

Notice of meeting and agenda

Pensions Audit Sub-Committee

2.00pm, Tuesday 26 September 2017

Dunedin Room, City Chambers, High Street, Edinburgh

This is a public meeting and members of the public are welcome to attend

Contact

Hannah King

E-mail: hannah.king@edinburgh.gov.uk

Tel: 0131 529 4121

1. Order of business

- 1.1 Including any notices of motion and any other items of business submitted as urgent for consideration at the meeting.

2. Declaration of interests

- 2.1 Members of the Committee and members of the Pensions Board should declare any financial and non-financial interests they have in the items of business for consideration, identifying the relevant agenda item and the nature of their interest.

3. Deputations

- 3.1 None.

4. Minute

- 4.1 Minute of the Pensions Audit Sub-Committee of 5 December 2016 – Submitted for approval as a correct record (circulated)

5. Reports

- 5.1 Considerations and matters to be raised by the Pension Board regarding any items on the agenda
- 5.2 Agenda Planning – report by the Executive Director of Resources (circulated)
- 5.3 Audited Annual Report 2017 of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund, including Annual Report by External Auditor (unaudited) – report by the Executive Director of Resources (circulated)
- 5.4 Fraud Prevention – report by the Executive Director of Resources (circulated)
- 5.5 Irrecoverable overpayment of pensions – decisions made under delegated authority – report by the Executive Director of Resources (circulated)
- 5.6 Overpayment of Pension – report by the Executive Director of Resources (circulated)
- 5.7 Risk Management Summary – report by the Executive Director of Resources (circulated)

6. Motions

- 6.1 If any

Laurence Rockey

Head of Strategy and Insight

Committee Members

Councillors Rose (Convener), Child and John Anzani.

Information about the Pensions Audit Sub-Committee

The Pensions Audit Sub-Committee consists of 3 members of the Pensions Committee of which a minimum of two are City of Edinburgh Councillors and its membership is appointed by the Pensions Committee.

The Pensions Audit Sub-Committee usually meets in the City Chambers on the High Street in Edinburgh. The meeting is open to all members of the public.

Further information

If you have any questions about the agenda or meeting arrangements, please contact Hannah King, Committee Services, City of Edinburgh Council, City Chambers, High Street, Edinburgh EH1 1YJ, Tel 0131 529 4121, e-mail hannah.king@edinburgh.gov.uk.

A copy of the agenda and papers for this meeting will be available for inspection prior to the meeting at the main reception office, City Chambers, High Street, Edinburgh.

The agenda, minutes and public reports for this meeting and all the main Council committees can be viewed online by going to www.edinburgh.gov.uk/cpol.

Pensions Audit Sub-Committee of the Pensions Committee

14.00, Monday 5 December 2016

Present

Councillors Rose (Convener), and Orr.

Pensions Board Members Present:

Catriona Warren and Alan Williamson

1. Minute

Decision

To approve the minute of the Pensions Audit Sub-Committee of the Pensions Committee of 27 September 2016 as a correct record.

2. Agenda Planning

An overview of potential reports for future Pensions Committee and Pensions Audit Sub-Committee meetings for March 2017 and June 2017 were outlined.

Decision

To note the agenda planning document.

(Reference – report by the Acting Executive Director of Resources, submitted.)

3. EU Tax Claims & Income Recovery

A summary was provided of the activity on EU tax and other tax claims made on behalf of Lothian Pension Fund. During the period since the last report, no additional claims had been received and the amount recovered to date remains at £1,370.1k.

Decision

To note the report by the Acting Executive Director of Resources.

(Reference – report by the Acting Executive Director of Resources, submitted.)

4. Global Custody Services Performance

The Fund's custodian, Northern Trust, had provided their key performance report for the 12 months ended 30 September 2016. Northern Trust was currently meeting the needs of the three Pension Funds.

Decision

To note the report by the Acting Executive Director of Resources.

(Reference – report by the Chief Internal Auditor, submitted.)

5. Investment Income Review Cross Border Withholding Tax

Information was provided on a benchmarking study prepared by E&Y into the effectiveness of the procedures in place to manage the tax exposure on the investment income of Lothian Pension Fund and Lothian Buses Pension Fund.

Decision

To note the report by the Acting Executive Director of Resources.

(Reference – report by the Acting Executive Director of Resources, submitted.)

6. Lothian Pension Fund – Internal Audit Update 2016/17

A summary was provided of Internal Audit activity during the period 1 September 2016 to 30 November 2016.

Decision

- 1) To note the Internal Audit activity during the period 1 September 2016 to 30 November 2016.
- 2) To note the matters arising from the Internal Audit review undertaken in this period.
- 3) To note the status of management actions from audits undertaken in 2015/16, and in 2016/17.

(Reference – report by the Acting Executive Director of Resources, submitted.)

7. Resolution to consider in private

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the following items of business on the grounds that they involved the disclosure of exempt information as defined in Paragraph 6 of Schedule 7(A) of the Act.

8. Lothian Pension Fund – Third Party ICT Supplier Risk

A summary of the findings of the external vulnerability assessment for online modules accessible to employers and members of the Lothian Pension Funds was provided.

Decision

- 1) To note the matters arising from the external vulnerability assessment undertaken in this period.
- 2) To agree that an update concerning Third Party ICT Supplier Risk would be submitted to the Pensions Audit Sub Committee during the summer of 2017 and that should issues arise during the interim that these be referred to the Convener of the Pensions Committee for consideration.

(Reference – report by the Acting Executive Director of Resources, submitted.)

9. Risk Management in depth Review

A summary was provided of the Lothian Pension Fund's risk management procedures, including details on the operational risk register and the Fund's action to mitigate these risks.

Decision

To note the Operational Risk Register and Quarterly Risk Overview as at 25 October 2016.

(Reference – report by the Acting Executive Director of Resources, submitted.)

Pensions Audit Sub Committee

2.00pm, Tuesday, 26 September 2017

Agenda Planning

Item number	5.2
Report number	
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for all

Executive Summary

This document provides Committee with an overview of the proposed agendas for future meetings of the Pensions Committee and Pensions Audit Sub Committee. It also provides a more general overview of the current cycle of papers for the Committees.

There will, of course, be specific matters and papers which need to be brought to the attention of the Pensions Committee and the Pensions Audit Sub Committee in addition to those set out herein.

Agenda Planning

1. Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider; and
- 1.2 Note the agenda planning document.

2. Background

- 2.1 In order for the Committee and Pension Board to gain an overview of the content of future meetings it was agreed that an agenda planning document be submitted each quarter.

3. Main report

- 3.1 Due to the cancellation of the meetings of the Pensions Audit Sub-Committee and the Pensions Committee in June 2017, a number of amendments have been made to the agendas as follows:
 - Investment reports, normally considered in June, are included in the agenda for September;
 - LPFE and LPFI Limited Accounts are included in the report on the LPF Annual Report & Accounts for September. A report on LPFE staffing issues is also included in the September agenda and an update on Collaboration (including LPFI activity) is scheduled for December 2017;
 - Pensions Data Quality report (which would normally be considered in September) has been postponed to December. It was felt that this would reduce the volume of papers for Committee in September but it would also allow the Committee the opportunity to see a report from the Actuary on the data provided for the 2017 actuarial valuation.

3.2 Based on the Committee cycle and the current position, the proposed agendas for the next two meetings are set out below.

December 2017

Pensions Committee	Audit Sub Committee
<ul style="list-style-type: none"> • Referrals / recommendations from Pensions Audit-Sub Committee • Considerations and matters to be raised by the Pension Board regarding any items on the agenda • Benchmarking • Stewardship and Engagement • Actuarial Valuation: Lothian Pension Fund/Lothian Buses Pension Fund/Scottish Homes Pension (if complete) • Update on Collaboration • Service Plan Update • Risk management summary 	<ul style="list-style-type: none"> • Internal Audit reports • Pensions Data Quality (postponed from September 2017) • EU Tax Claims & Income Recovery • Investment Income Review-Cross-Border withholding tax • Investment Controls & Compliance • Global Custody Services Performance • Risk Management in-depth review

March 2018

Pensions Committee
<ul style="list-style-type: none"> • Referrals / recommendations from Pensions Audit-Sub Committee • Considerations and matters to be raised by the Pension Board regarding any items on the agenda • Audit plans and reports (internal and external) * • Policies/Strategies/Training (including revised Pension Administration Strategy biennial from March 2016) • Governance Update • Audit Sub-Committee Appointments • Actuarial Valuation: Lothian Pension Fund/Lothian Buses Pension Fund/Scottish Homes Pension (if not reported in December 2017) • Funding Strategy Statement • Employers Participating in Lothian Pension Fund • 2016 – 2019 Service Plan Update • 2018 – 2021 Service Plan and Budget • Risk management summary

*Draft audits and plan will be developed in consultation with the Convenor of the Audit Sub Committee.

Future Pensions Committee and Audit Sub Committee dates:

Pensions Committee	Pensions Audit Sub Committee
<ul style="list-style-type: none">• Tuesday 12 December 2017, 2pm, Dunedin Room, City Chambers• Monday, 26 March 2018, 2pm, Dunedin Room, City Chambers• Wednesday 27 June 2018, 2pm, Dunedin Room, City Chambers	<ul style="list-style-type: none">• Monday, 11 December 2017, 2pm, Dunedin Room, City Chambers• Tuesday 26 June 2018, 2pm, Dunedin Room, City Chambers

4. Measures of success

- 4.1 The Committee and Pension Board have greater clarity regarding the content of the Committee cycle.

5. Financial impact

- 5.1 None.

6. Risk, policy, compliance and governance impact

- 6.1 There is no direct impact as a result of this report. The forward planning of the Committees' agendas should facilitate improved risk management and governance for the pension funds

7. Equalities impact

- 7.1 There are no adverse equalities impacts arising from this report.

8. Sustainability impact

- 8.1 There are no adverse sustainability impacts arising from this report.

9. Consultation and engagement

- 9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

10. Background reading/external references

- 10.1 None

Stephen S. Moir

Executive Director of Resources

Contact: Struan Fairbairn, Chief Risk Officer, Lothian Pension Fund

E-mail: struan.fairbairn@edinburgh.gov.uk | Tel: 0131 529 4689

11. Appendices

Appendix 1 – Scheme of Committee Papers

Frequency	Pensions Committee	Audit Sub Committee	Month
Annually	Audit plans and reports (internal and external)	N/A - Draft audits and plan will be developed in consultation with the Convenor of the Audit Sub Committee.	March
	Policies/Strategies/Training (including revised Pension Administration Strategy biennial from March 2016)	N/A	March
	Service Plan (every 2 years)	N/A	March
	Budget	N/A	March
	Governance Update	N/A	March
	Audit Sub-Committee Appointments	N/A	March
	LPF Annual Report & Accounts Unaudited	LPF Annual Report & Accounts Unaudited	June
	Statement of Investment Principles	N/A	June
	Investment Strategy Panel Activity	N/A	June
	Annual Investment Updates - Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund	N/A	June
	LPFE limited and LPFI limited Annual Report	LPFE limited and LPFI limited Annual Report	September
	LPF Annual Report & Accounts Audited	LPF Annual Report & Accounts Audited	September
	ISA 260 Audit Report	ISA 260 Audit Report	September
	N/A	Pensions Data Quality	September
	N/A	Irrecoverable overpayment of pensions – decisions made under delegated authority	September
	N/A	Fraud Prevention	September
	Annual Report by External Auditor	Annual Report by External Auditor	December (or September if available)
	Benchmarking	N/A	December
	N/A	EU Tax Claims & Income Recovery	December
	N/A	Investment Income Review-Cross-Border withholding tax	December
Stewardship and Engagement	N/A	December	
N/A	Investment Controls & Compliance	December	
N/A	Global Custody Services Performance	December	
	Risk Management In-depth review	December	

Frequency	Pensions Committee	Audit Sub Committee	Month
Semi Annually	Employers Participating in Lothian Pension Fund	N/A	March & September
3 Times per year	Service Plan Update	N/A	March, September & December
	Referrals / recommendations from Pensions Audit-Sub	N/A	June, September & December
Quarterly	Risk management summary	Risk management summary	March, June, September and December
	Considerations and matters to be raised by the Pension Board regarding any items on the agenda	N/A	March, June, September and December
Every 3 years	Actuarial Valuation: LPF/LBPF/SHPF Funding Strategy Statement		December or March
As required	Delegated authorities (provider appointments) Discretions (death grants etc.) N/A Regulatory Update Investment Strategy Reviews (at least every 3 years) N/A	N/A N/A Internal Audit Reports N/A N/A Risk management (in depth review)	

Pensions Audit Sub Committee

2.00pm, Tuesday, 26 September 2017

Audited Annual Report 2017 of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund, including Annual Report by External Auditor

Item number	5.3
Report number	
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for all

Executive Summary

The unaudited Annual Report for the year ended 31 March 2017 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund has now been considered by the external auditor, Scott-Moncrieff.

International Standard on Auditing (ISA) 260 requires the external auditor to communicate their findings to those charged with governance of the Funds. Accordingly, the Scott-Moncrieff “Lothian Pension Funds 2016/17 Annual Audit Report to Members and the Controller of Audit” is included at Appendix 1.

The review of the unaudited financial statements concluded that no numerical adjustments were required. Some presentational changes have been reflected in the full revised report at Appendix 2 – “Audited Annual Report 2017 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund”.

Scott-Moncrieff has provided “an unqualified opinion on the financial statements and other prescribed matters for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund within our independent auditor’s report” and has also stated “that there were no matters which we were required to report by exception”.

Audited Annual Report 2017 of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund, including Annual Report by External Auditor

1. Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider;
- 1.2 Note the report by Scott-Moncrieff “Lothian Pension Funds 2016/17 Annual Audit Report to Members and the Controller of Audit” (at Appendix 1);
- 1.3 Note the audited Annual Report for the year ended 31 March 2017 for the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund (at Appendix 2);
- 1.4 Note that the audited financial statements, for the year ended 31 March 2017, of both the wholly-owned companies, LPFE Limited and LPFI Limited, were approved by the respective Board of Directors in June 2017. These statements are shown in full at Appendices 3 and 4.
- 1.5 Note that Scott-Moncrieff has made no comment in respect of the Chartered Institute of Public Finance and Accountancy (CIPFA) guidance “Accounting for Local Government Pension Scheme Management Costs”, as revised in June 2016, and its failure to reflect full transparency of investment management fees, specifically through “fund of fund arrangements”; and
- 1.6 Highlight any points that it would like to raise at the Pensions Committee on 27 September 2017;

2. Background

ISA 260 annual report by External Auditor

- 2.1 Under statutory accounting guidance issued by the Scottish Government, Administering Authorities are required to issue a separate Annual Report covering the Local Government Pension Scheme (LGPS) funds that they are responsible for. These Annual Reports are subject to a separate external audit.
- 2.2 International Standard on Auditing (UK and Ireland) 260 (ISA 260) requires the External Auditor to communicate his findings to those charged with governance of

the Funds. This summarises any matters arising from the audit of the financial statements prior to the formal signing of the independent auditor's report.

2.3 As part of the standard, the External Auditor is required to provide its view of the following:

- Any significant qualitative aspects within the Funds' accounting practice;
- Any significant difficulties encountered during the audit;
- Any material weakness in the design, implementation or operating effectiveness of the system of internal control;
- Any significant matters arising from the audit discussed with management;
- Any representations that have been requested from management; and
- Any other matter that is significant.

2.4 City of Edinburgh Council noted the Unaudited Annual Report 2017 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund at its meeting on 29 June 2017.

3. Main report

Scott-Moncrieff - Lothian Pension Funds 2016/17 Annual Audit report to Members and the Controller of Audit

- 3.1 The report by the external auditor on the financial statements is included at Appendix 1 – “Scott-Moncrieff - Lothian Pension Funds 2016/17 Annual Audit Report to Members and the Controller of Audit.
- 3.2 Scott-Moncrieff has stated that its “work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK and Ireland) and Ethical Standards”.
- 3.3 This report will be presented to Committee by Nick Bennett, Partner, and Kirstie MacDonald, Public Sector Audit Senior, Scott-Moncrieff.
- 3.4 Scott-Moncrieff has provided “an unqualified opinion on the financial statements and other prescribed matters for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund within our independent auditor's report” and has also stated “that there were no matters which we were required to report by exception”.
- 3.5 Scott-Moncrieff has made no comment in respect of the Chartered Institute of Public Finance and Accountancy (CIPFA) guidance “Accounting for Local Government Pension Scheme Management Costs”, as revised in June 2016, and its failure to reflect full transparency of investment management fees, specifically through “fund of fund arrangements”. Committee is reminded that the financial statements of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund continue, however, to include full transparency of all investment management fees.

- 3.6 Appendix 1 (“Appendix 1: Management action plan”, Pages 28 to 30 of that report) “details the control weaknesses and opportunities for improvement that we (Scott-Moncrieff) have identified during our audit”. Planned management actions by Lothian Pension Fund staff in relation to the points raised by the external auditor are also stated.
- 3.7 In addition to members of the Pensions Committee and Pensions Audit Sub-Committee, Scott-Moncrieff has also sent the report to the Controller of Audit and has advised that it will be published on the Audit Scotland web-site in due course.

Audited Annual Report 2017 for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

- 3.8 With the completion of the work by Scott-Moncrieff, the Audited Annual Report 2017 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund has been finalised and is included at Appendix 2.
- 3.9 No numerical adjustments were required to be made on the unaudited financial statements following the Fund’s audit. Some minor presentational changes have also been incorporated.
- 3.10 As part of the completion of the audit, the auditor seeks written assurances from the Chief Finance Officer, Lothian Pension Fund, on aspects of the financial statements and judgements and estimates made. A draft letter of representation under ISA580 is attached at Appendix 5.

Audited Financial Statements for the year ended 31 March 2017; LPFE Limited and LPFI Limited

- 3.11 The consolidated financial statements (within the Annual Report 2017) combine those of the Fund (the parent entity) and its controlled entities (the investment staffing company, LPFE Limited, and now also the investment services company, LPFI Limited, which commenced trading during the year) as defined in International Accounting Standard (IAS) 27. The financial statements of both companies have been audited by Scott-Moncrieff and approved by the respective Board of Directors in June 2017, LPFE Limited on 12 June 2017 and LPFI Limited on 15 June 2017. These statements are shown in full at Appendices 3 and 4.
- 3.12 As previously reported to Committee, LPFE Limited is the employment vehicle for the Fund’s investment and senior staff. It provides staffing services to the City of Edinburgh Council, LPFI Limited and to Falkirk Council. The company’s financial objective is “to make a modest trading surplus before adjustments required under International Financial Reporting Standards (IFRS)”. Such adjustments primarily relate to pension costs, as required by International Accounting Standard (IAS) 19, and the related deferred tax. For the year ended 31 March 2017, the underlying trading profit of the company was £30,730 (2016: £28,243).
- 3.13 A separate report on the Phase 2 transfer of staff to the company is provided elsewhere on the agenda for this Committee.
- 3.14 LPFI Limited provides Financial Conduct Authority (FCA) regulated investment services, both to Lothian Pension Fund and other pension funds, but does not

employ any staff directly. Its financial objective is “to make a modest trading surplus”. LPFI commenced trading in December 2016 and completed its first collaborative “club-deal” in the infrastructure sector in January 2017. A second project was in progress at the year-end. Profit for the financial year after taxation was £432.

- 3.15 Committee was previously advised of the appointment of Leslie Robb as non-executive director of LPFI Limited, subject to the receipt of requisite approvals from the FCA. These were received and his appointment commenced from 1 February 2017. Leslie is expected to attend the meeting of the Pensions Committee on 27 September.
- 3.16 A full report will be provided to Committee in December 2017 on the progress and further development of collaborative initiatives with other LGPS funds.

4. Measures of success

- 4.1 The prime objective of the Council, as administering authority of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund, is to ensure an unqualified audit opinion of the Annual Report 2017. This has been achieved.
- 4.2 Planned management actions in relation to the points raised by the external auditor, Scott-Moncrieff, are stated at Appendix 1 (“Appendix 1: Management action plan”, Pages 28 to 30 of that report).

5. Financial impact

- 5.1 There are no direct financial implications arising from this report.

6. Risk, policy, compliance and governance impact

- 6.1 The financial statements have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 and also in compliance with the requirements of the Local Government Scotland Act 1973.
- 6.2 The annual report summarises the opinions and conclusions of Scott-Moncrieff, in accordance with International Standards on Auditing (UK and Ireland) and the principles contained in the Code of Practice issued by Audit Scotland in May 2011. The Scott-Moncrieff report sets out the significant audit risks identified at the planning stage and how the auditor addressed each risk in arriving at his opinion on the financial statements. Appendix I (of that report) is the “Management action plan” “detailing the control weaknesses and opportunities for improvement” which were identified by the External Auditor during the audit. Officers have considered the issues and responded in the column headed “Management Comments”.

7. Equalities impact

7.1 There are no adverse equalities impacts arising from this report

8. Sustainability impact

8.1 There are no adverse sustainability impacts arising from this report.

9. Consultation and engagement

9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

10. Background reading/external references

10.1 None

Stephen S. Moir

Executive Director of Resources

Contact: John Burns, Chief Finance Officer, Lothian Pension Fund

E-mail: john.burns@edinburgh.gov.uk | Tel: 0131 469 3711

11. Appendices

Appendix 1 – Scott-Moncrieff - Lothian Pension Funds 2016/17 Annual Audit Report to Members and the Controller of Audit, in accordance with International Standard on Auditing (UK and Ireland) 260 (ISA 260)

Appendix 2 - Audited Annual Report 2017 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

Appendix 3 - LPFE Limited – Financial Statements (Audited) for the year ended 31 March 2017

Appendix 4 – LPFI Limited – Financial Statements (Audited) for the year ended 31 March 2017

Appendix 5 – Letter of Representation (ISA 580) by Chief Finance Officer, Lothian Pension Fund



Scott-Moncrieff
business advisers and accountants

Appendix 1

Lothian Pension Funds

2016/17 Annual Audit Report to Members and
the Controller of Audit

August 2017

Contents

- Key messages..... 1**
- Introduction..... 3**
- Annual accounts..... 5**
- Financial management 13**
- Financial Sustainability 17**
- Governance & transparency 21**
- Value for money..... 25**
- Appendix 1: Management action plan 28**
- Appendix 2: Unadjusted differences 31**
- Appendix 3: Respective responsibilities of the Pensions Committee and the Auditor 32**

Key messages

Annual accounts

Lothian Pension Funds are scheduled to approve the annual accounts for 2016/17 on 27 September 2017 and the accounts will be submitted, together with this report, to the Controller of Audit by the deadline of 30 September 2017. We intend to report unqualified opinions on the financial statements and other prescribed matters for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund within our independent auditor's report. We also intend to report that there were no matters which we were required to report by exception.

