedule of Contributions these are payable by 31 December of the following year end. At 31 December 2016, no additional contributions were payable to the Scheme.

As reported on page 7 of the Trustee Report, following a review of the calculation of the one-off Employer expense contribution payable, it was determined the Scheme had over-provided for the amount due from the Employer in respect of 2015 by £105,000 due to the incorrect inclusion of investment expenses relating to Legal & General. The Trustee subsequently agreed with the Employer that the previously reported amount payable to the Scheme in respect of 2015 of £447,000 would be reduced to £342,000. The adjusted amount payable of £342,000 was fully settled by the Employer by 31 December 2016. During 2016, the Employer made further expense contributions totalling £715,000, as shown in the Summary of Contributions payable on page 39. As a result of the adjustment, the reported Employer other expense contributions for the year ended 31 December 2016 of £610,000 as shown in note 3 to the financial statements, is the net of the expense contribution receipts in respect of 2016, and the 2015 over-provided amount of £105,000.

## 19. Current Liabilities

	2016 £'000	2015 £'000
Accrued expenses	191	182
Amounts due to Employer related companies:		
Hermes Fund Managers Limited	8	4
HEOS	-	-
Accrued benefits	-	175
Other creditors	58	58
	<u>257</u>	<u>419</u>

## Notes to the Financial Statements (continued)

### 20. Related Party Transactions

One Trustee Director earned fees of £62,000 (2015: £76,000) for their services to the Scheme as disclosed in note 7. Of this amount £12,500 (2015: £14,000) was payable at the year end date.

Other Trustee Director fees of £38,000 (2015: £28,000) were recharged to the Scheme by Hermes Fund Managers Limited during the year as disclosed in note 7. Of this amount £8,000 (2015: £4,000) was payable at the year end date as disclosed in note 19.

During the year fees of £Nil (2015: £470) were payable to HEOS in respect of Scheme governance services and therefore £Nil (2015: £nil) was payable at the year end date.

At 31 December 2016, the Scheme held investments, on an arm's length basis, with Hermes Investment Management Limited of £10.9m (2015: £11.2m) and with Hermes Alternative Investment Management Limited of £12.8m (2015: £12.1m).

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

There have been no employer related investments during the year.

### 22. Contingencies and Commitments

At 31 December 2016 in the opinion of the Trustee, the Scheme had no contingent liabilities or undrawn commitments (2015: £nil).

### 23. Subsequent Events

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

## Summary of Contributions Payable

For the Year Ended 31 December 2016

During the year ended 31 December 2016 the contributions payable to the Scheme under the Schedules of Contributions were as follows:

	£000s	£000s
<b>Employer's deficit funding contributions</b>		<b>7,357</b>
Employer other contributions in respect of 2016 Scheme expenses:		
- Monthly amounts received	600	
- Other amounts received allocated towards Scheme expenses	115	
<b>Total Employer other contributions in respect of 2016 Scheme expenses</b>	<u>715</u>	<b>715</b>
<b>Contributions required by the Schedule of Contributions as Reported on by the Scheme auditor</b>		<u><b>8,072</b></u>
Reversal of over-provision of 2015 Employer other expense contributions (see below)		(105)
<b>Total contributions included in the Financial Statements (note 3)</b>		<u><u><b>7,967</b></u></u>

As reported on page 7 of the Trustee Report, following a review of the calculation of the one-off Employer expense contribution payable, it was determined the Scheme had over-provided for the amount due from the Employer in respect of 2015 by £105,000 due to the incorrect inclusion of investment expenses relating to Legal & General. The Trustee subsequently agreed with the Employer that the previously reported amount payable to the Scheme in respect of 2015 of £447,000 would be reduced to £342,000. The adjusted amount payable of £342,000 was fully settled by the Employer by 31 December 2016.

During 2016, the Employer made further expense contributions totalling £715,000, as shown above.

As a result of the adjustment, the reported Employer other expense contributions for the year ended 31 December 2016 of £610,000 as shown in note 3 to the financial statements, is the net of the expense contribution receipts in respect of 2016, and the 2015 over-provided amount of £105,000.

Approved by the Trustee on 11 May 2017 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 2016 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 Trustee 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 Trustee- 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 Schedules 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 Schedules of Contributions.

### Statement about contributions payable under the Schedules of Contributions

In our opinion, contributions for the Scheme year ended 31 December 2016 as reported in the summary of contributions and payable under the Schedules of Contributions have in all material respects been paid for the period 1 January 2016 to 23 March 2016 at least in accordance with the Schedule of Contributions certified by the actuary on 16 July 2012, and for the period 24 March 2016 to 31 December 2016 at least in accordance with the Schedule of Contributions certified by the actuary on 24 March 2016.



**Deloitte LLP**

Chartered Accountants and Statutory Auditor

London, United Kingdom

Date: 11 May 2017

# 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) was 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.