Wider Scope

Financial management

- The Funds have adequate and effective arrangements in place for managing their financial position and use of resources.
- We have evaluated the Funds' key financial systems and internal financial controls and determined these are adequate to prevent material misstatements in the annual accounts.

Financial sustainability

- We have concluded that the Funds have effective arrangements in place to ensure the ongoing sustainability of the pension funds.

Governance & transparency

- Our work on corporate governance focussed on reviewing the Funds' arrangements to ensure effective systems are in place regarding internal control, prevention and detection of fraud and irregularity and standards of conduct.
- Governance arrangements at the Funds were found to be satisfactory and appropriate.

Value for money

- The Funds have appropriate arrangements in place to monitor performance of investments and the administration of the Funds.

Key facts

- Net assets increased by 21% in 2016/17 to £6,595 million (2015/16: £5,433 million).
- Contributions received in year (£201.8 million) fell below the benefits paid out by the fund (£211.1 million) leaving a net withdrawal on the fund of £9.2 million.
- Return on investments in 2016/17 was 21.7% slightly behind the benchmark of 24.8%; however, the performance over the five year period to 31 March 2017 is exceeding the target of 11.4% by 1.5%.

Conclusion

This report concludes our audit for 2016/17. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK and Ireland) and Ethical Standards.

Scott-Moncrieff August 2017

1

Introduction

Introduction

1. This report summarises our findings from the 2016/17 audit of the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund (collectively referred to as the “Funds”).
2. We outlined the scope of our audit in our external audit plan, which we presented to the Pensions Committee on 20 March 2017. The core elements of our audit work in 2016/17 have been:
 - an interim audit of the Funds’ key financial systems and governance arrangements;
 - an audit of the Funds’ 2016/17 annual report and accounts, including a review of the Annual Governance Statement;
 - a review of arrangements as they relate to the four dimensions of wider-scope public audit: financial management, financial sustainability, governance and transparency, and value for money; and
 - consideration of the local impact of the national performance report [The Role of Boards](#).
3. The Funds are responsible for preparing annual accounts that show a true and fair view and for implementing appropriate internal control systems. The weaknesses and risks identified in this report are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.
4. We discussed and agreed the content of this report with the Chief Finance Officer and Chief Executive. We would like to thank all management and staff for their co-operation and assistance during our audit.

5. This report contains an action plan with specific recommendations, responsible officers and dates for implementation. Senior management should assess these recommendations and consider their wider implications before deciding appropriate actions. We give each recommendation a grading to help the Funds assess their significance and prioritise the actions required.

Adding value through the audit

6. All of our clients quite rightly demand of us a positive contribution to meeting their ever-changing business needs. Our aim is to add value to the Funds through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the Funds promote improved standards of governance, better management and decision making and more effective use of resources.
7. We welcome any comments you may have on the quality of our work and this report via: www.surveymonkey.co.uk/r/S2SPZBX
8. This report is addressed to both Lothian Pension Funds and the Controller of Audit and will be published on Audit Scotland’s website. www.audit-scotland.gov.uk.

2

Annual accounts

Annual accounts

Introduction

9. The Funds' annual financial statements are the principal means of accounting for the stewardship of its resources and its performance in the use of those resources. The respective responsibilities of the Funds and the auditor in relation to the financial statements are outlined in appendix 2.

Overall conclusion

Unqualified audit opinions

10. The annual accounts for the year ended 31 March 2017 are due to be approved by the Pensions Committee on 27 September 2017. We plan to report within our independent auditor's report:
- an unqualified opinion on the financial statements; and
 - an unqualified opinion on other prescribed matters.

11. We are also satisfied that there are no matters which we are required to report to you by exception.

Good administrative processes were in place

12. We received draft financial statements and supporting papers of a good standard, in line with our agreed audit timetable. Our thanks go to management and staff for their assistance.

Our assessment of risks of material misstatement

13. The assessed risks of material misstatement described below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the audit team. We designed our audit procedures relating to these matters in the context of our audit of the annual report and accounts as a whole, and not to express an opinion on individual accounts or disclosures. We outline the significant risks below.

Audit Risk 1: Revenue Recognition

Under ISA 240 - The auditor's responsibilities relating to fraud in an audit of financial statements there is a presumed risk of fraud in relation to revenue recognition. The presumption is that the Funds could adopt accounting policies or recognise income and expenditure transactions in such a way as to lead to a material misstatement in the reported financial position.

14. While we did not suspect incidences of material fraud and error, we evaluated each type of revenue transaction and documented our conclusions. We have reviewed the controls in place over revenue accounting and found them to be sufficient. We have evaluated key revenue transactions and streams and carried out testing to confirm that the Funds' revenue recognition policies are appropriate and have been applied consistently.

Audit Risk 2: Management override of controls


In any organisation, there exists a risk that management have the ability to process transactions or make adjustments to the financial records outside the normal financial control processes. Such issues could lead to a material misstatement in the annual accounts. This is treated as a presumed risk area in accordance with ISA 240 - *The auditor's responsibilities relating to fraud in an audit of financial statements*.

15. While we did not suspect any incidences of management override leading to financial reporting issues, we reviewed the accounting records for significant transactions outside the normal course of business and obtained evidence to ensure that these were valid and accounted for

correctly. Based on our audit work to detect potential material misstatement we have not identified any indications of such management override during the year.


Audit Risk 3: Valuation of Investments

The Lothian Pension Fund held investments of £5.399 billion as at 31 March 2016, of which 30% (£1.663 billion) were classified as level 2 or level 3 financial instruments, meaning the valuation was not based on unadjusted quoted prices in active markets. Investments of this nature are complex, difficult to value and include a significant degree of judgement from the investment manager. The material nature of this balance means that any error in judgement could result in a material valuation error.

- 
16. In 2016/17 the value of level 2 and level 3 investments rose in year to £2.069 billion increasing as a proportion of overall investments to 31%. Fair values of investments of this nature are provided by the fund managers and custodian using different bases as deemed appropriate, including reference to similar companies and bid prices. The valuation basis for each class of investment is disclosed within the accounting policies of the Funds.
 17. We have considered the competence, capability and objectivity and control environment of the key fund managers and the custodian. Our testing did not raise any issues regarding the qualifications of or work provided by management's experts.
 18. The disclosures in the financial statements are consistent with the information provided by the custodian.

Audit Risk 4: Pension liability assumptions

An actuarial estimate of the pension fund liability is calculated on an annual basis under IAS 19 and on a triennial funding basis by independent firm of actuaries with specialist knowledge and experience. The estimates are based on the most up to date membership data held by the pension fund and have regard to local factors such as mortality rates and expected pay rises with other assumptions around inflation when calculating the liabilities. There is a risk that the assumptions used are not appropriate.

- 
19. Our review of the control environment around membership data did not identify any weaknesses in its design which would be likely to lead to a material misstatement.
 20. The assumptions used by the actuary were compared to benchmarks across the sector and deemed to be reasonable.

Our application of materiality

21. Materiality is an expression of the relative significance of a matter in the context of the financial statements as a whole. A matter is material if its omission or misstatement would reasonably influence the decisions of an addressee of the auditor's report. The assessment of what is material is a matter of professional judgement over both the amount and the nature of the misstatement.

22. On receipt of the draft 2016/17 accounts, we reassessed materiality which resulted in a change to the level of materiality applied. Our revised assessment of materiality along with our planning materiality for each Fund is set out in the table below. The Funds hold significant investment assets, which form the largest part of the net asset statements for each pension fund. We consider that the net asset statements are of primary interest to the reader of the annual accounts and therefore consider that these should be used in the calculation of overall materiality.

23. ISA 320 states that in certain circumstances it is appropriate to set a materiality amount for particular classes of transactions for which the lesser amounts than the overall materiality could influence the decision of the users of the accounts. We considered the transactions in

the Fund Accounts to be of key interest to the users as it contains information around the day to day performance of the Funds. We have therefore set a materiality for this class of transactions based on return on investments and the expenditure incurred for providing payments to pensioners.

	Overall Planning materiality £million	Fund account planning materiality £million	Overall Final materiality £million	Fund account final materiality £million
Lothian Pension Fund (group) ¹	81.5	8.8	98.9	19.9
Lothian Pension Fund (single entity)	81.5	8.8	98.9	19.9
Lothian Buses Pension Fund	5.9	0.4	7.3	1.5
Scottish Homes Pension Fund	2.3	0.2	2.5	0.5

24. We set a performance materiality for each area of work which is based on a risk assessment for that area. We have performed audit procedures on all transactions, or groups of transactions, and balances that exceed our performance materiality. This means that we performed a greater level of testing on the areas deemed to be of significant risk of material misstatement

Scottish Homes Pension Fund	1.7	1.4	1.1
-----------------------------	-----	-----	-----

	Area risk assessment £million		
	High (45%)	Medium (55%)	Low (70%)
Lothian Pension Fund (group and parent)	44.5	54.4	69.2
Lothian Buses Pension Fund	13.9	10.9	8.9

25. We agreed to report any misstatements identified through our audit that fall into one of the following categories:

- All material corrected misstatements;
- Uncorrected misstatements over £250,000, less than 1% of the overall materiality figure;
- Misstatements below the £250,000 threshold we believe warrant reporting on qualitative grounds.

Other matters

26. We identified one medium risk matter relating to the authorisation of journal entries. We have reported on this fully within appendix 1 to this report.

¹ Lothian Pension Fund group comprises Lothian Pension Fund, LPFE Ltd and LPFI Ltd

Audit adjustments identified

27. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual accounts.

Board representations

28. We have requested that the Pensions Committee present a signed representation letter, covering a number of issues, to us at the date of signing the financial statements.
29. In June 2017 a voluntary disclosure of under-declared Output Tax was made to HMRC by the City of Edinburgh Council on behalf of the Funds. The under declaration arose from two properties managed by Standard Life which did not have VAT applied correctly. A review of all properties has been undertaken and the total under declaration was £0.51 million. The total under declaration covers a number of tax periods and does not breach the penalty threshold in any financial year. The proposed adjustment is outlined at appendix 2.
30. We do not consider the difference to be material to the financial statements, either individually or in aggregate. Through discussion with the Chief Finance Officer, the decision was taken not to adjust the financial statements. The difference is reported through the representation letter.

An overview of the scope of our audit

31. We detailed the scope of our audit in our external audit plan. We presented the plan to the Pensions Committee on 20 March 2017.
32. Our plan explained that we follow a risk-based approach to audit planning that reflects our overall assessment of the relevant risks that apply to the Pensions Committee. This ensures that our audit focuses on the areas of highest risk. Planning is a continuous process and our audit plan is subject to review during the course of the audit to take account of developments that arise.

33. At the planning stage we identified the significant risks that had the greatest effect on our audit. We then designed audit procedures to mitigate these risks. We base our standard audit approach on performing a review of the key accounting systems in place, substantive tests and detailed analytical review.

34. Tailored audit procedures, including those designed to address significant risks, were completed by the audit fieldwork team and the results were reviewed by the audit manager and audit partner. In performing our work, we have applied the concept of materiality, which is explained earlier in this report.

Accounting and Internal Control systems

35. The Funds have adequate systems in place to record, process, summarise and report financial and other relevant data. We have not identified any material weaknesses or governance issues in the Funds' accounting and internal control systems during our final audit.

Other matters identified during our audit

36. During the course of our audit we noted the following:

The Local Authority Accounts (Scotland) Regulations 2014

37. As part of our audit we reviewed the Council's compliance with the Local Authority Accounts (Scotland) Regulations 2014, in particular with respect to regulations 8 to 10² as they relate to the annual accounts. Overall we concluded that appropriate arrangements are in place to comply with these Regulations.

Management commentary

38. The Local Authority Accounts (Scotland) Regulations 2014 require pension funds to include a management commentary within the annual accounts. The management commentary is intended to assist readers in understanding the annual accounts and the organisation that has prepared them. As auditors we are required to read the

² Regulations 8 to 10 relates to the preparation and publication of unaudited accounts, notice of public right to

inspect and object to the accounts and consideration and signing of the audited accounts.

management commentary and express an opinion as to whether it is consistent with the annual accounts. We have concluded that the management commentary is consistent with the annual accounts.

39. As part of our audit we also reviewed the Council's management commentary against the non-statutory guidance issued by the Scottish Government (Local Government Finance Circular 5/2015). We considered the extent to which the Funds' management commentary included relevant information in respect of:

- The context of the annual accounts;
- Insight into the priorities of the Funds' and strategies adopted to achieve these priorities and objectives;
- Information on future plans;
- KPIs which measure the investment performance of the Funds'; and
- Information on the principal risks and uncertainties facing the authority.

Annual governance statement and Governance Compliance Statement

40. The Chief Executive and Acting Executive Director of Resources of the City of Edinburgh Council along with the Chief Executive Officer of Lothian Pension Fund have confirmed that in their opinion, reasonable assurance can be placed upon the adequacy and effectiveness of Lothian Pension Funds' systems of governance. The Annual Governance Statement identifies a range of actions that have been, or will be, taken by the Council to continue to progress improvements in the Council's governance arrangements.

41. We have reviewed the Funds' Annual Governance Statement and have found that it complies with the relevant guidance: *Delivering Good Governance in Local Government*. However, it is a requirement that the Annual Governance Statement outlines an action plan outlining the actions that the Funds' will take to continue to progress improvements in the Funds' governance processes. This was not present in the draft accounts.

Action Plan point 2

42. We found that the processes used to prepare the statements are reasonable and appropriate.

43. The Local Government Pension Scheme (Scotland) Regulations 2014 require all pension

funds to prepare a Governance Compliance Statement. The purpose of this statement is to compare the Funds' governance arrangements with those standards set out in guidance from the Scottish Ministers.

44. We have reviewed the Governance Compliance Statement and we are satisfied the disclosures comply with guidance issued by Scottish Ministers and are not inconsistent with our knowledge of the arrangements in place at the Funds.

Group accounts

45. The Pensions Committee for the Funds approved the creation of two special purpose vehicles, LPFE Ltd and LPFI Ltd in October 2014. The companies are wholly owned and controlled by the City of Edinburgh Council. Group accounts were prepared for the Funds for the first time in 2015/16 incorporating LPFE Ltd. LPFI Ltd became operational in 2016/17 after the funds received Financial Conduct Authority authorisation.

46. We reviewed the consolidation process in 2016/17 and concluded the subsidiary companies had been correctly included in the group accounts of Lothian Pension Fund.

Legality

47. We have planned and performed our audit recognising that non-compliance with statute or regulations may materially impact on the annual accounts. Our audit procedures included the following:

- Reviewing minutes of relevant meetings;
- Enquiring of senior management and the Funds' solicitors the position in relation to litigation, claims and assessments; and
- Performing detailed testing of transactions and balances.

48. We are pleased to report that we did not identify any instances of concern with regard to the legality of transactions or events.

Qualitative aspects of accounting practices and financial reporting

49. We have considered the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided by the financial statements. Our findings are summarised below:

Qualitative aspect considered	Audit conclusion
The appropriateness of the accounting policies used.	<p>We have reviewed the significant accounting policies which are disclosed in the annual accounts of the Funds. We consider the policies to be appropriate to the Funds, however, we have noted that the Funds have departed from CIPFA Guidance in relation to investment management expenses.</p> <p>During 2015/16 CIPFA issued guidance stating that pension funds should only report the direct costs of using investment managers. The impact of this is that investment management costs associated with fund of funds transactions would not be reported. The Funds feel this would detract from the transparency of the accounts and have reported indirect costs of £4.16 million for Lothian Pension Fund and £0.33 million for Lothian Buses (there were no indirect costs for Scottish Homes).</p> <p>The impact of this accounting treatment is to increase the investment management expense which is offset by an increase in the change in market value of investments. The net impact on the fund account is therefore zero.</p>
The timing of the transactions and the period in which they are recorded.	We did not identify any concerns over the timing of transactions or the period in which they were recognised.
The appropriateness of the accounting estimates and judgements used.	<p>The Funds have significant levels of accounting estimates and judgements used by management in preparing the financial statements. The principal areas of estimation concern the valuation of unquoted private equity and infrastructure investments and the actuarial valuation of promised retirement benefits.</p> <p>We are satisfied with the appropriateness of the accounting estimates and judgements used in the preparation of the annual accounts. We have considered the disclosures around the estimates, including sensitivity analysis and concluded that they are appropriate.</p>
The potential effect on the financial statements of any uncertainties, including significant risks and related disclosures that are required.	We have not identified any uncertainties, including any significant risk or required disclosures, which should be included in the financial statements (beyond the existing disclosures made).

The extent to which the financial statements have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed.	From the testing performed, we identified no significant unusual transactions in the period.
Apparent misstatements in the Management Commentary or material inconsistencies with the financial statements.	The annual report and accounts contain no material misstatements or inconsistencies with the annual accounts in the Management Commentary.
Any significant financial statements disclosures to bring to your attention.	There are no significant financial statements disclosures that we consider should be brought to your attention. All the disclosures required by relevant legislation and applicable accounting standards have been made appropriately.
Disagreement over any accounting treatment or financial statements disclosure.	While some disclosure and presentational adjustments were made through the audit process, there was no material disagreement during the course of the audit over any significant accounting treatment or disclosure.
Difficulties encountered in the audit.	There were no significant difficulties encountered during the audit.

3

Financial management

Financial management

Overall conclusion

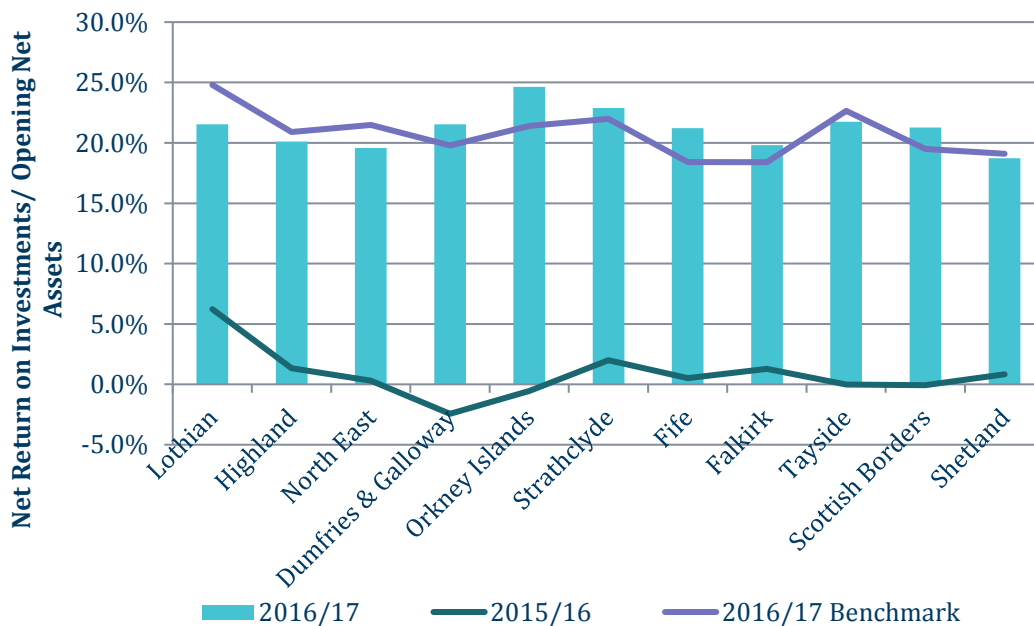
The Funds have effective arrangements in place for financial management and the use of resources

50. Overall, the Funds have effective arrangements in place for financial management and the use of resources. Our conclusion is based on a review of the Funds' financial performance against their investment strategy and our review of the system of internal control

The Funds' financial performance in 2016/17

The Funds were slightly behind the 1 year benchmark but achieved their longer term targets

51. The key financial indicator for the across pension funds in Scotland is the return on investments. Following a relatively poor performance across all investment funds in 2015/16 the investment performance has improved across all Scottish Finds in 2016/17.



52. The average return on investments in 2016/17 was 21.19% a significant increase compared to 0.86% in 2015/16.

53. The Lothian Pension Funds have consistently performed above the average figure.

54. The graph above focuses on the short term performance of the Scottish Pension Funds but the Funds investment programme recognises that long term performance is key to ensure the sustainability of the Funds. Consequently the Funds review performance against benchmark over one, five and ten years.

55. The Funds were slightly behind the one year benchmark on Lothian Pension Fund and Lothian Buses Pension Fund. The performance over the longer term is consistently meeting or exceeding benchmark which indicates the investment portfolio is being managed appropriately.

	1 year		5 years		10 Years	
	Return	Benchmark	Return	Benchmark	Return	Benchmark
Lothian Pension Fund	21.7%	24.8%	12.9%	11.4%	8.2%	6.6%
Lothian Buses	23.7%	24.2%	13.2%	11.5%	9.6%	8.0%
Scottish Homes	18.9%	18.7%	10.8%	10.7%	9.1%	9.1%

Financial Position

56. The net assets of the Fund continued to increase in 2016/17, reflecting the level of returns achieved in year and the relatively strong position of the market in year.

	2016/17 £m	2015/16 £m	% Movement
Lothian Pension Fund	6,594	5,434	21.3%
Lothian Buses	488	394	19%
Scottish Homes	171	150	14%

57. Although the net assets position is increasing the Funds' actuary, Hymans Robertson estimated that the present value of the promised retirement benefits had risen across Lothian Pension Fund and Lothian Buses Pension Fund by approximately 31%. Scottish Homes had a smaller increase of only 12%.

58. The actuarial calculations are based on the 2014 Actuarial Valuation rolled forward. It was noted by the Actuary in their report that the performance of real bond yields has declined in recent years meaning the funding levels set in 2014 are likely to be worse than predicted and the liability increased.

59. The liability figures do not appear in the primary financial statements and appear only in the notes to the accounts. This is in line with the options in the CIPFA Code of Practice on Local Authority Accounting.

60. This recognises that the liabilities are recognised on the employing bodies' balance sheets. However, the financial environment continues to be challenging and following the 2017 Actuarial Valuation it may become increasingly difficult for employers to meet the contribution demands of the Funds.

61. In addition to this there are a number of employers within the Lothian Pension Fund with fewer than 5 employees who may be in a position where the debt crystallises on the cessation of active members. Due to the low market yields it is anticipated that cessation valuations would show sizable deficits.

62. This has increased the risk of employers defaulting on the exit payments required to cover the liability attributable to their employees.

63. The Funds have recognised this as a significant risk and are taking steps to mitigate this risk. Lothian Pension Fund is working with the at risk employers to ensure they can continue to meet the contribution demands of the fund or can meet the cessation liability.

64. Lothian Pension Fund currently has a contingent asset of £0.33 million relating to unsecured assets due from ceased employers.

65. As this is deemed to be a significant risk to Lothian Pension Fund we recommend that increased disclosure around the nature of the risk, the level of at risk employers within the Fund and the potential impact on the funding level is included in the financial statements.

Action Plan Point 3

The Funds have effective budget setting and monitoring arrangements

66. We have considered the Funds' system of budgetary control and financial management and did not identify any significant deficiencies.

67. The Funds align their financial regulations and policies with the City of Edinburgh Council. The financial regulations were last subject to review in 2017 and were approved by the Council in June 2017.

68. The Pensions Committee consider the investments control environment and performance over the annual committee cycle in line with a formal long term agenda plan. Over the course of the financial year the Pensions Committee has taken reports on the investment strategy panel, investment principles and the performance of the Funds.

69. The Pensions Committee also receive a report on the financial performance of the Funds in year, encompassing the contributions received and pensions paid

along with the administration costs. Where there are variances adequate narrative is provided to ensure the Pensions Committee have an understanding of the reason for the movement and the action being taken by the Funds.

Prevention and detection of fraud and irregularity

70. Our audit was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity. We found the Funds' arrangements for the prevention and detection of fraud and other irregularities to be adequate.

Financial sustainability4



Financial Sustainability

Overall Conclusion

The Funds have effective arrangements in place to ensure the ongoing sustainability of the pension funds.

71. The Funds have a responsibility to pay pensions to members until the end of their life. The payments required are based on the contributions made by members over the course of their employment.
72. Overall we have concluded that the Funds have effective arrangements in place to ensure the ongoing sustainability of the pension funds. When assessing financial sustainability we have considered the contribution rates set, the Funding Strategy Statement and the Investment Strategies in place for the Funds.

Triennial Valuation

73. The Funds' undertook an actuarial valuation in 2014 in line with the requirements of the Local Government Pension Scheme Regulations 2014. The 2014 Actuarial Valuation was a triennial valuation with the purpose of setting rates for the three year period commencing 1 April 2015.
74. The 2014 Actuarial Valuation was undertaken by Hymans Robertson in accordance with Regulation 32 of the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008 as amended.
75. At the 2014 Actuarial Valuation the funding level reduced for Lothian Pension Fund but increased across Lothian Buses Pension Fund and Scottish Homes Pension Fund. The Lothian Buses Pension Fund was the only fund achieving its target funding level.

Funding level

	Actual 2014 (%)	Target (%)
Lothian Pension Fund	91.3%	100%
Lothian Buses	117%	100%
Scottish Homes	88.8%	91.5%

76. In light of the funding levels the 2016/17 financial statements show that the Lothian Pension Fund has now moved to a position where payments exceed contributions received.

	Lothian Pension	Lothian Buses	Scottish Homes
Contributions and transfers	201,849	9,801	675
Payments (including admin)	(211,085)	(12,522)	(7,540)
Net position	(9,236)	(2,721)	(6,865)

77. Lothian Buses and Scottish Homes have operated at a net withdrawals position for a number of years. This is due to the fact both schemes are now closed to members, with Scottish Homes having no active members. The Funds are managing their investment strategy to ensure there is adequate investment income to cover payments.

78. The next detailed actuarial valuation for the Funds will be carried out as at 31 March 2017 and at this stage the contribution rates required to support the Lothian Pension Fund back to fully funded status will be considered.

Funding Strategy Statement

79. The longer term sustainability of the Funds' is considered in the Funding Strategy Statement which was prepared in 2015 concurrently with the triennial actuarial valuation and creates a different strategy for each of the funds.

	Pension Fund Membership	Funding Strategy										
Lothian Pension Fund	<table border="1"> <caption>Lothian Pension Fund Membership</caption> <thead> <tr> <th>Category</th> <th>Percentage</th> </tr> </thead> <tbody> <tr> <td>Active</td> <td>43%</td> </tr> <tr> <td>Pensioners</td> <td>29%</td> </tr> <tr> <td>Deferred</td> <td>23%</td> </tr> <tr> <td>Dependants</td> <td>5%</td> </tr> </tbody> </table>	Category	Percentage	Active	43%	Pensioners	29%	Deferred	23%	Dependants	5%	<p>Lothian Pension Fund is open to new members with active members still being the highest proportion of members. Lothian Pension Fund has adopted a long term investment strategy split into 2 strategies. Strategy 1 applies to 99% of the employee liability and aims to maximise the investment return within reasonable and considered risk parameters.</p> <p>The second strategy invests in a portfolio of UK index linked gilts to reduce funding level and contribution rate risk to a level appropriate to their circumstances.</p>
Category	Percentage											
Active	43%											
Pensioners	29%											
Deferred	23%											
Dependants	5%											
Lothian Buses Pension Fund	<table border="1"> <caption>Lothian Buses Pension Fund Membership</caption> <thead> <tr> <th>Category</th> <th>Percentage</th> </tr> </thead> <tbody> <tr> <td>Active</td> <td>28%</td> </tr> <tr> <td>Pensioners</td> <td>34%</td> </tr> <tr> <td>Deferred</td> <td>29%</td> </tr> <tr> <td>Dependants</td> <td>9%</td> </tr> </tbody> </table>	Category	Percentage	Active	28%	Pensioners	34%	Deferred	29%	Dependants	9%	<p>Lothian Buses Pension Fund is closed to new members and the liabilities are expected to mature. A revised strategy was approved in March 2016 to be implemented over the period from 2016 to 2021. The revised strategy reduces the Fund's allocation to equities and increases the allocation to index gilts and fixed income assets. The revised strategy is designed to reduce risk in order to take account of the maturing employee liability.</p>
Category	Percentage											
Active	28%											
Pensioners	34%											
Deferred	29%											
Dependants	9%											
Scottish Homes Pension Fund	<table border="1"> <caption>Scottish Homes Pension Fund Membership</caption> <thead> <tr> <th>Category</th> <th>Percentage</th> </tr> </thead> <tbody> <tr> <td>Active</td> <td>17%</td> </tr> <tr> <td>Pensioners</td> <td>55%</td> </tr> <tr> <td>Deferred</td> <td>28%</td> </tr> <tr> <td>Dependants</td> <td>0%</td> </tr> </tbody> </table>	Category	Percentage	Active	17%	Pensioners	55%	Deferred	28%	Dependants	0%	<p>Scottish Homes Pension Fund currently has a funding arrangement in place with the Scottish Government, where the government is acting as guarantor for the scheme and provides funding on an annual basis to help fund the employee liability.</p> <p>A bespoke Investment strategy is in place to reduce the level of funding in equities and increase the level of funds invested in bonds. In line with this strategy the investments in equities reduced from 30% to 17.5% in 2016/17.</p>
Category	Percentage											
Active	17%											
Pensioners	55%											
Deferred	28%											
Dependants	0%											

■ Active
 ■ Deferred
 ■ Pensioners
 ■ Dependants

- 80.** As part of the triennial valuation process the Funds' Funding Strategy Statement is being reviewed and revised. In line with the Scheme Regulations the Funds' are making arrangements for consultation with scheme employers. The draft Funding Strategy Statement will be issued for consultation in late 2017.

Investment Strategy Panel

- 81.** The Pensions Committee has delegated responsibility for investment strategy to an Investment Strategy Panel made up of:
- Head of Finance, City of Edinburgh Council;
 - Chief Executive, LPFE Ltd;
 - Chief Investment Officer, LPFE Ltd;
 - Chief Finance Officer, LPFE Ltd; and
 - three external investment consultants.
- 82.** In 2016/17 Lothian Pension Fund set up a joint working arrangement with Falkirk Pension Fund which includes a joint Investment Strategy Panel. The role of this panel will be to advise the Finance Directors of each administering authority on the implementation of investment strategy. There has been collaborative investment in 2016/17 with 7 investments being made alongside Falkirk Pension Fund.
- 83.** The Funds' are committed to reducing costs thereby improving longer term sustainability through increasing collaboration with other Scottish Local Authorities.

5

Governance & transparency

Governance & transparency

84. Governance and transparency is concerned with the adequacy of governance, leadership and decision making, and transparent reporting of financial and performance information. The Funds are responsible for ensuring the proper conduct of their affairs including compliance with relevant guidance, the legality of activities and transactions and for monitoring the adequacy and effectiveness of these arrangements.

Overall conclusion

85. The Funds have appropriate governance arrangements in place. Our audit work has included reviewing corporate governance arrangements as they relate to the corporate governance framework in place, the information provided to the Pension Committee and Audit Sub-Committee and the risk management arrangements in place.

Governance Structure

86. The Pensions Committee, supported by an Audit Sub-Committee, has been delegated responsibility for governance by the City of Edinburgh Council, the administering authority.
87. As outlined by the City of Edinburgh Council Scheme of Delegation the Pensions Committee has responsibility for the administration, management and investment strategy for the Funds.
88. From 1 April 2015 all pension funds were required to introduce local pension boards in line with the Public Service Pension Act 2013. This is the second year of operation of the Pension Board.
89. The Pension Board meet quarterly on a concurrent basis with the Pension Committee.
90. The remit of the Pension Board is to support the Pension Committee in compliance with regulations and the requirements of the Pension Regulator. In line with legislation if more than half of the members of the Pension Board disagree with a decision of

the Pension Committee then they can request in writing that the Pension Committee review that decision. There have been no requests to review decisions in 2016/17.

Risk Management

91. A developed and integrated approach to risk management is a key feature of a robust system of internal control. The Pension Funds maintain a risk register in line with the City of Edinburgh Council Risk Management Policy and Procedures.
92. Risk management arrangements are firmly embedded in the governance process. The Pensions Committee receive a risk management update on a quarterly basis which provides information of the movement in risks and the actions being taken on the most notable risks.
93. The Pensions Audit Sub-Committee reviews the risk management process on an annual basis to ensure it is appropriate.
94. From our review of the risk management arrangements in place we have concluded that there are adequate arrangements in place at the Funds.

Internal Audit

95. An effective internal audit service is an important element of the Funds' governance arrangements. The Funds' internal audit service is provided by the City of Edinburgh Council via a co-source arrangement with PricewaterhouseCoopers (PwC).
96. Internal audit completed three reviews in year as follows:
- internally managed investments;
 - a vulnerability assessment for online modules accessible to employers and members of the Funds; and
 - governance of the Lothian Pension Fund Group.

97. The Internal Audit Plan was subject to scrutiny at the Pensions Audit Sub-Committee in December 2016. The Committee were satisfied that the level of review would provide them with adequate assurance in 2016/17.

98. During our audit we considered the work of internal audit wherever possible to avoid duplication of effort and make the most efficient use of the Funds' audit resource.

Standards of conduct

99. In our opinion the Funds' arrangements in relation to standards of conduct and the prevention and detection of bribery and corruption are adequate.

All non-executives should receive a formal induction	Boards should review the skills and expertise required on the Board and attract people to plug the gaps	Performance of non-executives should be assessed on a regular basis	Scrutiny efforts should be focused on organisational performance, financial and risk management
Performance information provided to the Board could be improved	Boards should aim to maximise openness and accessibility of papers	Declarations of interest should be considered at every meeting	Boards should review the use of Committees and ensure delegation levels are appropriate

100. Our conclusion has been informed by a review of the arrangements for adopting and reviewing standing orders, financial regulations and schemes of delegation and for complying with national and local codes of conduct.

The Role of Boards

101. In September 2010 the Auditor General for Scotland published a report aiming to assess the role and work of boards across 67 public bodies and 39 colleges. The report made a number of recommendations as follows:

102. As part of our audit work in 2016/17 we followed up on the Funds' response to the issues highlighted by Audit Scotland. Our aim was to identify any causes for concern or areas of good practice. Our detailed findings were submitted to Audit Scotland and are summarised below.

103. In our opinion arrangements for scrutiny and decision making are appropriate.

104. The Pensions Committee and Board members receive an induction which includes specific training on the activity of pension funds and investment management. Following the local elections in May 2017 there were 2 new Councillors elected to the Pensions Committee. Appropriate training for new members is scheduled for September 2017.

105. Due to the specialised nature of the Funds, it is vital that members have the appropriate knowledge and understanding to provide appropriate challenge and operate effectively. Training is therefore seen as a fundamental requirement for all Committee and Board members. Our review found that all Pension Committee and Board members met the requirement to have a minimum of 21 hours training during 2016/17.

106. The Pensions Committee and Pensions Audit Sub-Committee meetings are held in public, papers are available in advance and minutes of the meetings are published on the City of Edinburgh Council's website. Information about the Funds is published on the Funds' website including key strategic documents. Overall we have concluded there is a good level of transparency around the pension fund business.

6

Value for Money

Value for money

Introduction

107. Value for money is concerned with the appropriate use of resources and ensuring continuous improvement of services delivered.

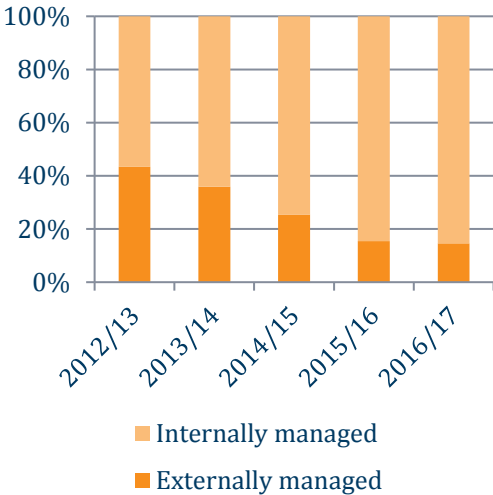
Overall conclusions

108. The Funds have appropriate arrangements in place to monitor performance of investments and the administration of the Funds. Our review was informed by the information provided to the Pensions Committee and the operations in place at the Pension Fund.

Investment operations

- 109. In October 2014 the Pensions Committee and City of Edinburgh Council agreed to the creation of two special purpose vehicles: LPFE Ltd and LPFI Ltd. Both companies were wholly owned and controlled by the Council.
- 110. In 2016/17 LPFI Ltd obtained Financial Conduct Authority authorisation (LPFE Ltd obtained this in 2015/16). The special purpose vehicles were established to support the investment programme of the in-house investment team by providing operational efficiencies.
- 111. Investments at the Funds are managed through a combination of external fund managers and the Funds' investment management team. The proportion of funds managed internally has increased over recent years.

Lothian Pension Fund proportion of internally managed Funds



- 112. The Funds' have used the internal investment team to drive efficiencies in year including a reduction of investment managers expenses as a proportion of net return on investment from 9% to 1% for Lothian Pension Fund.
- 113. Lothian Buses Pension Fund and Scottish Homes Pension Fund have followed the same pattern with a decrease in the level of externally managed investments by 12.9% and 54.9% respectively. Both funds have also seen a reduction of investment manager's expenses as a proportion of net investment to below 1%.

Monitoring investment performance

114. There is an annual review of investment performance in June. Due to the elections in 2017 the Pension Committee was cancelled, however, a briefing meeting was held for the newly formed Committee. From our attendance at this briefing and the Pensions Committee in year we concluded that Pension Committee and Board Members are engaged in monitoring the performance of investments.
115. In addition to monitoring at a Committee level the Funds' performance is reviewed by an external provider on a monthly basis. The external provider compiles information covering monthly, quarterly, yearly and 3 yearly performance measures. This information is presented to the Investment Strategy Panel to allow for scrutiny investment performance of the Funds.

Administrative Performance

116. The Funds' have developed a Service Plan covering the period 2016- 2018 which focuses on four key objectives:
- We put our customers first and aim to provide the very best service
 - Our people are at the very heart of our business and we work together to deliver our service
 - We strive to improve our services by thinking ahead and developing new solutions
 - We are committed to supporting a culture of honesty and transparency.
117. The Pensions Committee receive updates on the service plan at each meeting. The annual results for 2016/17 are presented in the Funds' Management Commentary. The Performance Report highlights that the Fund are meeting the majority of their targets (81%) with only 2 areas where performance was not in line with target levels:

- Overall staff satisfaction decreased in year from 73% to 70% which was below the target level of 75%.
- The target for the proportion of active members receiving their annual benefit statement by 31 August 2016 was 100% but the Funds' achieved a level of 99.6%. The issue of annual benefits statements by 31 August is a requirement of the Local Government Pension Scheme (Scotland) 2014. The statements not issued related to members employed on a casual basis prior to March but who did not contribute to the scheme up to the end of the year. The members should consider whether they deem this an issue which should be self-referred to the Pension Regulator.

Action Plan point 4

Tendering for Services

118. The Funds make use of a range of service providers including investment managers, an actuary and a custodian. In order to ensure the Funds are achieving value for money it is good practice to tender for services at set intervals.
119. The Funds follow the City of Edinburgh Council procurement procedures and maintain a contract register.
120. It was noted that two contracts were currently in their extension period and were due to go out to tender in 2017/18. We will consider the adequacy of this process as part of our 2017/18 audit procedures.

7

Appendices

Appendix 1: Management action plan

Our action plan details the control weaknesses and opportunities for improvement that we have identified during our audit.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist. The weaknesses or risks identified are only those which have come to our attention during our normal audit work, and may not be all that exist.

Communication of the matters arising from the audit of the annual report and accounts or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

Action plan grading structure

To assist the Funds in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been rated. The rating structure is summarised as follows:

Grade 5	Very high risk exposure – major concerns requiring Board attention
Grade 4	High risk exposure – material observations requiring senior management attention
Grade 3	Moderate risk exposure – significant observations requiring management attention
Grade 2	Limited risk exposure – minor observations requiring management attention
Grade 1	Efficiency / housekeeping point

Action plan point	Issue & Recommendation	Management Comments
1. Authorisation of journals	<p>Observation Our review of the journals environment found that there was a lack of segregation of duties over the posting of journals. Journals are currently posted by individuals without an authorisation process. Journals can be used to override controls and create fraudulent errors therefore it is crucial there are strong controls in place.</p> <p>Recommendation Whilst we were able to obtain alternative audit evidence to provide assurance that there were no material issues with regards to the posting of journals, we recommend that a review process for all journals is put in place.</p>	<p>Agreed the fund will undertake a review of the journals processes.</p> <p>All parties that use the Council's financial systems are affected by this finding. The Fund awaits the Council's response to the issue.</p> <p>The Fund is satisfied that there are sufficient controls in place to prevent an actual cash payment leaving the Fund without full authorisation and that the ability to post journals is limited to staff authorised to do so. The system also records the username of the person posting the journal.</p> <p>Action owner: John Burns</p> <p>Due Date: 31 January 2018</p>
Rating		
Grade 3		
Paragraph ref		
25		

Action plan point	Issue & Recommendation	Management Comments
2. Annual Governance Statement	<p>Observation We have reviewed the Funds' Annual Governance Statement and identified that improvements could be made. To be fully compliant with the Delivering Good Governance in Local Government guidance an action plan outlining the actions the Funds' will take to progress improvements in the Funds' governance process should be disclosed.</p> <p>Recommendation We recommend the Funds' consider the disclosures in the Annual Governance Statement to ensure they are meeting applicable guidance.</p>	<p>Agreed to review for next year's accounts</p> <p>Action owner: Struan Fairbairn</p> <p>Due Date: 31 March 2018</p>
Rating		
Grade 3		
Paragraph ref		
40		

Action plan point	Issue & Recommendation	Management Comments
3. Employer cessation liabilities	<p>Observation Lothian Pension Fund has identified that there are significant pressures facing the employing body members of the Fund. This has increased the risk of employers defaulting on payments required to cover the liability attributable to their employees.</p> <p>Recommendation We recommend that increased disclosure around the nature of the risk, the level of at risk employers within the Fund and the potential impact on the funding level is included in the financial statements.</p>	<p>Agreed to review disclosures in management commentary for next year's accounts after the completion of the 2017 triennial actuarial valuation.</p> <p>Contingent assets in respect of Funding Agreements for employers which have terminated membership of the Fund are disclosed to the extent that such default protection is provided to any aligned body (as defined in the Funding Strategy Statement) or other employers in the Fund. Such contingent assets do not have a material impact on net liabilities.</p> <p>Action owner: John Burns</p> <p>Due Date: 31 March 2018</p>
Rating		
Grade 3		
Paragraph ref		
63		

Action plan point	Issue & Recommendation	Management Comments
4. Annual benefits statements	<p>Observation The issue of all annual benefit statements by 31 August 2016 is a requirement of the Local Government Pension Scheme (Scotland) Regulations 2014. In 2016/17 the Funds' achieved 99.6% of the annual benefits statements by the deadline.</p> <p>Recommendation The Pension Committee members should consider whether they deem this to be an issue which should be self-referred to the Pension Regulator.</p>	<p>The Funds have considered this in line with the Pensions Regulator guidance and do not feel this would be of material significance and therefore have deemed it unnecessary to declare the breach to the Pensions Regulator.</p>
Rating		
Grade 2		
Paragraph ref		
116		

Appendix 2: Unadjusted differences

Board representations

We have requested that the signed representation letter, covering a number of issues, be presented to us at the date of signing the financial statements. We identified one unadjusted difference during our audit work. These differences are not considered to be material to the financial statements individually or in aggregate. The unadjusted items are included within the representation letter and shown below:

Unadjusted differences	Fund Account		Net Asset Statement	
	DR £'000	CR £'000	DR £'000	CR £'000
Investment Management Expenses	509			
Creditors				509
<i>Being the under declaration of output tax dating back to 2011.</i>				

Appendix 3: Respective responsibilities of the Pensions Committee and the Auditor

Responsibility for the preparation of the annual report and accounts

It is the responsibility of the Pensions Committee and the Chief Finance Officer, as Accountable Officer, to prepare financial statements in accordance with the Local Government (Scotland) Act 1973 and directions made thereunder.

In preparing the annual report and accounts, the Pensions Committee and the Chief Finance Officer, as Accountable Officer are required to:

- apply on a consistent basis the accounting policies and standards;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards as set out in the Code of Practice on Local Authority Accounting (the Code) have not been followed where the effect of the departure is material;
- prepare the accounts on a going concern basis unless it is inappropriate to presume that the Lothian Pension Fund will continue to operate.

The Chief Finance Officer is also responsible for

- keeping proper accounting records which are up to date; and
- taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditor responsibilities

We audit the annual report and accounts and give an opinion on whether:

- give a true and fair view, in accordance with applicable law and the Code, of the state of the affairs of the Funds as at 31 March 2016 and of the income and expenditure of the Council and its group for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the Code;
- they have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Authority Accounts (Scotland)

Regulations 2014 and the Local Government in Scotland Act 2003;

- the information given in the Management Commentary is consistent with the annual accounts.

We are also required to report by exception if, in our opinion

- adequate accounting records have not been kept;
- we have not received all the information and explanations we require for our audit;
- there has been a failure to achieve a prescribed financial objective.

Wider scope of audit

The special accountabilities that attach to the conduct of public business, and the use of public money, mean that public sector audits must be planned and undertaken from a wider perspective than in the private sector. This means providing assurance, not only on the annual accounts, but providing audit judgements and conclusions on the appropriateness, effectiveness and impact of corporate governance and performance management arrangements and financial sustainability.

The Code frames a significant part of our wider scope responsibilities in terms of four audit dimensions. As part of our annual audit we will consider and report against these four dimensions: financial management; financial sustainability; governance and transparency; and value for money.

Independence

We are required by International Standards on Auditing to communicate on a timely basis all facts and matters that may have a bearing on our independence. We can confirm that we have complied with the Financial Reporting Council's Ethical Standard. In our professional judgement the audit process has been independent and our objectivity has not been compromised. In particular, there have been no relationships between Scott-Moncrieff and the Pensions Committee or senior management that may reasonably be thought to bear on our objectivity and independence.



Scott-Moncrieff
business advisers and accountants

© Scott-Moncrieff Chartered Accountants 2017. All rights reserved. "Scott-Moncrieff" refers to Scott-Moncrieff Chartered Accountants, a member of Moore Stephens International Limited, a worldwide network of independent firms. Scott-Moncrieff Chartered Accountants is registered to carry on audit work and regulated for a range of investment business activities by the Institute of Chartered Accountants of Scotland.



Lothian Pension Fund
Lothian Buses Pension Fund
Scottish Homes Pension Fund

**Audited Annual Report and
Financial Statements 2016/17**



Contents

Foreword	3
-----------------------	---

Management Commentary

Introduction.....	5
Governance.....	8
Investments.....	10
Funding Strategy Statement.....	16
Financial performance.....	17
Performance	21

Financial Statements

Lothian Pension Fund Financial Statements.....	29
Lothian Buses Pension Fund Financial Statements.....	65
Scottish Homes Pension Fund Financial Statements.....	91
Statement of accounting policies and general notes.....	112
Statement of responsibilities for the Statement of Accounts.....	121
Independent Auditor’s Report.....	122

Governance

Annual Governance Statement.....	124
Governance Compliance Statement.....	129
Additional information.....	133

Foreword

Head of Finance, City of Edinburgh Council

Welcome to the Annual Report and Financial Statements for 2016/17 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund. The report keeps members, employers and other interested stakeholders informed about the activities and performance of the pension funds, as well as their investments and financial statements.

This year has seen no let-up in the challenges and pace of change both across the pensions sector generally and within the LGPS specifically. The Pensions Committee, Pension Board, together with officers of the Fund are ever mindful of our responsibilities to our 81,000 scheme members and 94 active employers. Therefore our decision making is always clearly focussed on working together to deliver the best outcomes for all our stakeholders.



We know that pensions can be difficult for scheme members to understand, and increasingly complex and challenging for employers to manage; they are a significant cost and short term decisions can have very long term effects. Our average pension in payment is £5,392, reflecting the earnings and work profile of our membership. We believe the LGPS offers a very safe way of saving for a secure income in retirement, particularly important for part time or lower paid employees. We remain committed to helping scheme members and employers understand the LGPS, to enable them to make informed and timely decisions. We continue to focus on investing in people and technology in order to maintain and drive up our high standards of service and performance. I am delighted that our service has been accredited by the Pension Administration Standards Association (PASA), the first Local Government Pension Fund to achieve this.

The LGPS is a Scotland-wide scheme and we continue to take a leading role nationally. Councillor Alasdair Rankin had served on the Scottish LGPS Scheme Advisory Board. Officers also provide advice to the Scheme Advisory Board.

The Scottish Government is encouraging LGPS funds to collaborate with each other. Our authorisation from the Financial Conduct Authority has enabled the expansion of our collaborative efforts over the year, enabling other LGPS funds to benefit from the Funds' expertise in infrastructure. A new collaborative model has been agreed with Falkirk Pension Fund which should bring further opportunities and efficiencies.

I would like to take this opportunity to record my thanks for the hard work of the Pensions Committee, Pension Board, fund advisers, employers and staff.

Hugh Dunn
Head of Finance
The City of Edinburgh Council

Report by the Chair of the Pension Board

The Pension Board comprises both employer and member representatives, and undertakes an important role in helping to ensure the correct governance and functioning of the Lothian Pension Funds.

Having on the 1st April 2016 taken on the role of Chairperson (the first 'employee' representative to do this) I am now able to provide the following information relating to the Board and it's work for the preceding year.

During this time, the Board itself has undergone some changes in membership, but I can confirm that none of these changes detracted in any way from the continuing and important work the Board undertook during the course of the year.

As an example of its diligence, all the Board members have undertaken the extensive training required to ensure their understanding of their role, general pensions issues and the operations of the Funds themselves, and as a result, even those Board Members who joined us late in the year fully met the LPGA Pension Board Members training requirements.



Report by the Chair of the Pension Board cont'd

The Board has, in the past 12 months, undertaken a considerable amount of work attending not only all of the meetings of the Pensions Committee and Pensions Audit Sub-Committee, but also ensuring their active participation at the Board's own quarterly meetings.

As part of its remit, the Board members have also maintained a positive involvement in relation to the funds governance and its consideration of the various environmental, social and governance (ESG) issues being brought to its attention.

During the course of the year, the Scottish Public Pensions Agency (SPPA) instigated a major review of the 'effectiveness of the governance' arrangements for all pension funds, in which the Board was fully and pro-actively involved. We provided both feedback on the Board's work so far in supporting the Funds and in respect of the actual remit of the review' itself and then ultimately provided in-depth feedback on the reviews findings.

The Board has also taken a very keen and active interest in the many ESG matters that were brought before the Pensions Committee for consideration during the year, and we have been instrumental in ensuring that the Funds and its managers continue to consider fairly these important issues whilst maintaining a clear perspective in relation to both its legal fiduciary duties and also its duty of care towards all its various Fund members.

I am grateful to all my Pension Board colleagues for their ongoing commitment to supporting the Board over the last year and for ensuring that both scheme members and employers continue to be well represented within the governance and running of the fund.

As required by the constitution, the chair of the Pension Board rotates annually between employer and member representatives, and Darren May, (an employer member from Scottish Water), was selected by the Board to take on this important role as and from 1 April 2017. I therefore take this opportunity to wish Darren well in his new role as our Chair for the incoming year and I look forward to continuing working with him and the Pension Board members along with the LGPS funds in the coming year.

Jim Anderson

Member Representative and Chair of the Pension Board

Report by the Independent Professional Observer

This is my third year as Independent Professional Observer for the pension funds. My function is to assist the Pensions Committee and Pension Board undertake their governance responsibilities effectively and efficiently. My role as a pension trustee and knowledge of institutional investment allows me to support the Committee and Board in ensuring the Funds comply with relevant pension legislation and requirements set out by The Pensions Regulator.

During the year, I held surgeries to assist the Pensions Committee and Pension Board in working collaboratively and efficiently together in their joint oversight of the pension funds. Topics such as funding, investment and collaboration have been considered in addition to the normal business of the funds.

The quality of engagement and discussion over the year has demonstrated a high standard of governance within the funds. I look forward to working with the new Pensions Committee following the Local Government Elections in May 2017 to provide continuity, knowledge and guidance to them.



Sarah Smart

Independent Professional Observer

Management commentary

Introduction

Customer Service

The quality of membership data has been a key area of focus for the Funds over recent years to ensure we meet The Pensions Regulator's standards. All but three employers are now providing monthly contribution data for each member which is enabling us to see changes in membership quickly and hence provide a better service. Work was also undertaken to tackle historic leavers where information had not been provided by their employer at the time of leaving.

The Funds also registered for the national Tell Us Once service which means we can now be informed about the death of a member notified to another public service. This makes it easier for relatives of deceased members to deal with us, as well as reducing the risk of over-paying pensions.

Over the year, the City of Edinburgh Council undertook a voluntary redundancy exercise as part of a significant transformation project. In view of the scale of this exercise, we reviewed the way we deal with retirements to maximise the use of our online service and speed up the process. As well as reducing the administration work involved, customer satisfaction also improved.

The Funds continue to monitor movements in membership numbers, in particular the impact of early retirement initiatives and auto-enrolment. The number of pensioners from the City of Edinburgh Council has increased significantly over the year because of the transformation project. Over the year, the numbers of pensioner members rose by 922. The number of active members for the Lothian Pension Fund has increased marginally by 378 due to auto enrolment.

Funding & Investment

Changes in membership of the Funds have implications for cashflow. On retirement there are immediate outflows due to the payment of tax free lump sums and pensions and a reduction to inflows as contributions cease. However, payment of strain costs by employers on early retirements helps to mitigate current cashflow pressures.

Lothian Pension Fund is now in a negative cash flow position where payments exceed contributions received. The Fund has targeted increased investment income in recent years and this is expected to exceed net cashflow for the foreseeable future. It is therefore not anticipated that the sale of investments will be required to meet this funding requirement. Lothian Buses and Scottish Homes Pension Funds expenditure continues to exceed income as both funds are closed to new members with Scottish Homes Pension Fund having no members paying in to the scheme. Investment income funds these shortfalls, together with asset sales for Scottish Homes Pension Fund.

All three Funds delivered strong investment performance over the year. Lothian Pension Fund's assets have increased by £1,161million, with investments returning 21.7% over the year, slightly behind the benchmark of 24.8%. The internal team manages a significant proportion of assets of all three pension funds in-house. For Lothian Pension Fund this includes approximately £3.4billion of listed equity assets and a currency hedging programme specifically designed to provide downside protection in times of market stress while participating in some, though not necessarily all, of any upward movement. The underperformance relative to the benchmark this year follows on from a period of significant outperformance (+6.2%) in the prior year (2015/16) and over longer term periods the Fund is meeting its objective, exceeding the benchmark but with lower volatility.

Despite this strong performance, liability values have grown faster as discount yields have fallen. Hence, overall funding levels have fallen. In advance of the 2017 actuarial valuations, Lothian Pension Fund's Actuary reviewed the suitability of the Contribution Stability Mechanism used for setting the employer contribution rates for long-term secure employers. The Actuary concluded that despite changes to market conditions and reducing certainty of full funding due to the outlook for investment returns, at present the Contribution Stability Mechanism remains appropriate for long-term secure employers. However, its ongoing suitability will be reviewed ahead of the 2020 actuarial valuation.

During the 2014 actuarial valuation, Lothian Pension Fund addressed the previous inconsistency between the actuarial and cessation valuations to raise awareness of pension deficits and reduce the risk of employers being unable to pay deficits when their last active member leaves. During 2016/17, the Fund, in consultation with external advisers, has drawn up a funding agreement to address repayment of the cessation debt in order to avoid employer default or insolvency.

This agreement allows for repayment of the cessation debt over longer terms, and in special circumstances, for repayment of less than the full cessation debt. The standard agreement is tailored to each employer's circumstances, taking into consideration the employer's financial circumstances and ability, where applicable, to offer security over assets.

The Pensions Committee regularly considers the legal responsibilities of administering the Funds and its fiduciary duty to members and employers. During the year, the Scheme Advisory Board of the Scottish Local Government Pension Scheme sought a legal opinion on how Pension Committees in Scotland should exercise their fiduciary duty when investing pension fund money. The Committee considered this legal opinion and agreed that it reaffirmed that the approach taken by the Funds is appropriate. Non-compliance with the fiduciary duty could leave the Council and Pensions Committee open to legal challenge or otherwise have an adverse impact on the Council, the Funds and their stakeholders. However, there has been a significant increase in lobbying from external interest groups on certain investments and the Funds continue to engage with these groups as appropriate.

Collaboration with other Pension Funds

LPFI Limited, was granted FCA authorisation in June 2016 which facilitates collaboration with other pension fund investors to bring economies of scale. A new corporate structure, including two new companies (LPFI Limited and LPFE Limited), was introduced in 2015 to support the in-house investment team and create efficiencies. LPFE Limited, employs staff and facilitates separate governance and control for the in-house investment team. Collaboration allows other funds to benefit from the commercial advantage that the existing in-house team has in the market to bring tangible benefits through scale investing. In addition, sharing costs between collaborating funds allows reinvestment in the systems and in-house team to improve long-term sustainability.

Lothian Pension Fund has provided Falkirk Council Pension Fund with support on investment matters, including assisting with infrastructure investing, for the past five years. With Lothian's recent FCA authorisation, a review of the arrangements and a new collaborative model, including a joint Investment Strategy Panel, has been agreed. The Pensions Committee of Falkirk Council will agree investment strategy but will now delegate the implementation of strategy, including selection of investment managers, to officers. This governance model is similar to that of Lothian Pension Fund. The new joint Investment Strategy Panel will advise the Finance Directors of each administering authority (the City of Edinburgh Council and Falkirk Council) on implementation of investment strategy. The assets of Lothian Pension Funds and Falkirk Council Pension Fund will remain separate and investment strategy decisions retained by the respective Pensions Committees.

During 2016/17, Lothian Pension Fund has made seven investments alongside Falkirk Council Pension Fund and one with Northern Ireland Local Government Officers' Superannuation Committee. Further collaboration with other Scottish Local Government Pension Scheme partners is expected in 2017/18.

Awards

During the year, we retained the Customer Service Excellence award once again demonstrating commitment to customers. In March 2017, we became the first UK Local Government Pension Scheme fund to be awarded accreditation from Pension Administration Standards Association (PASA), which promotes a high standard for administration services for UK pension schemes. Accreditation involved a three-day site visit undertaken by two independent assessors. The award means the Fund has been independently recognised by PASA for delivering good quality administration, and showing a commitment to ongoing improvement. We use the standards to improve various areas of our service including procedure manuals, performance reporting and business continuity planning.

We also received five pension industry awards this year. At the Local Government Investment Awards 2016 we won Fund of the Year (over £5billion) for Lothian Pension Fund and Fund of the Year (under £750million) for Lothian Buses Pension Fund. At the Professional Pension's Pension Scheme of the Year Awards we were winner in the Defined Benefit Communications category and in the LAMP magazine investment awards, we were successful in the categories Investment Performance, Small LGPS Fund and Investment Strategy.

Challenges

Continuing budgetary constraints across the public and charity sectors are expected to lead to further accelerated increases in pensioner numbers and an increasing number of admitted bodies seeking to exit Lothian Pension Fund. There is also a risk that members decide to opt-out of the Funds on grounds of affordability or lack of appreciation of the value of pension benefits. Together with the new pension freedoms and pension auto-enrolment, these will further impact on the Funds membership, liabilities and cashflow.

Despite strong investment performance since the last actuarial valuation, liability values have grown faster as discount yields have fallen. Hence, the overall funding levels have fallen and the 2017 actuarial valuation is likely to prove

challenging. Further, there is greater oversight and scrutiny of funding plans for all LGPS funds as a result of the Public Service Pensions Act 2013. The Government Actuary's Department has carried out a dry-run analysis on the 2014 valuations in Scotland. The results identified differences in the way information is presented and work is ongoing amongst actuarial firms and funds to address inconsistencies. They noted different financial assumptions, which may reflect local circumstances, although the evidence at this stage is limited. The analysis may influence the approach to the 2017 actuarial valuation.

There has always been interest from members and specific campaign groups in investments and over recent years this has increased significantly. There is an ongoing need to be clear, open and transparent in communicating investment strategy and the way in which the Funds must invest in the best interests of members and employers.

To ensure we meet these challenges we have four objectives for our service:

- We put our customers first and aim to provide the very best service
- Our people are at the very heart of our business and we work together to deliver our service
- We strive to improve our services by thinking ahead and developing new solutions
- We are committed to supporting a culture of honesty and transparency.



Hugh Dunn
Head of Finance
The City of Edinburgh Council
27 September 2017



Clare Scott
Chief Executive
Lothian Pension Fund
27 September 2017

Governance

The City of Edinburgh Council is the administering authority for the Funds and delegates pension matters to the Pensions Committee and Pensions Audit Sub-Committee. The Pensions Committee members act as 'quasi trustees' and held four meetings during the year with the Pensions Audit Sub-Committee meeting three times.

The table below shows the membership of the Committees to 31 March 2017 and the current membership following the Local Government elections held on 4 May 2017.

1 April 2016 to 3 May 2017	May Election 2017
Pensions Committee	Pensions Committee
Councillor Alasdair Rankin (Convener)	Councillor Alasdair Rankin (Convener)
Councillor Maureen Child	Councillor Maureen Child
Councillor Jim Orr	Councillor Cameron Rose
Councillor Bill Cook	Councillor Adam McVey
Councillor Cameron Rose	Councillor Claire Miller
John Anzani (member representative, Midlothian Council)	John Anzani (member representative, Midlothian Council)
Richard Lamont (employer representative, VisitScotland)	Richard Lamont (employer representative, VisitScotland)
Pensions Audit Sub-Committee	Pensions Audit Sub-Committee
Councillor Cameron Rose (Convener)	Councillor Cameron Rose
Councillor Jim Orr	Councillor Maureen Child
Councillor Bill Cook	John Anzani (member representative, Midlothian Council)

The Pension Board

The Pension Board was set up on the 1 April 2015 as a result of the Public Services Pensions Act 2013 and the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014.

The role of the Pension Board is to help ensure that the operation of the Funds is in accordance with the applicable law and regulation. The Board attends all Pensions Committee meetings and has appointed two representatives to attend Pensions Audit Sub-Committee meetings. The membership comprises of ten members, five representatives appointed from the employer bodies and five members appointed by trade unions representing the membership of the Funds.

The Pension Board membership for the period 1 April 2016 to 31 March 2017 membership was as follows. There were two member vacancies at 31 March 2017.

Member representatives

Jim Anderson (Chair)	Unison
Catrina Warren	Unison
Thomas Carr Pollock	GMB
Graeme Turnbull	UCATT (to 26 January 2017)
John Rodgers	Unite (to 14 March 2017)

Employer representatives

Eric Adair	EDI Group
Darren May	Scottish Water
Sharon Dalli	Police Scotland (from 23 September 2016)
Paul Ritchie	East Lothian Council (from 5 September 2016)
Alan Williamson	Edinburgh College (from 2 September 2016)
Simon Belfer	Napier University (to 10 June 2016)
Linda McDonald	Handicabs (to 1 July 2016)
Rucelle Soutar	The Royal Edinburgh Military Tattoo (to 20 July 2016)

Pensions Committee and Pension Board training

The Committee and Board members must attend no less than 21 hours of training per year as outlined in the Funds' training policy which is available on our website at www.lpf.org.uk. All new members of the Pensions Committee and Pension Board attend induction training. Other training included fiduciary duty, investment markets after Brexit, collaboration and investment pooling. All members of the Committee and Board achieved the required training hours during 2016/17. Pensions Committee members collectively attended 322 hours of training over the year and members of the Pension Board undertook 288 training hours.

Investment Strategy Panel

The Pensions Committee sets the overall investment strategy with the implementation of that strategy, including investment monitoring, delegated to the Executive Director of Resources who takes advice from the Investment Strategy Panel. The Investment Strategy Panel meets quarterly and comprises the Executive Director of Resources of the City of Edinburgh Council, the Chief Executive of Lothian Pension Fund, Chief Financial Officer of Lothian Pension Fund and Chief Investment Officer of Lothian Pension Fund along with external advisers. The external advisers are currently Gordon Bagot, Scott Jamieson and KPMG, represented by David O'Hara.

Lothian Pension Fund staff

The day-to-day running of the three pension Funds is carried out by the Investment and Pensions service division of the Resources Directorate within the City of Edinburgh Council. The Division functions include investment, pension administration, communications and accounting. The investment responsibilities include carrying out in-house investment management and the monitoring and selection of external investment managers.

In February 2015, two limited companies (LPFE Limited and LPFI Limited) were established to facilitate the development of the internal investment capabilities and improve governance as well as delivering efficiencies for the administration of the Funds. Both companies are wholly owned and controlled by the City of Edinburgh Council as the administering authority of the Funds. LPFI Limited has been established to support the investment programme of the in-house investment team by providing operational and other efficiencies. LPFI Limited was authorised by the Financial Conduct Authority (FCA) in June 2016.

In 2015, key investment staff were transferred to LPFE Limited. As part of the transfer new terms and conditions were introduced which includes increased notice periods to reduce the risks facing the Funds. A second phase to transfer the remaining staff to LPFE Limited is currently ongoing. This will result in a more streamlined organisation better able to facilitate the collaborative efforts with other local government pension funds that are currently being explored.

Over the year, senior officers were:

- Hugh Dunn, Acting Executive Director of Resources, The City of Edinburgh Council
- Clare Scott, Chief Executive of Lothian Pension Fund
- Bruce Miller, Chief Investment Officer of Lothian Pension Fund
- Struan Fairbairn, Chief Risk Officer of Lothian Pension Fund
- John Burns, Chief Finance Officer of Lothian Pension Fund
- Esmond Hamilton, Financial Controller of Lothian Pension Fund.

Scheme Advisory Board

The Scheme Advisory Board for the Local Government Pension Scheme in Scotland was set up following the Public Service Pensions Act 2013. The Board's main function is to advise Scottish Ministers, when requested, on the desirability of changes to the Scheme. They can also provide advice to scheme managers and pension boards in relation to effective and efficient administration and management of the Scheme in Scotland.

The membership of the Scheme Advisory Board comprises of seven member representatives and seven employer representatives and a Joint Secretary is appointed in support of each of the Member and Employer groups. Councillor Rankin was a member of the Scheme Advisory Board over the year. Officers of Lothian Pension Fund have also been called upon to advise the Board and its Joint Secretaries. There is more information on the Scheme Advisory Board at www.lgpsab.scot.

Investments

Investment Markets

UK economic growth moderated further in 2016, slowing from 2.2% in 2015 to 1.8% in 2016, with political events dominating the news over the year.

Towards the end of June, the UK voted to leave the European Union, a result which was largely unanticipated by most investors. Global equity markets fell for two days before steadying and recovering most of their ground by the end of the month. However, the pound weakened sharply following the result, declining by almost 15% against the dollar, contributing to an increase in expected inflation over the next year. UK bond markets rose on fears of weaker economic growth.

Anticipating a potential slowdown in the economy, the Bank of England cut interest rates in August to a historic low of 0.25%. Subsequent economic news pointed to the UK economy faring better than expected, with the Bank revising its 2017 growth forecasts upwards from 1.4% in November 2016 to 2.0% in February 2017.

Following the EU referendum, investor attention focused on the November US Presidential election. Having fallen prior to the election, equity markets then recovered strongly following another unexpected result, confounding those that had predicted market turmoil accompanying a Trump victory. Signaling its confidence in the state of the US economy, the US Federal Reserve raised interest rates during December 2016 and then again in March 2017. While signalling that further rate rises would be likely over the remainder of 2017, the chair of the Federal Reserve Bank also noted that the outlook remained uncertain.

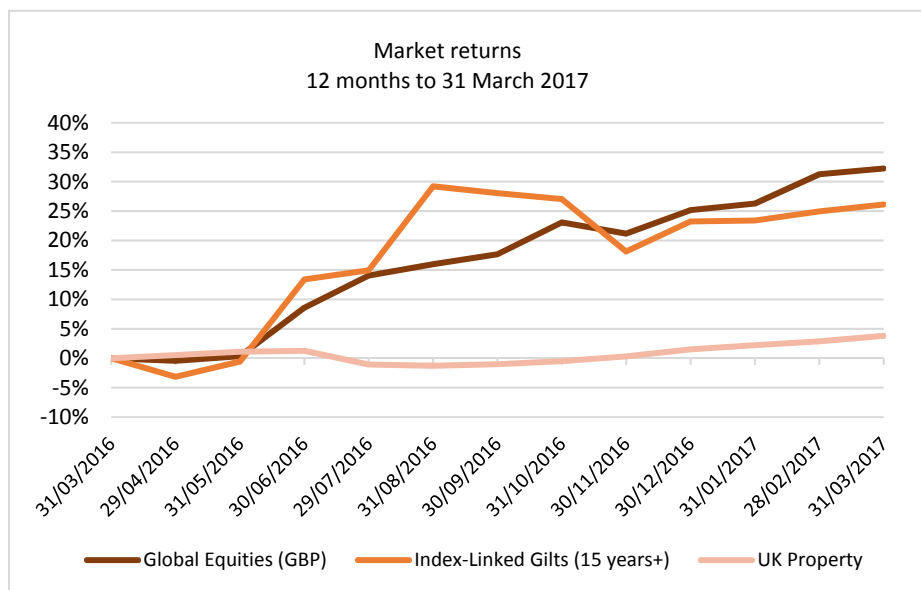
In December, the European Central Bank (ECB) voted to extend its quantitative easing programme by a further nine months to the end of 2017, as estimates suggested inflation would remain below its 2% target in 2019. The Bank of Japan left its bank rate unchanged over the year and maintained its ongoing quantitative easing programme.

For the 12 months to 31 March 2017, equity market returns for sterling-based investors were boosted by the immediate drop in the currency after the referendum, and then further weakness as investors priced in the likelihood of an unpleasant Brexit in economic terms. Index-linked bonds delivered strong returns over the year, as bond investors also priced in the likelihood of weaker UK economic growth. The weaker UK outlook also contributed to subdued returns from UK property, with rental income offsetting a small decline in capital values.

The outlook for the global economy – steady developed market growth and mixed conditions across emerging markets – has remained broadly constant over the past year. Recent divergence in central bank monetary policy suggests the US is ahead of the rest of the world in its economic cycle. Trump's pre-election promises of higher infrastructure spending and tax reform has been positive for equities but negative for US bonds.

However, the prospect of the US turning inwards to support its domestic economy also looms, which would be negative for global growth and raise the risk of a global recession.

The year ahead also sees potential for further surprises on the political front, most notably in Europe, where elections in France, the UK, and Germany fall due.



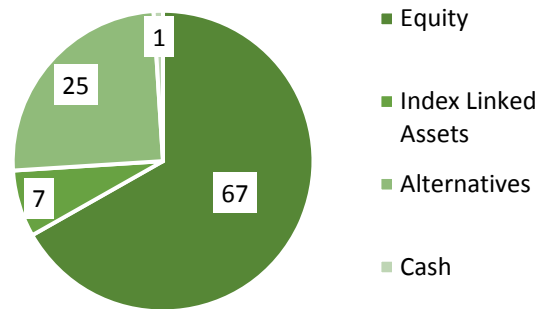
Investment strategies

The review of investment strategies for all three Funds during 2012 resulted in long term plans to achieve a reduction in investment risk as the Funds mature. The investment strategies were again reviewed during 2015/16, taking into account the results of the 2014 actuarial valuations. As at 31 March 2017, the three funds (Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund) were invested broadly in line with their target asset allocations, as expected.

To provide suitable investment strategies for the differing requirements of employers, **Lothian Pension Fund** currently operates two investment strategies.

Most employer liabilities are funded under Strategy 1, which adopts a long-term investment strategy, aiming to maximise the investment return within reasonable and considered risk parameters and hence minimise the cost to the employer. The investment strategy is set at the broad asset class level of Equities, Index-Linked Gilts and Alternatives, which are the key determinants of investment risk and return.

Lothian Pension Fund Actual Asset Allocation Strategy 1 (%) at 31 March 2017

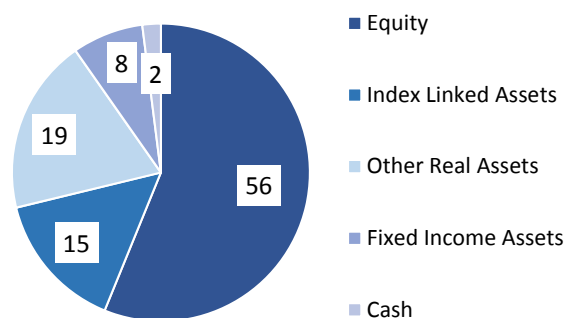


In 2015, the Pensions Committee agreed that there was no reason to amend the planned changes to Strategy 1. Lothian Pension Fund will continue to implement that strategy over 2017, and undertake a further review when the results of the 2017 actuarial valuation are available.

A small number of employers are funded in Strategy 2, which invests in a portfolio of UK index-linked gilts to reduce funding level and contribution rate risk to a level appropriate to their circumstances. The liabilities funded by Strategy 2 represent less than 1% of total Lothian Pension Fund liabilities.

For **Lothian Buses Pension Fund**, the review of strategy had greater implications. In March 2016, the Pensions Committee agreed a revised long term strategy allocation for the five-year period 2016-21. This involves making meaningful changes to asset allocation over that timeframe reflecting the requirement for greater funding stability as the Fund matures. (The Fund is closed to new entrants and is maturing at a faster pace than the Lothian Pension Fund.) In addition, as Lothian Buses Pension Fund is defined in regulations as a sub-fund of Lothian Pension Fund, the Pensions Committee agreed that the option for it to be merged into Lothian Pension Fund would be explored in consultation with stakeholders. This will be progressed during 2017, and the investment strategy implemented gradually over 2016-21.

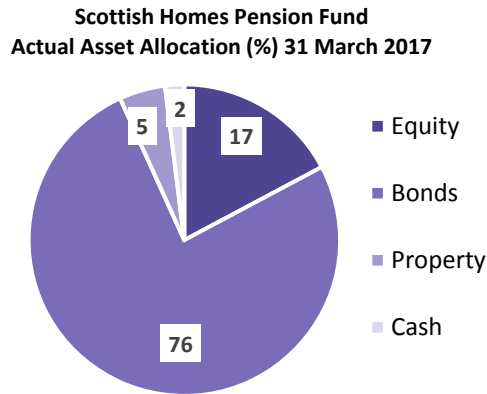
Lothian Buses Pension Fund Actual Asset Allocation (%) at 31 March 2017



During the year to end March 2017, Lothian Pension Fund and Lothian Buses Pension Fund continued to reduce equity holdings and to make new commitments to alternative assets, including infrastructure investments in the UK and overseas. The two funds invest in private markets, selecting specialist managers to access a wide range of opportunities that are not available in the public markets. Over the past 10+ years, the funds has built a portfolio of private market assets in equity, debt, real estate, timber and especially in infrastructure, which is the largest proportion of the private market assets held and is described in more detail below. For the Lothian Buses Pension Fund, the remaining externally managed index-linked gilts mandate was brought in-house during the year to be managed internally, reducing risk and resulting in savings on ongoing investment fees.

For **Scottish Homes Pension Fund**, the strategic review concluded that a less prescriptive investment and funding strategy would allow a higher-yielding investment strategy and a more flexible approach to setting contributions from the Scottish Government.

The current investment strategy adjusts asset allocation based on the evolution of the funding level. The Fund's current strategy is bond-focused and generates an annual income yield of less than 2% and, given its maturity, it is required to sell assets on a regular basis to pay pensions.



The Scottish Homes Pension Fund investment strategy was adjusted through the year as its funding level continued to improve, resulting in a reduced equity target allocation of 17.5% at 31 March 2017, compared to 30% at the previous year-end.

In addition, during March 2017, the assets previously managed by State Street were transferred to be managed internally. Management of the bond portfolios was brought in-house to improve cash-flow matching of the assets with future liability payments and management of the equity portfolios was brought in-house to improve the cash-flow generation of the equity assets.

Strategies for all three funds are implemented and monitored by an experienced internal team of investment professionals supported by external advisers. Over recent years, the internal team has expanded with very positive effects on costs and capabilities. This is reflected in two structural shifts. Firstly, the percentage of Lothian Pension Fund's listed equity assets managed internally has risen from 23% to more than 85% and most publicly traded bond assets are also now managed internally. Secondly, the Fund has altered the construction of the listed equity portfolios, increasing the global mandates from 32% to more than 85%. Despite these large changes in the Fund, performance equity returns have been ahead of benchmark by 1.5% per year over the last five years and this has been achieved with lower risk. The Fund's guiding principle is to use strong internal investment capabilities to their maximum potential and to retain external managers for specialist mandates.

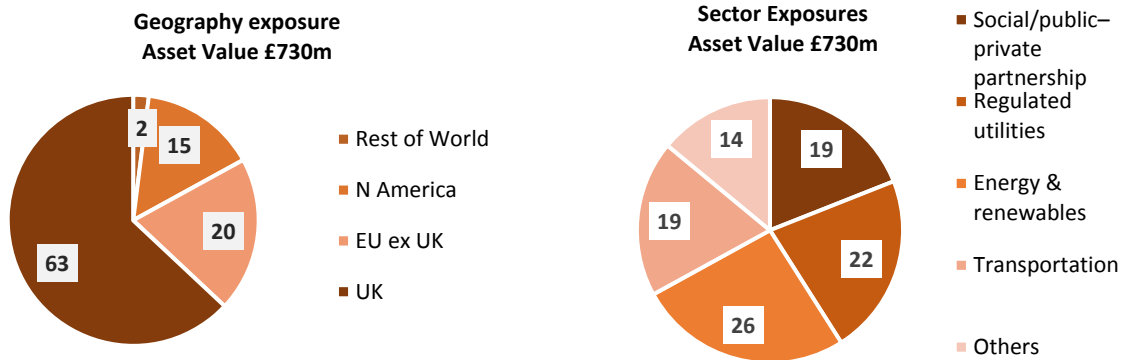
Infrastructure Investment

Infrastructure investment continues to receive publicity as the UK and Scottish governments encourage Local Government Pension Schemes to increase their investment in this area. Infrastructure investments may offer the potential to generate attractive risk-adjusted returns based on cash flows that are often linked to inflation and can play a diversifying role in the Funds' strategies.

Over the last decade, the Fund has developed its reputation, networking and execution capabilities to secure access to investment opportunities within this market niche. The Funds' experienced team appraises, models and invests in primary and secondary funds as well as co-investments to achieve its target allocation in a cost-effective manner. An important element of the implementation strategy is to work with managers to ensure execution certainty and to fully understand transaction fees.

Infrastructure investments represented 10% of the value of the Lothian Pension Fund at 31 March 2017, one of the largest and most diversified allocations compared with other UK Local Government Pension Funds. Lothian Buses Pension Fund investments in infrastructure accounted for 9% at 31 March 2017. Of the combined £730 million (31 March 2016: £439m) invested in infrastructure, 63% is invested in a diverse range of projects in the UK.

Lothian Pension Fund and Lothian Buses Pension Fund combined infrastructure investment allocations are illustrated below.



The market value of infrastructure investments in the UK at 31 March 2017 was £461million. The map and table shows the location of the major UK infrastructure investments.



Location	Sector - Subsector	%
Worthing	Utility - Water	6.5
Walsall	Utility - Water	5.3
Various	Renewables - Solar	5
Manchester	Energy meters	4.7
Redhill	Roads	4.7
Livingston	Energy meters	4.6
Liverpool	Ports	4.5
Isle of Man	Utility - Gas	4.5
Perth	Renewables - Hydro	4.3
Warwick	Utility - Gas	4
London	Sewage system	3.4
Barnsley	Utility - Water	2.3
North Sea	Pipeline	2.3
London	Utility - Water	2.2
Edinburgh	Ports	2.1

Location	Sector - Subsector	%
West Lothian	Renewables - Wind	1.9
Newport Pagnell	Motorway service	1.8
Dudley	Healthcare	1.6
Winchester	Telecommunication	1.3
Dundee	Education	1.2
Suffolk	Utility - Electricity	1.2
Tayside	Healthcare	1.1
London	Utility - Gas	0.8
Birmingham	Roads	0.8
London	Roads	0.7
Nottinghamshire	Healthcare	0.7
North Wales	Utility - Electricity	0.6
Essex	Education	0.6
London	Healthcare	0.6
Corsham	Defence	0.6

During 2016/17, Lothian Pension Fund and Lothian Buses Pension Fund completed two primary fund investments, acquired two secondary fund interests at material discounts to net asset value and invested in eight co-investment and/or specified asset investment vehicles. Approximately £245 million has been invested over the year in UK, European and infrastructure assets, including UK utilities, concessions and contracted infrastructure.

Over the last year, Lothian collaborated with Falkirk Council Pension Fund on seven infrastructure investments. A staff secondment arrangement shares internal staff costs between the Funds, supporting Falkirk's strategy to increase its allocation to UK infrastructure and giving both Funds greater scale and so access to opportunities that would not have otherwise been available.

During the year, Financial Conduct Authority approval was granted to LPFI Limited to enable us to more effectively collaborate in this sector, and for Lothian to benefit from scale in the market whilst further supporting other institutional pension funds in accessing infrastructure markets.

Responsible Investment

The Funds' policy on responsible investment stems from its fiduciary duty to its members and employers, which was endorsed by a legal opinion in September 2016 on the responsibilities of Scottish Local Government Pension Scheme funds (available to view at www.lgpsab.scot). The Funds are regularly approached by groups that lobby for the divestment of the shares of companies operating in certain industries, most recently those in defence and fossil fuels. The issues raised often involve complex social, legal and moral issues.

The Fund invests only in legal businesses and is an active shareholder with a view to enhancing the long-term value of its investments. Environmental, social and governance (ESG) issues are taken into consideration in the investment process in a manner which is consistent with the fiduciary duty to provide the highest standard of stewardship on behalf of the members and employers.

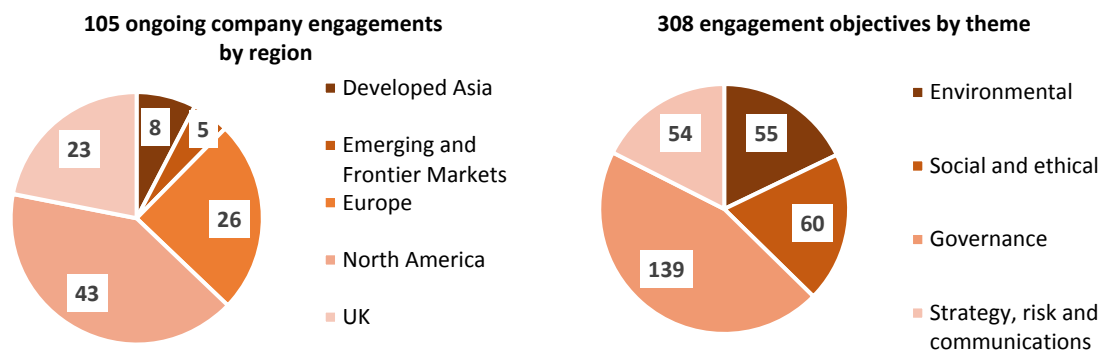
Robust arrangements are in place to ensure that the Funds' shareholdings are monitored and appropriate voting and engagement activity is undertaken with the aim of bringing about positive long term change at companies through a focused and value oriented approach. Share ownership brings with it the right to engage with management to affect strategic change in a positive direction. Divestment relinquishes that right. The Funds, however, do disinvest from shares where financial risk of loss is expected to outweigh reward.

The Funds have been a signatory to the Principles for Responsible Investment (PRI) since 2008. The PRI undertakes a detailed annual assessment of the Funds and their responsible investment activities. It publishes Transparency and Assessment Reports on the Funds, both of which can be found on the Fund’s website. The Assessment Report benchmarks performance against the Funds’ history and against peers, and the latest report published in 2016 is very favourable. The Funds are also a Tier 1 signatory to the Financial Reporting Council (FRC) UK Stewardship Code.

During 2016/17, voting and engagement activities related to the Funds’ shareholdings were largely undertaken by Hermes Equity Ownership Services (EOS). Baillie Gifford and State Street also took direct responsibility for stewardship issues for the investments they managed for the Funds.

Hermes EOS collates voting and engagement data for the Funds and reports this for calendar year periods. During calendar year 2016, the Funds voted at the annual meetings of the 541 companies in which it was invested. There were votes on 7,525 resolutions, and the Fund opposed 524 of them. In addition, Hermes EOS engaged on the Funds’ behalf with companies across the world on topics such as board structure, executive compensation and climate change. These are summarised in the charts below. By collaborating with Hermes and their other clients and other local authorities, the Fund’s influence is much enhanced with investee companies.

Engagement activities are also undertaken on behalf of the Fund and approximately 70 other local authority pension schemes in the UK by the Local Authority Pension Fund Forum. Councillor Alasdair Rankin, Convener of the Pensions Committee, was nominated to the Executive Committee of the LAPFF. He replaces Pensions Committee Member Councillor Cameron Rose, who had served on LAPFF’s Executive Committee for 10 years, latterly as Vice Chair. Membership of the LAPFF Executive entails meeting with the boards of companies and attending company Annual General Meetings to represent shareholders’ interests.



There has been notable success in engagement surrounding the ‘Aiming for A’ initiative that was launched last year. ‘Aiming for A’ seeks to implement strategies to limit man-made climate change to 2°C, and to demand that companies explain how they plan to achieve this. A resolution filed at the Chevron meeting and supporting these goals garnered over 40% votes in favour (the highest ever for a shareholder resolution for that company) and engagement with French oil company Total led to the company to announce goals in line with the ‘Aiming for A’ objectives.

The Fund continues to monitor the evidence on the impact of ESG on investment returns, and notes evidence that the shares of companies with improving ESG ratings provide better investments than those that are simply highly rated. As such, engaging with companies to improve ESG practices can lead to better long term outcomes for the Funds.

In summary, the Pensions Committee undertakes regular training to understand the legal responsibilities that its fiduciary duty to its members, and to its employers, entails. The Funds are committed to responsible investment with a view to raising corporate standards. It does this by voting on all stocks and engages with companies with poor corporate practices. It engages individually and collectively with other investors to maximise its influence as a shareholder to enhance shareholder returns and effect positive change for society.

Funding Strategy Statement

The Funding Strategy Statement sets out how we balance the potentially conflicting aims of affordability and stability of employers' pension contributions whilst taking a prudent long-term view of funding pension liabilities. The Funding Strategy Statement was revised at the 2014 Actuarial Valuation and further revised in November 2015. It can be viewed on our website at www.lpf.org.uk/publications. The Statement covers the funding strategies of each of the three Funds.

The Funding Strategy Statement will be reviewed at the 2017 Actuarial Valuation with the Actuary in consultation with employers.

The Fund is seeking to enhance the transparency of the fund assets attributable to each employer and, to that end, has introduced a system of investment unitisation (asset tracking). This enables investment assets for each employer to be tracked monthly, with the cash flow of an employer resulting in either a purchase or sale of units. The aim is to implement this change at the 2017 actuarial valuation, and data has been loaded to the system retrospectively in readiness. Another benefit of the system is that it also facilitates the future provision of more tailored investment strategies for employers if required.

Financial performance

Administrative expenses

A summary of the Funds' administrative expenditure for 2016/17, against the budget approved by Pensions Committee, is shown in the table below.

The budget focuses on controllable expenditures and therefore excludes all benefit payments and transfers of pensions from the Funds. Similarly, income does not include contributions receivable and pension transfers to the Funds. The total net cost outturn of £8,385k against budgeted of £12,242k represented an underspending of £3,855k (31.5%) for the Funds. The key budget variances serving to generate this underspending were:-

- Investment management fees – Invoiced - £2,534k underspend. This saving arose from continued greater use of in-house investment management expertise, with assets transferred from an external global equity manager in March 2016. The budget for external fund management costs was set prior to this in-sourcing having been anticipated.
- Other third party payments - £651k underspend. This saving arose primarily from investment broker research costs continuing to be paid via commission, rather than being invoiced directly. The Funds also had an underspend on budgeted broken deal costs in relation to its co-investment infrastructure investments.
- Employees - £467k underspend. This arose from savings in unfilled posts, partly due to the timing of recruitment during the financial year.

	Approved budget	Actual outturn	Variance
	£000	£000	£000
Employees	2,906	2,439	(467)
Property	195	211	16
Plant and Transport	41	38	(3)
Supplies and Services	1,195	1,102	(93)
Investment Managers Fees - Invoiced	7,120	4,586	(2,534)
Other Third Party Payments	1,375	724	(651)
Capital funding - Depreciation	87	84	(3)
Direct Expenditure	12,919	9,184	(3,735)
Support Costs	300	265	(35)
Income	(977)	(1,062)	(85)
Total net controllable cost to the Funds	12,242	8,385	(3,855)

Reconciliation to total costs

	Actual outturn
	£000
Actual outturn on budgeted items above	8,385
Add back securities lending revenue included in income above	877
Investment property administration costs	559
Investment transaction costs	1,029
Investment management fees deducted from capital	20,473
Securities lending management fee	176
IAS19 LPFE retirement benefits	505
LPFE deferred tax on retirement benefits	(80)
Total cost to the Funds (inclusive of full investment management fees)	31,924
Per Fund Accounts	
Lothian Pension Fund group	29,666
Lothian Buses Pension Fund	1,978
Scottish Homes Pension Fund	280
Total	31,924

Cash-flow

Cashflow to and from a pension fund is very dependent upon the profile of its membership. Specifically, a maturing membership, where the proportion of active to deferred and pensioner members is reducing, would be expected to see a reduction in contributions received, together with additional outlays on payments to pensioners.

Significantly, Lothian Pension Fund experienced a net reduction in value from its dealings with members. Despite active membership numbers rising marginally, reflecting pensions auto-enrolment, pensioner numbers increased more significantly, driven mainly by continuing early retirement initiatives by employers. Outlays exceeded receipts by £9.2million representing a £20.6million change in position from 31 March 2016 (net addition of £11.4million).

As a fund which is closed to new entrants, the income and expenditure of Lothian Buses Pension Fund reflect this relative maturity. As at 31 March 2017, outlays from dealing with members remained in excess of receipts, by £2.7million for 2016/17. This represents a change of £1.4million on the position as at 31 March 2016, where net outlays totaled £1.3million. Primarily, this was the result of significant outgoings due to the early payment of retirement benefits.

Scottish Homes Pension Fund is a mature fund with no active members. As a result, pension outlays are met from investment income and funding from the Scottish Government, supplemented by asset sales. Net pension outlays were £6.9million, a decrease of £0.1million (1.4%) on the previous year.

Membership statistics for the three Funds and funding statements from the Actuary are provided in the Fund accounts sections.

Investment management cost transparency

Local authorities are required to account for pension funds in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). The Code is based on approved accounting standards issued by the International Accounting Standards Board and interpretations of the International Financial Reporting Interpretations Committee, except where these are inconsistent with specific statutory requirements. The Code also draws on approved accounting standards issued by the International Public Sector Accounting Standards Board and the UK Financial Reporting Council where these provide additional guidance. The Code now requires that preparers have regard to CIPFA guidance "Accounting for Local Government Pension Scheme Management Costs".

CIPFA published this guidance in July 2014, which promoted greater transparency of investment management fees. These principles were adopted as best practice in the presentation of the Lothian Pension Fund audited Annual Report 2015. In June 2016, CIPFA revised its guidance including the following "Investment costs incurred by a separate legal entity, or in respect of investment decisions over which the pension fund has no control, should not be included in the Fund Account." The revised guidance changed the disclosure of fees for fund of funds investment arrangements. A "fund of funds" is an investment holding a portfolio of other investment funds rather than investing directly in funds. Typically fees are payable to the "fund of funds" manager as well as to the managers of the underlying funds. Generally, under the revised guidance from CIPFA, the second and third layer of fees would not be disclosed with just the fees from the "fund of funds" manager stated.

In the preparation of the Funds' Annual Report for 2014/15 and 2015/16, the Funds made efforts to be completely transparent on the totality of costs incurred for managing its investment assets. The Funds disclosures included all layers of fees. At its meeting on 28 September 2016, the Pensions Committee agreed to instruct the Committee Clerk to communicate to the Chartered Institute of Public Finance and Accountancy (CIPFA), Audit Scotland and the Scottish Local Government Pension Scheme Advisory Board (SLGPSAB), the Committee's and Convener's disquiet with the relaxation of the principle of full cost transparency of investment management fees, as explicit in CIPFA's revised guidance "Accounting for Local Government Pension Scheme Management Costs".

On 18 November 2016, the Scottish LGPS Scheme Advisory Board issued Circular 01/2016, entitled "Transparency Code". This stated that it welcomed the "Code of Transparency for LGPS Asset Managers", as developed by its counterpart in England and Wales, and asked "pension funds in Scotland to promote the code with their own asset managers". This Code is voluntary with asset managers encouraged to demonstrate their commitment to transparent reporting of costs. The financial statements of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund continue, however, to include full transparency of all investment management fees.

	Investment management expenses in compliance with CIPFA guidance	Investment management expenses per 2016/17 financial statements	Disclosure in excess of CIPFA guidance
	£000	£000	£000
Lothian Pension Fund	23,555	27,712	4,157
Lothian Buses Pension Fund	1,555	1,880	325
Scottish Homes Pension Fund	212	212	0
TOTAL	25,322	29,804	4,482

Investment cost benchmarking

In an effort to provide stakeholders with some comfort that the Fund is carefully managing and fully understands investment costs, Lothian Pension Fund provides data to a benchmarking expert for analysis. Investment strategy focuses on risk adjusted returns, net of costs. The Fund has participated in investment cost benchmarking provided by CEM, an independent benchmarking expert for global pension funds with a database of 297 global pension funds representing £5.6 trillion in assets. To provide a fair comparison, CEM calculates a benchmark based on fund size and asset mix, which are key drivers of investment costs.

The latest analysis shows Lothian Pension Fund's investment costs of 0.36% of Fund assets are significantly lower than CEM's benchmark cost of 0.45%, an equivalent annual saving of approximately £4.4m. This saving largely reflects the fact that the Fund manages a relatively high percentage of assets internally compared with other similar pension funds and that it has low exposure to fund-of-fund investment vehicles.

Risk management

The Funds are committed to a strong control environment to ensure that risks are identified, understood, managed and monitored appropriately. The risks faced by the Funds change over time and ongoing management of risk is crucial. The Funds also have a compliance policy and each manager is responsible for ensuring compliance within their area of responsibility.

As at 31 March 2017, the most significant risks (after taking account of risk reduction controls), as assessed using a score out of 10 by the Funds' management team, were as follows:

Description	Impact	Likelihood	Risk score
Adverse investment performance leading to pressure on employer contributions	5	4	20
Adverse movement against non-investment funding assumptions leading to pressure on employer contributions	5	7	35
Collapse/restructuring of an employer body leading to pressure on other employers	4	8	32
Failure of IT leading to poor ICT responsiveness, legal exposure and cost/risk implications.	6	7	42

Performance

The Funds have a strong commitment to customer service which drives the continual development of our services to ensure the best possible service for customers whilst recognising potential demands of the future. Our vision, objectives and key actions are shown in our service plan along with how we measure their success. Our progress is reported regularly to the Pensions Committee and Pension Board.

In 2016/17 we have delivered the following achievements:

- Received Financial Conduct Authority registration of LPFI Limited
- Begun collaborative working on infrastructure with other LGPS funds
- Achieved Pensions Administration Standards Association accreditation
- Commenced implementation of investment unitisation system
- Continued work to undertake Guaranteed Minimum Pension (GMP) reconciliation with HMRC
- Continued to provide a shared service to Falkirk Pension Fund.

We also measure our performance against a set of behaviours, values and attitudes:



- We put our customers first and aim to provide the very best service
- Our people are at the very heart of our business and we work together to deliver our service
- We strive to improve our services by thinking ahead and developing new solutions
- We are committed to supporting a culture of honesty and transparency.



We put our customers first and aim to provide the very best service.

	Target	Actual
Maintain Customer Service Excellence Standard	Retain	Retained
Overall satisfaction of employers, active members and pensioners with our services as measured by surveys	88%	90%
Proportion of active members receiving a benefit statement by 31 August 2016	100%	99.6%

Customer Service Excellence

To maintain our commitment to customer service, we use the Customer Service Excellence (CSE) framework which ensures we are continuously making improvements. We are assessed annually by an external assessor and at our assessment in February 2016, we retained the CSE award for another year. We also gained an additional Compliance Plus award bringing the number held to five for areas such as complaint handling and working with employers.

In 2017, the assessor said, "Lothian Pension Fund has been a long-term holder of both the Charter Mark and CSE standards, and this is clearly shown in the outcome of this year's rolling programme review. The service has continued to show that it consults with its customers and adapts its services to reflect their growing expectations. The approach to complaints resolution continues to be of the highest standard, and the service demonstrated a robust approach to root cause analysis to prevent repetition of failures."

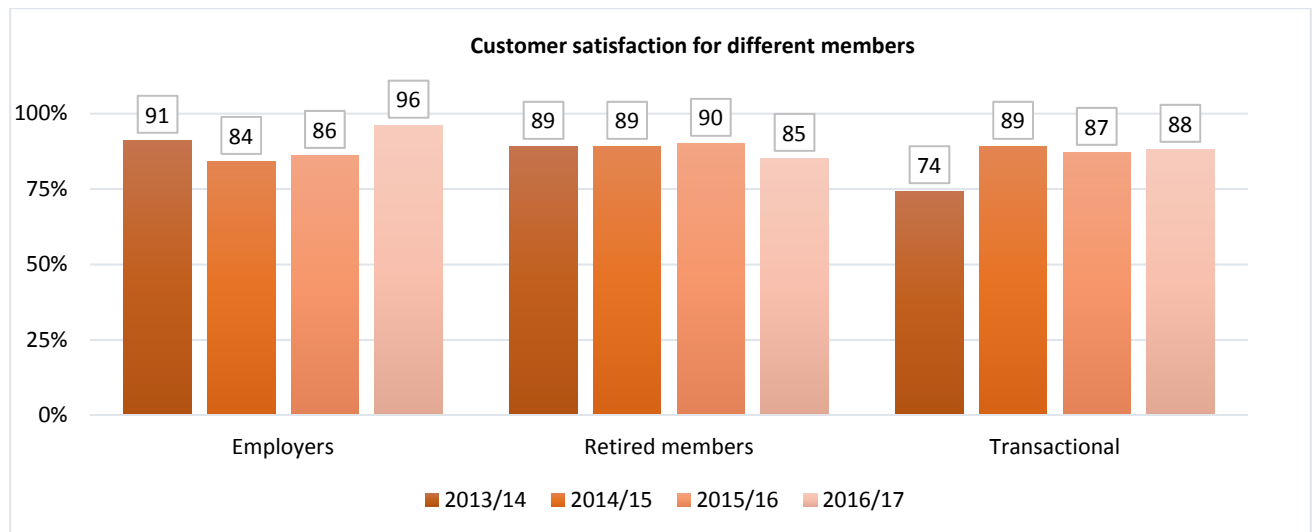
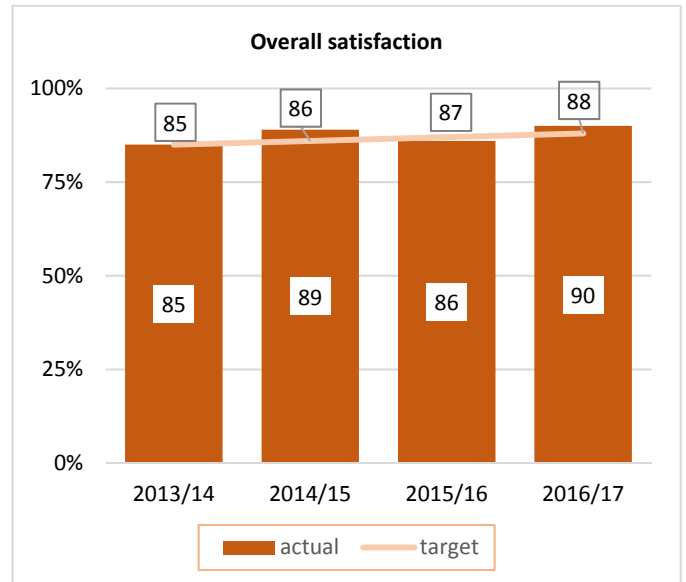


Customer satisfaction

Our overall customer satisfaction has increased steadily over recent years and was 90% in 2016/17, exceeding the target of 88%.

The chart below shows the satisfaction of different customer groups.

We received over 7,300 emails about general pension issues and have worked hard to improve our service provided via email by improving the quality of responses and reducing the time taken to respond. We also received over 6,000 emails about registering for our online service with some members reporting difficulties registering for the service. We have worked with our IT supplier to address these issues.



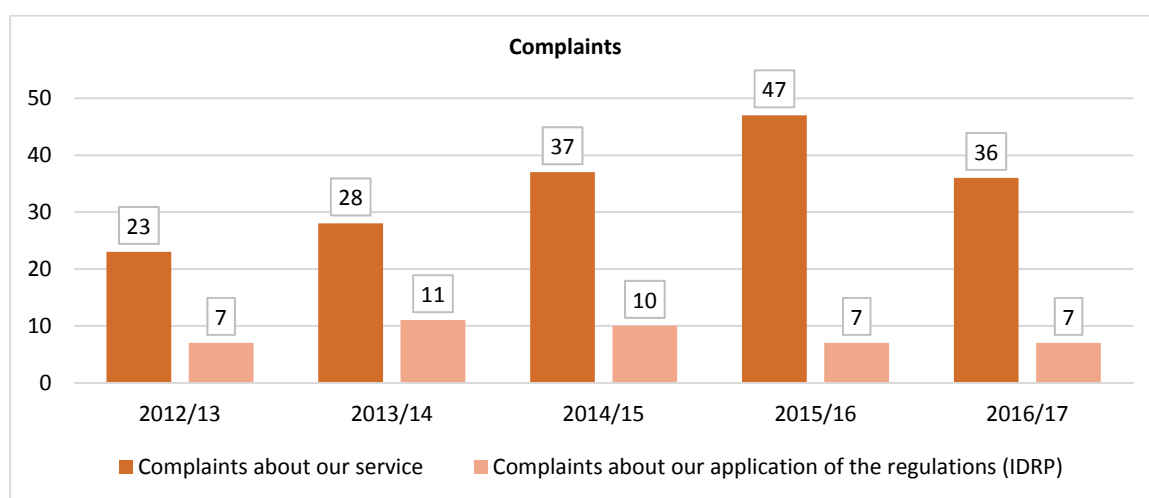
Complaints

We monitor complaints we receive and ensure they are responded to promptly. We investigate and learn from complaints to improve the service. We categorise our complaints in two ways:

- Complaints about our service
- Complaints about our application of the regulations

The graph shows the number of complaints in each of the categories. These represent less than 0.1% percentage of the procedures (over 23,000) we carried out in 2016/17.

The Funds responds, and where possible resolves, complaints within 20 working days. In 2015/16, there was an increase in complaints resulting from delays in processing requests to transfer out of the fund. This year, the number of complaints has reduced and related to a broader range of issues including the differences in pension entitlements, late payment of benefits and changes to the State Pension and ending of contracting out.



Annual benefit statements and data quality

We issued 99.6% of benefit statements by 31 August 2016 meeting The Pension Regulator's target for the issuing benefit statements. A small number of statements were not issued where the member was employed on a casual basis prior to March but did not do any work up to the end of the year. During the year, most employers submitted monthly contribution data to the Funds, leading to cleaner membership data, quicker services to members and fewer queries at the end of the year. Three employers who did not supply data to us monthly had a fine imposed under section 8.2 of our Pensions Administration Strategy.

Along with our employer web portal, introduced to assist with the transfer of data, we have adopted other initiatives to improve member information. We use Tell Us Once, the Department of Work and Pension service which allows the relatives of a person who has died to inform central and local government services of the death all at one time rather than having to contact each service individually. We also participate in specialist longevity and data analyses through "Club Vita", a service provided by the Funds' Actuary. We also carry out quarterly checks with the General Register Office and participate in the National Fraud Initiative. In 2014, we carried out a matching exercise for deferred members where we have lost touch with them. The project is currently being followed up with contact being made where a possible match has been found.

Following the end of contracting-out of the Second State Pension (S2P) on 5 April 2016, pension schemes need to reconcile the Guaranteed Minimum Pension (GMP) values they hold for members with those calculated by HMRC. Schemes will be obliged to pay whatever GMPs are attributed to them, even those that may be incorrectly calculated or have been transferred out. An initial assessment shows 54% of member records matching those of the Government's and reconciliation is underway for the remainder.



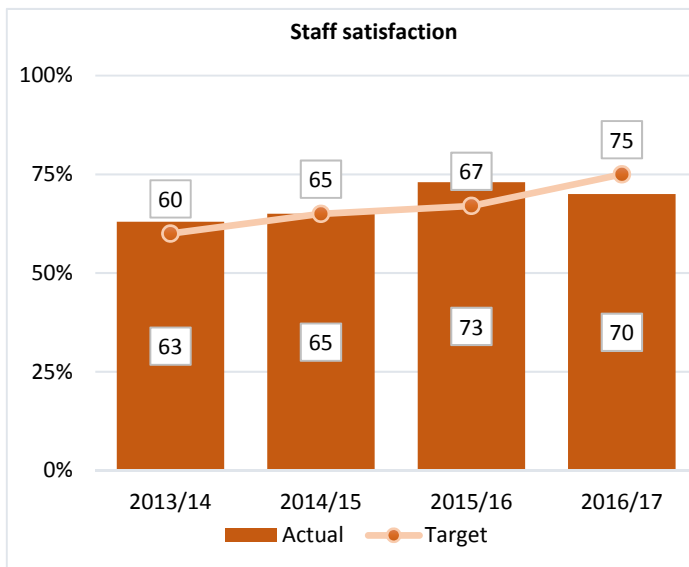
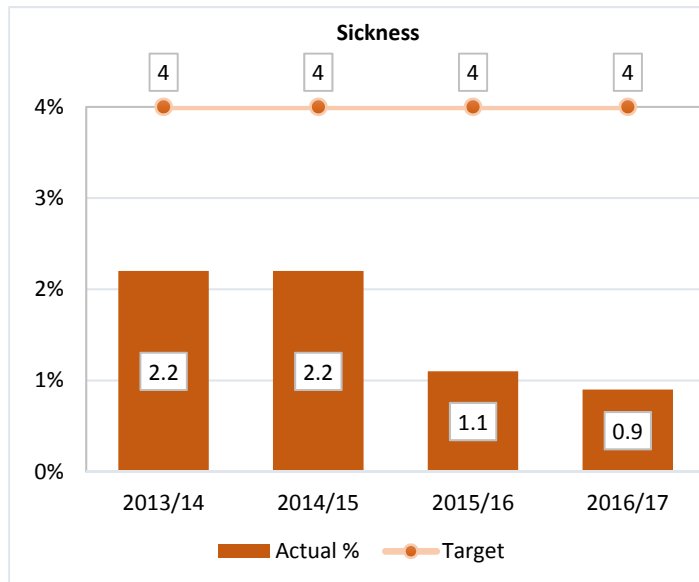
Our people are at the very heart of our business and we work together to deliver our service.

	Target	Actual
All staff complete at least two days training a year	Yes	Yes
Level of sickness absence	4%	0.9%
Staff survey satisfaction	75%	70%

Over the last financial year, staff participated in regular training. As well as attendance at external seminars and studying for qualifications, we held in-house sessions covering topics such as investments, annual accounts and funding.

The sickness absence rate was very low again at 0.9%.

We also participate in the Modern Apprentice programme, which offers paid employment and workplace training for those who have left school in the past three years, and the Job, Education and Training Programme (JET) for school pupils which is a work-based learning programme which combines school education with vocational training and real-life work experience.



In our annual staff survey in 2016, 96% of staff responded with overall satisfaction decreasing marginally from 73% to 70% which is lower than the target of 75%. The graph shows the comparison figures since 2013/14.

This year's survey also included questions regarding views on collaboration with other pension funds. 86% said they understood the reasons for collaboration and 66% felt that Lothian Pension Fund should look to collaborate with other funds.



We strive to improve our services by thinking ahead and developing new solutions.

	Target	Actual
Proportion of critical pensions administration work completed within standards	Greater than 90%	93%

Our in-house pension administration team provides a dedicated service for the three pension Funds. We monitor the time taken to complete our procedures. Key procedures include processing of retirement and dependent benefits, providing information for new members, transfers and retirement quotes.

The introduction of the career average pension scheme in April 2015 has meant that pension administration has become more complex for both the Fund and employers. We continue to review our processes to improve our performance so that the Fund can meet new challenges and deliver an excellent service to members.

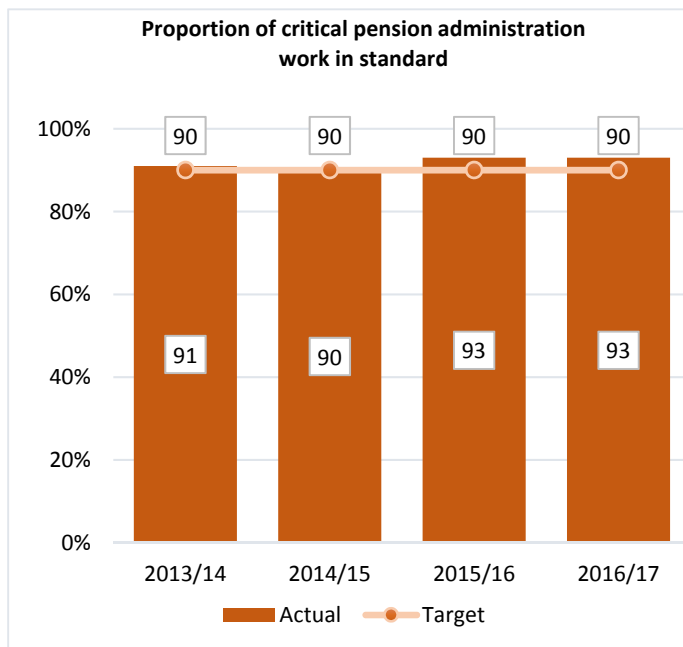
Despite the challenging environment, 93% of key procedures in 2016/17 were completed in target.

The Pensions Administration Strategy sets out the roles and responsibilities of both the Funds and employers specifying the levels of services the parties will provide to each other, and making reference to four key areas where the Funds will pass on the costs of poor performance from employers:

- Late payment of contributions
- Late submission of membership information at the end of the year
- Failure to supply the Funds with information required to provide members with pensions savings statements
- Failure to provide details of member contributions on a monthly basis.

These areas are particularly important to ensure compliance with legislation, including accurate data to administer the new career average pension scheme and the requirement to provide members with a pension forecast by 31 August each year. Charges for late payment of contributions are as stated in the Scheme regulations whilst other charges have been set to reflect the additional time spent in resolving queries and pursuing late information.

The Funds monitors employer performance against the standards set out in the Pension Administration Strategy. Results are reported to employers by way of an annual performance, with more regular reporting for larger employers.



Overall employer performance for 2016/17 is shown below, with 2015/16 shown for comparison purposes.

Case type	Target (working days)	2015/16			2016/17		
		Number received	Number within target	% within target	Number received	Number within target	% within target
New members	20	4,653	4,074	88%	4,737	4,052	86%
Leavers	20	2,377	1,207	51%	3,425	1,421	42%
Retirements	20	1,156	398	34%	1,244	440	35%
Deaths in Service	10	40	11	28%	29	21	72%

The majority of new member information continued to be received within target and the increase in numbers is due to auto-enrolment. Information provided within the 20-day target of the member leaving fell this year. As part of the Fund's drive to improve data, over 1,000 members who had left without the employer supplying details have been targeted within the last six months and we appreciate the support and effort employers have made to address this issue.

Retirement information was provided late than target in a significant proportion of cases and the primary reason for this was due to employers making decisions at short notice for cases such as voluntary redundancy. We have introduced a process for large scale early retirement exercises to handle up to 500 quotes in one quarter with our online facility allowing members to see potential benefits before applying for voluntary redundancy. This has significantly reduced work for both employers and the Funds reducing the numbers who apply speculatively. We also provide voluntary redundancy estimates online and email members the answer to frequently asked questions to help them understand their options.



We are committed to supporting a culture of honesty and transparency.

	Target	Actual
Audit of Annual Report and Financial Statements	Unqualified opinion	Yes
Monthly pension payroll paid on time	Yes	Yes
Data quality - compliance with best practice as defined by The Pensions Regulator	Fully compliant	YES
Contributions received within 19 days of the end of the month to which they relate	99.0%	99.3%

Our 2015/16, Annual Report and Financial Statements were audited by Audit Scotland and received an unqualified audit. The Funds also paid over £216million of pension benefits and lump sums to our members, primarily into the local economy where most of our members live.

Pension record keeping standards are measured against The Pension Regulator’s best practice guidance. The Pension Regulator has amended their guidance and now does not provide a target. However, for this year we have used the target set previously. Significant work has been complete to ensure data is up to date. We have also carried out tracing of members where we do not hold a current address. An action plan to meet the additional guidance going forward will be prepared with overall and individual targets set in the future to give a clear indication of any areas that require further work.

	Target	Actual
Common data	100%	99.9%
Conditional and numerical data Fund specific measurement including date of joining, pensionable remuneration, date of leaving and reasons for leaving etc.	98%	99.9%

The Pensions Act 1995 requires employers to pay pension contributions by the 19th of the month following the deduction from an employee’s pay. This requirement is highlighted in the Fund’s Pensions Administration Strategy. We monitor this requirement via our key performance indicators to ensure compliance with the Act. The target for 2016/17 year was 99% pension contributions paid in time. 99.3% of contributions by value were paid on time. Of the 1,180 payments made to the Fund in 2016/17, in total 46 were paid later than the target of the 19th of the month. The number of late payments for each employer is provided below.

Employer	Number of late payments	Employer	Number of late payments
Baxterstorey	1	Homes for Life	1
Canongate Youth [1]	2	Keymoves	1
Centre for Moving Image	1	Mitie	1
Dean Orphanage	3	Museums Galleries Scotland	1
Donaldson Trust	2	Open Door Accommodation Project	1
Edinburgh Leisure	2	Pilton Equalities Project	2
Edinburgh Rape Crisis Centre [1]	1	Police Scotland	2
Edinburgh World Heritage Trust	1	Royal Edinburgh Military Tattoo	2
Enjoy East Lothian	4	Scotland’s Learning Partnership [1]	5
Festival City Theatres Trust [1]	2	Scottish Futures Trust	1
Forth and Oban	1	Skanska [1]	3
Four Square	1	Victim Support Scotland	1
Granton Information Centre	1	Visit Scotland	1
Homeless Action Scotland	2	TOTAL	46

[1] includes contributions paid in part

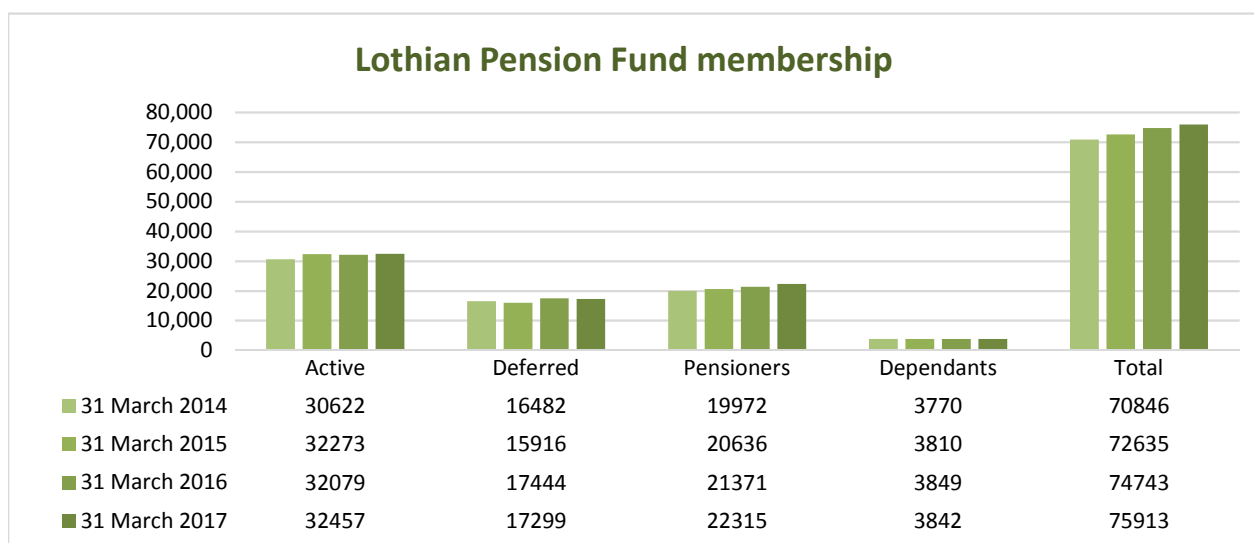
Management commentary approved by:

ANDREW KERR
Chief Executive
The City of Edinburgh Council
27 September 2017

CLARE SCOTT
Chief Executive
Lothian Pension Fund
27 September 2017

JOHN BURNS
Chief Financial Officer
Lothian Pension Fund
27 September 2017

Lothian Pension Fund



Investment Strategy

Following completion of the 2014 Actuarial Valuation, the Investment Strategy Panel and Pensions Committee reviewed the Fund's investment strategy in light of developments in pension fund membership, expected cash flow, funding level, investment risk and returns.

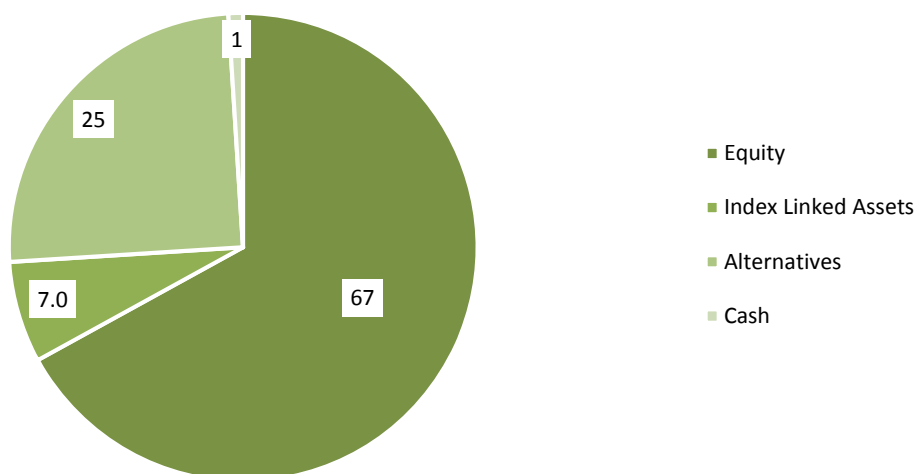
Lothian Pension Fund manages two investment strategies, which provides employers with access to an appropriate level of risk dependent on their individual characteristics (covenant strength, funding position, liability profile and time horizon). Most employer liabilities are funded in Strategy 1, which invests in a diversified portfolio of assets that are expected to generate positive real returns over the long term, but which will be volatile over shorter periods. Employers accounting for less than 1% of the Fund's liabilities are funded on a 'gilts' basis in Strategy 2, which invests in a portfolio of index-linked gilts to minimise risk for these employers.

Following completion of the 2014 Actuarial Valuation, the Fund's Investment Strategy was reviewed. The Pensions Committee agreed in December 2015 that the Investment Strategy 2012-17 remained appropriate for the vast majority of employer liabilities. This strategy, Strategy 1, reduces the allocation to equities (including private equity) from 71.5% at the end of 2012 to 65% by the end of 2017 and increases the allocation to index-linked assets and alternatives. (Alternatives include property, infrastructure, timber and fixed income assets, such as corporate bonds and other debt investments.) The strategy recognises a gradually changing risk profile for the Fund, but retains significant exposure to investments, such as index-linked assets and equities, which have a history of protecting or enhancing purchasing power after the effects of inflation have been taken into account.

The long term strategy for 2012-17 is set out in the table below along with the current interim strategy allocation and the asset allocation limits under normal financial conditions.

Strategy 1	Strategic Allocation 31/03/2017 %	Long term Strategy 2012 - 2017 %	Permitted ranges %
Equities	66	65	50 - 75
Index Linked Assets	7	7	0 - 20
Alternatives	26.5	28	20 - 35
Cash	0.5	0	0 - 10
Total	100	100	n/a

Actual Asset Allocation (%) at 31 March 2017



The implementation of the Investment Strategy 2012-17 continued to proceed at a measured pace over 2016/17 as investment opportunities became available and as research on opportunities was completed. Progress towards the long term strategy allocation involves the interim strategy allocation and the actual asset allocation changing gradually over time. The pace of change can be accelerated or slowed depending on asset prices, the availability of alternative investments and research conclusions on new investment opportunities.

A key objective of the Fund's investment strategy is to reduce risk, including risk within the equity pool of assets, and has involved a shift from a regional to a global manager structure. Significant steps have been taken in this regard in prior years. As such, 2016/17 represented much more of a "steady state" in terms of the structure within the equity exposure. The only notable change to report over the year was within one of the internally managed regional portfolios. The Europe (ex UK) is being managed using an investment process created by the internal portfolio management team. Almost 90% of the Fund's equities are now managed internally with the majority of these in low cost, low turnover strategies, which are expected to enhance the Fund's risk-adjusted returns over the long term. The Fund continues to outsource a small proportion of investment management services which complement the portfolio strategies employed internally.

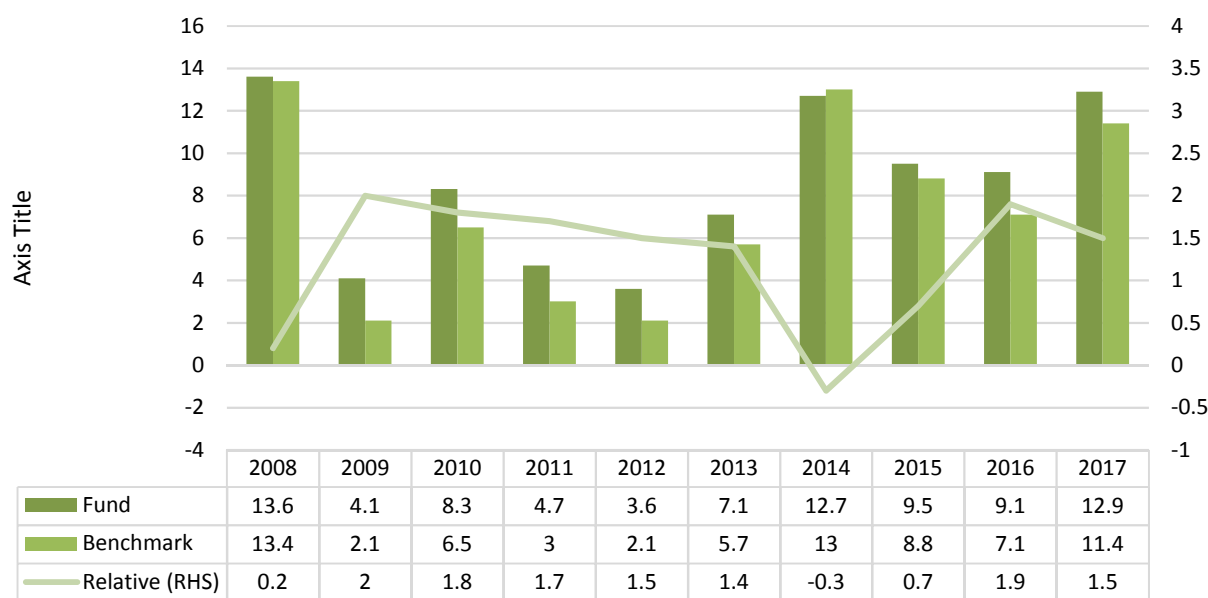
Investment performance

Annualised returns to 31 March 2017 (% per year)	1 year	5 year	10 years
Lothian Pension Fund - Strategy 1	21.7	12.9	8.2
Benchmark*	24.8	11.4	6.6
Lothian Pension Fund - Strategy 2 (from 2015)	19.9	-	-
Benchmark	19.9	-	-
Actuarial Valuation Assumptions - Strategy 1 **	5.0	5.5	5.8
Actuarial Valuation Assumptions - Strategy 2 **	3.5	4.9	5.5
Retail Price Index (RPI)	3.1	2.3	2.8
Consumer Price Index (CPI)	2.3	1.4	2.3
National Average Earnings	2.4	1.9	2.0

*Comprises equity, index-linked gilts and cash indices as well as an inflation-linked index for the alternatives allocation

**estimated

Annualised 5 yearly returns ending 31 March for Strategy 1 (% per year)



The objectives of the Fund are:

- over long-term economic cycles (typically 5 years or more) the achievement of the same return as that generated by the strategic allocation
- over shorter periods, the Fund should perform better than the strategic allocation if markets fall significantly.

Lothian Pension Fund's assets have increased by £1,161million, with investments returning 21.7% over the year, slightly behind the benchmark of 24.8%. The internal team manages a significant proportion of assets of all three pension funds in-house. For Lothian Pension Fund this includes approximately £3.4billion of listed equity assets and a currency hedging programme specifically designed to provide downside protection in times of market stress while participating in some, though not necessarily all, of any upward movement. The underperformance relative to the benchmark this year follows on from a period of significant outperformance (+6.2%) in the prior year (2015/16) and over longer term periods the Fund is meeting its objective, exceeding the benchmark but with lower volatility.

Returns relative to the benchmark over a one year period need to be placed in the context that there are no ideal benchmarks for many of the assets held in the Fund, especially the Alternatives. The true value and returns on the unlisted investments in the Alternatives portfolio will not be known until assets are realised, perhaps not for several years. Investments are made in Alternative asset classes due to the attractive expected long-term returns and the diversification they provide. Additionally, the low risk equity exposure is specifically designed to provide downside protection in times of market stress while participating in some, though not necessarily all, of any upward movement. It is therefore likely that returns may deviate meaningfully from the benchmark over shorter time periods. The Investment Strategy Panel assesses the underlying risks of the portfolios that make up the asset allocation to ensure that these are consistent with the long-term objectives of the Fund.

Lothian Pension Fund Group

Fund Account for year ended 31 March 2017

This statement shows a summary of the income and expenditure that the Pension Fund has generated and consumed in delivering the Local Government Pension Scheme. Included is the income generated from employers' and employees' contributions and investment income, as well as the cost of providing benefits and administration of the Fund.

Lothian Pension Fund Parent	Lothian Pension Fund Group		Lothian Pension Fund Parent	Lothian Pension Fund Group
2015/16	2015/16		2016/17	2016/17
£000	£000	Note	£000	£000
Income				
159,872	159,872	Contributions from employers	153,735	153,735
42,800	42,800	Contributions from members	42,578	42,578
2,780	2,780	Transfers from other schemes	5,536	5,536
205,452	205,452		201,849	201,849
Less: expenditure				
133,624	133,624	Pension payments including increases	141,778	141,778
46,315	46,315	Lump sum retirement payments	48,895	48,895
5,336	5,336	Lump sum death benefits	6,384	6,384
519	519	Refunds to members leaving service	615	615
417	417	Premiums to State Scheme	361	361
6,075	6,075	Transfers to other schemes	11,098	11,098
1,743	1,766	Administrative expenses	1,895	1,954
194,029	194,052		211,026	211,085
11,423	11,400	Net (withdrawals)/additions from dealing with members	(9,177)	(9,236)
Returns on investments				
134,113	134,113	Investment income	153,016	153,016
216,646	216,646	Change in market value of investments	1,044,952	1,044,952
(34,400)	(34,520)	Investment management expenses	(27,375)	(27,712)
316,359	316,239	Net returns on investments	1,170,593	1,170,256
327,782	327,639	Net increase in the Fund during the year	1,161,416	1,161,020
5,106,232	5,106,232	Net assets of the Fund at 1 April 2016	5,434,014	5,433,871
5,434,014	5,433,871	Net assets of the Fund at 31 March 2017	6,595,430	6,594,891

Lothian Pension Fund Group

Net Assets Statement as at 31 March 2017

This statement provides a breakdown of type and value of all net assets at the year end.

Lothian Pension Fund Parent	Lothian Pension Fund Group		Lothian Pension Fund Parent	Lothian Pension Fund Group
31 March 2016	31 March 2016		31 March 2017	31 March 2017
£000	£000	Note	£000	£000
Investments				
5,413,590	5,413,590	Assets	6,570,547	6,570,547
(14,627)	(14,627)	Liabilities	(1,798)	(1,798)
5,398,963	5,398,963	Net investment assets	6,568,749	6,568,749
Non current assets				
451	451	Debtors	259	259
332	332	Computer systems	248	248
-	-	Share Capital	50	-
-	36	Deferred tax	-	117
783	819		557	624
Current assets				
4,287	4,287	The City of Edinburgh Council	4,467	4,467
41,327	41,331	Cash balances	27,278	27,362
12,670	12,703	Debtors	14,938	14,965
58,284	58,321		46,683	46,794
Non current liabilities				
-	(180)	Retirement benefit obligation	-	(685)
-	(180)		-	(685)
Current liabilities				
(24,016)	(24,052)	Creditors	(20,559)	(20,591)
(24,016)	(24,052)		(20,559)	(20,591)
5,434,014	5,433,871	Net assets of the Fund at 31 March 2017	6,595,430	6,594,891

The unaudited accounts were issued on 28 June 2017 and the audited accounts were authorised for issue on 27 September 2017.

JOHN BURNS FCMA CGMA

Chief Finance Officer, Lothian Pension Fund

27 September 2017

Notes to the net asset statement

The financial statements summarise the transactions of the Fund during the year and its net assets at the year end. They do not take account of the obligations to pay pensions and benefits which fall due after the end of the year. The actuarial position of the Fund, which does take account of such obligations, is discussed in the Actuarial Valuation section of this report and these financial statements should be read in conjunction with that information. In addition, as required by IAS26, the Actuarial Present Value of Promised Retirement Benefits is disclosed in the notes to these financial statements.

Notes to the Accounts

1 Statement of Accounting Policies

The statement of accounting policies for all Funds can be found on page 112.

2 Lothian Pension Fund Group

Basis of consolidation, presentation of financial statements and notes

Commencing with the year ended 31 March 2016, Consolidated Financial Statements have been prepared for Lothian Pension Fund. The Financial Statements of Lothian Buses Pension Fund and Scottish Homes Pension Fund continue to be prepared on a single entity basis.

The Consolidated Financial Statements for Lothian Pension Fund are prepared by combining the Financial Statements of the Fund (the parent entity) and its controlled entities (LPFE Limited and LPFI Limited) as defined in accounting standard IAS27 - Consolidated and Separate Financial Statements. Consistent accounting policies are employed in the preparation and presentation of the Consolidated Financial Statements. All inter-entity balances and transactions between entities, including any unrealised profits or losses, have been eliminated on consolidation.

Because the controlled entities activities are primarily focused on the provision of services to the Fund, its consolidation has a limited impact on the figures included in the Fund Account and Net Assets Statement of Lothian Pension Fund. An additional column has been added in both the Fund Account and Net Assets Statement, with the figures prior to consolidation being identified as "Parent" and after consolidation as "Group". In the notes to the accounts, where there is a difference between the parent and group figures they are identified as either "Parent " or "Group".

Note	Description
28	Related party transactions and balances Describes transactions during the year and balances at year end which relate to the parent and the companies.
29a	Consolidated Lothian Pension Fund group - LPFE Limited - deferred tax Describes the deferred tax non-current asset of the Company. See 2 f) ii) in the Statement of Accounting Policies and General notes for more information.
29b	Consolidated Lothian Pension Fund group - LPFE Limited and LPFI Limited - share capital Describes the share capital of the Company.
30	Retirement benefits obligation - group Provides the information on the retirement benefits obligation of the Company as required under IAS19 - Employee Benefits. See 2 q) ii) in the Statement of Accounting Policies and General notes for more information.

3 Events after the Reporting Date

There have been no events since 31 March 2017, and up to the date when these accounts were authorised, that require any adjustments to these accounts.

Notes to the Accounts

4 Contributions from employers

The total contributions receivable for the administering authority, other scheduled bodies and admitted bodies were as follows:-

By category	2015/16 £000	2016/17 £000
Future service rate	133,035	133,301
Past service deficit	7,357	7,668
Strain costs	9,984	12,558
Cessation contributions	9,496	208
	159,872	153,735

By employer type	2015/16 £000	2016/17 £000
Administering Authority	63,459	63,542
Other Scheduled Bodies	77,198	71,426
Community Admission Bodies	18,784	18,312
Transferee Admission Bodies	431	455
	159,872	153,735

Employer contributions, as calculated by the Fund Actuary, comprise two elements:

- An estimate of the cost of benefits accruing in the future, referred to as the "future service rate", which is expressed as a percentage of payroll and;
- an adjustment for the solvency of the Fund based on the benefits already accrued. If there is a surplus, there may be a contribution reduction; if there is a deficit there may be a contribution increase. For all employers, contributions to cover any Past Service Deficit are expressed as a fixed monetary sum, rather than as a percentage of payroll and are payable on a monthly basis that is one twelfth of the annual total.

Where an employer makes certain decisions which result in benefits being paid early, this results in a "strain" on the Fund. The resulting pension strain costs are calculated and recharged in full to that employer.

Any employer that ceases to have at least one actively contributing member is required to pay cessation contributions.

5 Contributions from members

By employer type	2015/16 £000	2016/17 £000
Administering Authority	16,389	15,345
Other Scheduled Bodies	20,226	20,993
Community Admission Bodies	6,074	6,099
Transferee Admission Bodies	111	141
	42,800	42,578

6 Transfers in from other pension schemes

	2015/16 £000	2016/17 £000
Group transfers	-	-
Individual transfers	2,780	5,536
	2,780	5,536

Notes to the Accounts

7 Pensions payable

By employer type	2015/16 £000	2016/17 £000
Administering Authority	65,447	70,547
Other Scheduled Bodies	56,115	58,364
Community Admission Bodies	11,902	12,687
Transferee Admission Bodies	160	180
	133,624	141,778

Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998 [Section 31] allows employers to pay additional pensions on a voluntary basis.

As is typical within the Local Government Pension Schemes (LGPS), arrangements exist whereby additional teachers' pensions and employee pensions are paid with the payment of funded pensions. In order that such are not regarded as "unauthorised payments" by HMRC these pension payments are met by the administering authority through a general fund bank account and recharged to the body or service which granted the benefits.

As "unfunded payments" are discretionary benefits, they are not relevant to the sums disclosed in the Fund accounts. As such Lothian Pension Fund provides payment and billing services to certain employers on a no charge agency agreement basis.

8 Lump sum retirement benefits payable

By employer type	2015/16 £000	2016/17 £000
Administering Authority	27,160	26,340
Other Scheduled Bodies	15,336	18,503
Community Admission Bodies	3,685	3,900
Transferee Admission Bodies	134	152
	46,315	48,895

9 Lump sum death benefits payable

By employer type	2015/16 £000	2016/17 £000
Administering Authority	2,745	2,578
Other Scheduled Bodies	1,964	3,312
Community Admission Bodies	627	488
Transferee Admission Bodies	-	6
	5,336	6,384

10 Transfers out to other pension schemes

	2015/16 £000	2016/17 £000
Group transfers	-	173
Individual transfers	6,075	10,925
	6,075	11,098

Notes to the Accounts

11a Administrative expenses

	LPF Parent 2015/16 £000	LPF Group 2015/16 £000	LPF Parent 2016/17 £000	LPF Group 2016/17 £000
Employee Costs	992	994	1,093	1,098
The City of Edinburgh Council - other support costs	133	133	132	132
System costs	228	228	231	231
Actuarial fees	50	50	64	64
External audit fees	44	44	41	49
Legal fees	15	15	60	60
Printing and postage	77	77	79	79
Depreciation	57	57	57	57
Office costs	108	108	110	110
Sundry costs less sundry income	39	39	28	18
IAS19 retirement benefit adjustments - see note 30	-	27	-	66
Deferred tax on retirement benefit obligation - see note 29a	-	(6)	-	(10)
Corporation tax losses utilised by CEC group - see note 28	-	-	-	-
	1,743	1,766	1,895	1,954

The Investment and Pensions Service of the Council is responsible for administering the three pension Funds. The Service receives an allocation of the overheads of the Council. In turn the Service allocates administration and investment costs to the three pension funds. Costs directly attributable to a specific fund are charged to the relevant Fund, costs that are common to all three funds are allocated on a defined basis. Other costs are allocated on the basis of the number of members in each pension fund.

11b Investment management expenses

	LPF Parent 2015/16 £000	LPF Group 2015/16 £000	LPF Parent 2016/17 £000	LPF Group 2016/17 £000
External management fees -				
invoiced	7,123	7,123	3,970	3,970
deducted from capital (direct investment)	15,603	15,603	15,245	15,245
deducted from capital (indirect investment)	6,775	6,775	4,157	4,157
Securities lending fees	212	212	155	155
Transaction costs - Equities	2,201	2,201	956	956
Property operational costs	497	497	558	558
Employee costs	961	963	1,116	1,149
Custody fees	304	304	300	300
Engagement and voting fees	76	76	82	82
Performance measurement fees	46	46	50	50
Consultancy fees	78	78	64	64
System costs	185	185	245	245
Legal fees	103	103	210	210
The City of Edinburgh Council - other support costs	124	124	111	111
Depreciation	7	7	7	7
Office costs	71	71	85	85
Sundry costs less sundry income	34	34	64	(1)
IAS19 retirement benefit adjustments - see note 30	-	153	-	439
Deferred tax on retirement benefit obligation - see note 29	-	(30)	-	(70)
Corporation tax losses utilised by CEC group - see note 28	-	(5)	-	-
	34,400	34,520	27,375	27,712

Notes to the Accounts

11b Investment management expenses (cont)

Investment costs directly attributable to a specific fund are charged to the relevant Fund, costs that are common to all three funds are allocated based on the value of the Funds as at the year end.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions or in the proceeds of investment sales (see note 14 - Reconciliation of movements in investments and derivatives).

The external investment management fees (deducted from capital) above include £4.0m (£3.9m direct, £0.1m indirect) in respect of performance-related fees compared to £12.0m in 2015/16 (£7.9m direct, £4.1m indirect).

It should be noted that Lothian Pension Funds disclosure on investment management fees goes further than CIPFA's LGPS Management Cost revised guidance on cost transparency which came into effect from 1st April 2016. Consistent with previous years, the Fund recognises fees deducted from investments not within its direct control (such as fund of fund fees) to give a full picture of its investment management costs. Further details can be found on page 19. This further disclosure highlights an extra £4.2m in costs (2016 £6.8m).

11c Total management expenses

	LPF Parent 2015/16 £000	LPF Group 2015/16 £000	LPF Parent 2016/17 £000	LPF Group 2016/17 £000
Administrative costs	1,570	1,582	1,686	1,719
Investment management expenses	32,814	32,900	26,345	26,592
Oversight and governance costs	1,759	1,804	1,239	1,355
	36,143	36,286	29,270	29,666

In accordance with CIPFA, the above analysis looks at the combined administration and investment management expenses in note 11a and b and splits out the costs to include a third heading covering oversight and governance expenditure.

12 Investment income

	2015/16 £000	2016/17 £000
Income from fixed interest securities	3,898	3,589
Dividends from equities	94,637	120,326
Unquoted private equity and infrastructure	13,581	5,646
Income from pooled investment vehicles	1,026	1,111
Gross rents from properties	20,914	23,085
Interest on cash deposits	1,237	597
Stock lending and sundries	1,142	775
	136,435	155,129
Irrecoverable withholding tax	(2,322)	(2,113)
	134,113	153,016

Notes to the Accounts

13 Net investment assets

	Region	31 March 2016 £000	31 March 2017 £000
Investment Assets			
Bonds			
Public sector fixed interest	Overseas	153,740	-
Public sector fixed interest	UK	-	156,876
Public sector index linked gilts quoted	UK	380,290	502,439
		534,030	659,315
Equities			
Quoted	UK	561,064	655,522
Quoted	Overseas	2,887,886	3,564,953
		3,448,950	4,220,475
Pooled investment vehicles			
Private equity, infrastructure, private debt & timber	UK	165,547	457,647
Private equity, infrastructure, private debt & timber	Overseas	550,617	556,623
Property	UK	82,453	67,969
Other	UK	17,275	19,191
		815,892	1,101,430
Properties			
Direct property	UK	356,281	356,741
		356,281	356,741
Derivatives			
Derivatives - forward foreign exchange		-	1,081
		-	1,081
Cash deposits			
Deposits		227,409	216,036
		227,409	216,036
Other investment assets			
Due from broker		18,648	1,320
Dividends and other income due		12,380	14,521
		31,028	15,841
Total investment assets		5,413,590	6,570,919
Investment liabilities			
Derivatives			
Derivatives - forward foreign exchange		(13,183)	(424)
		(13,183)	(424)
Other financial liabilities			
Due to broker		(1,444)	(1,746)
		(1,444)	(1,746)
Total investment liabilities		(14,627)	(2,170)
Net investment assets		5,398,963	6,568,749

Notes to the Accounts

14a Reconciliation of movement in investments and derivatives

	Market value at 31 March 2016 £000	Purchases at cost & derivative payments £000	Sale & derivative receipts £000	Change in market value £000	Market value at 31 March 2017 £000
Bonds	534,030	596,611	(595,768)	124,442	659,315
Equities	3,448,949	591,687	(573,782)	753,621	4,220,475
Pooled investment vehicles	815,893	266,289	(140,168)	159,416	1,101,430
Property	356,280	4,675	(2,358)	(1,856)	356,741
Derivatives - futures	-	(484)	(7,113)	7,597	-
Derivatives - forward foreign exchange	(13,183)	42,385	(8,823)	(19,722)	657
	5,141,969	1,501,163	(1,328,012)	1,023,498	6,338,618
Other financial assets / liabilities					
Margin balances	-			-	-
Cash deposits	227,409			21,837	216,036
Broker balances	17,205			(383)	(426)
Dividend due etc	12,380			-	14,521
	256,994			21,454	230,131
Net financial assets	5,398,963			1,044,952	6,568,749

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.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions and in the proceeds from sales and are therefore included in the tables above.

	Market value at 31 March 2015 £000	Purchases at cost & derivative payments £000	Sale & derivative receipts £000	Change in market value £000	Market value at 31 March 2016 £000
Bonds	414,330	308,910	(202,855)	13,645	534,030
Equities	3,267,975	1,256,575	(1,143,580)	67,979	3,448,949
Pooled investment vehicles	633,040	141,787	(81,080)	122,146	815,893
Property	316,169	25,153	(2,295)	17,253	356,280
Derivatives - futures	-	5	87	(92)	-
Derivatives - forward foreign exchange	29,800	4,316	(40,895)	(6,404)	(13,183)
	4,661,314	1,736,746	(1,470,618)	214,527	5,141,969
Other financial assets / liabilities					
Margin balances	-			-	-
Cash deposits	400,497			1,751	227,409
Broker balances	(384)			368	17,205
Dividend due etc	11,157			-	12,380
	411,270			2,119	256,994
Net financial assets	5,072,584			216,646	5,398,963

Notes to the Accounts

14d Reconciliation of fair value measurements within level 3

	Market value at 31 March 2016	Level 3 transfers		Purchases at cost & derivative payments	Sales & derivative receipts	Unrealised gains / (losses)	Realised gains / (losses)	Market value at 31 March 2017
		in	out					
Pooled investments								
Infrastructure	384,028	-	-	260,926	(57,620)	63,921	11,939	663,194
Property	64,743	-	-	5,492	(25,306)	(19,320)	19,811	45,420
Private Equity	168,904	-	-	6,939	(72,534)	(30,882)	56,884	129,311
Timber	125,313	-	-	-	(11,956)	2,491	16,684	132,532
Private debt	37,919	-	-	52,535	(3,866)	23	2,622	89,233
Freehold Property	348,375	-	-	3,955	-	(1,832)	-	350,498
Unlisted equity	566	-	-	-	-	-	(566)	-
	1,129,848	-	-	329,847	(171,282)	14,401	107,374	1,410,188

Unrealised and realised gains and losses are recognised in the profit and losses on disposal and changes in the market value of investments line of the fund account.

15 Derivatives - forward foreign exchange

Summary of contracts held at 31 March 2017

Contract settlement within	Currency bought	Currency sold	Local currency bought 000	Local currency sold 000	Asset value £000	Liability value £000
Up to one month	GBP	AUD	54,622	90,014	-	(261)
Up to one month	GBP	CAD	99,825	164,694	1,081	-
Up to one month	CAD	GBP	4,872	3,033	-	(112)
Up to one month	USD	JPY	28	3,116	-	-
One to six months	USD	AUD	868	1,186	-	(29)
One to six months	USD	CHF	4,154	4,143	-	(22)

Open forward currency contracts at 31 March 2017

1,081	(424)
-------	-------

Net forward currency contracts at 31 March 2017

657

Prior year comparative

Open forward currency contracts at 31 March 2016

-	(13,183)
---	----------

Net forward currency contracts at 31 March 2016

(13,183)

The above table summarises the contracts held by maturity date, all contracts are traded on an over-the-counter basis.

In order to maintain appropriate diversification of investments in the portfolio and take advantage of wider opportunities, the Lothian Pension Fund invests over half of the fund in overseas markets. A currency hedging programme, using forward foreign exchange contracts, has been put in place to reduce the extent to which the Fund is exposed to certain currency movements.

Notes to the Accounts

16 Investment managers and mandates

Manager	Mandate	Market value at 31 March 2016 £000	% of total 31 March 2016 %	Market value at 31 March 2017 £000	% of total 31 March 2017 %
In-house	UK all cap equities	106,884	2.0	130,362	2.0
In-house	UK mid cap equities	105,980	2.0	121,061	1.8
Total UK equities		212,864	4.0	251,423	3.8
In-house	European ex UK equities	105,479	2.0	120,393	1.8
In-house	US equities	117,119	2.2	150,941	2.3
Total regional overseas equities		222,598	4.2	271,334	4.1
In-house	Global high dividend	759,254	14.1	928,720	14.1
In-house	Global low volatility	966,835	17.8	1,162,921	17.7
In-house	Global value	824,967	15.2	985,286	15.0
Harris	Global equities	186,652	3.5	263,263	4.0
Nordea	Global equities	223,912	4.1	280,815	4.3
Total global equities		2,961,620	54.7	3,621,005	55.1
In-house	Currency hedge	(12,370)	(0.2)	708	-
Total currency overlay		(12,370)	(0.2)	708	-
Total listed equities		3,384,712	62.6	4,144,470	63.0
In-house	Private equity unquoted	168,904	3.1	129,311	2.0
In-house	Private equity quoted	57,145	1.1	75,902	1.2
Total private equity		226,049	4.2	205,213	3.2
Total equity		3,610,761	66.8	4,349,683	66.2
In-house	Index linked gilts	357,163	6.6	450,833	6.9
In-house	Gold	17,020	0.3	19,652	0.3
Total inflation linked bonds and gold		374,183	6.9	470,485	7.2
In-house	Property	50,003	0.9	38,038	0.6
Standard Life	Property	422,452	7.8	414,574	6.3
Total property		472,455	8.7	452,612	6.9
In-house	Infrastructure unquoted	384,028	7.1	663,194	10.1
In-house	Infrastructure quoted	30,060	0.6	23,548	0.4
In-house	Timber	125,313	2.3	132,532	2.0
Total other real assets		539,401	10.0	819,274	12.5
In-house	Secured loans	13,770	0.3	14,142	0.2
In-house	Treasury bills	134,399	2.5	-	0.0
In-house	Private debt	37,918	0.7	89,233	1.4
In-house	Other bonds	-	0.0	159,307	2.4
Total other bonds		186,087	3.5	262,682	4.0

Notes to the Accounts

16 Investment managers and mandates (cont)

Manager	Mandate	Market value at 31 March 2016 £000	% of total 31 March 2016 %	Market value at 31 March 2017 £000	% of total 31 March 2017 %
In-house	Cash	137,886	2.6	159,645	2.4
In-house	Transitions	32,905	0.6	92	0.0
Total cash and sundries		170,791	3.2	159,737	2.4
Strategy A financial assets		5,353,678	99.2	6,514,473	99.2
In-house	Mature employer gilts	45,285	0.8	54,276	0.8
Strategy B financial assets		45,285	0.8	54,276	0.8
Net financial assets		5,398,963	100.0	6,568,749	100.0

17 Investments representing more than 5% of the net assets of the Fund or 5% of any investment class

	Market value at 31 March 2016 £000	% of asset class 31 March 2016	Market value at 31 March 2017 £000	% of asset class 31 March 2017
Bonds				
UK Gov 1.5% Senior Gilt 22/07/26	-	-	156,875	23.8
UK Gov 1.125% Index Linked 22/11/37	29,311	5.5	78,952	12.0
UK Gov 0.125% Index Linked 22/03/44	47,630	8.9	62,332	9.5
UK Gov 0.125% Index Linked 22/03/68	36,048	6.8	50,312	7.6
UK Gov 1.25% Index Linked 22/11/55	41,499	7.8	49,488	7.5
UK Gov 0.125% Index Linked 22/03/58	34,099	6.4	39,287	6.0
UK Gov 1.25% Index Linked 22/11/32	-	-	34,847	5.3
UK Gov 0.625% Index Linked 22/03/40	-	-	33,551	5.0
UK Gov 1.25% Index Linked 22/03/50	-	-	32,615	5.0
US Treasury Bill 0.375% 31/05/16	133,396	25.0	-	-
Pooled funds				
Stafford Elm Inc	45,094	5.5	50,421	4.6
Macquarie Infrastructure A & B LP	43,748	5.4	51,480	4.7
Property				
London, 119-125 Wardour St	28,050	7.9	27,100	7.6
Martlesham Heath, Retail Park	24,650	6.9	24,250	6.8
London, 100 St John Street	22,500	6.3	21,000	5.9
Sheffield, Bochum Parkway	19,850	5.6	20,200	5.7
Exeter, David Lloyd Leisure	17,875	5.0	18,825	5.3

Over the last two years no single investment represented more than 5% of the net assets of the Fund.

Notes to the Accounts

18 Securities lending

During the year Lothian Pension Fund participated in a securities lending arrangement with the Northern Trust Company. As at 31 March 2017, £220.3m (2016 £49.8m) of securities were released to third parties. Collateral valued at 104.6% (2016 107.6%) of the market value of the securities on loan was held at that date.

19 Property holdings

	2015/16 £000	2016/17 £000
Opening balance	316,169	356,280
Additions	25,153	4,675
Disposals	(2,295)	(2,358)
Net change in market value	17,253	(1,856)
Closing balance	356,280	356,741

As at 31 March 2017, there were no restrictions on the realisability of the property or the remittance of income or sale proceeds. The Fund is not under any contractual obligations to purchase or construct any of these properties. However, at year end the Fund does have funding approval in place for the development of Waterfront North Leisure Park, Walsall. The build period is 26 weeks, with practical completion anticipated in July 2017.

The future minimum lease payments receivable by the Fund are as follows

	2015/16 £000	2016/17 £000
Within one year	22,018	22,526
Between one and five years	67,158	67,195
Later than five years	94,517	99,741
	183,693	189,462

20 Financial Instruments

20a Classification of financial instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the fair value amounts of financial assets and liabilities by category and net assets statement heading. No financial assets were reclassified during the accounting period.

All financial instruments are marked to market (at fair value) in the Fund's accounting records, hence there is no difference between the carrying value and fair value.

Notes to the Accounts

20a Classification of financial instruments (cont)

Classification of financial instruments - parent

	31 March 2016			31 March 2017		
	Designated as fair value through fund account	Loans and receivables	Financial liabilities at amortised cost	Designated as fair value through fund account	Loans and receivables	Financial liabilities at amortised cost
	£000	£000	£000	£000	£000	£000
Investment assets						
Bonds	534,030	-	-	659,316	-	-
Equities	3,448,950	-	-	4,220,475	-	-
Pooled investments	815,892	-	-	1,101,430	-	-
Property Leases	7,905	-	-	6,243	-	-
Derivative contracts	-	-	-	1,081	-	-
Margin balances	-	-	-	-	-	-
Cash	-	227,409	-	-	216,036	-
Other balances	-	31,029	-	-	15,841	-
	4,806,777	258,438	-	5,988,545	231,877	-
Other assets						
City of Edinburgh Council	-	4,287	-	-	4,467	-
Cash	-	41,327	-	-	27,278	-
Share Capital	-	-	-	-	50	-
Debtors - current	-	12,670	-	-	14,937	-
Debtors - non-current	-	451	-	-	259	-
	-	58,735	-	-	46,991	-
Assets total	4,806,777	317,173	-	5,988,545	278,868	-
Financial liabilities						
Investment liabilities						
Derivative contracts	(13,183)	-	-	(424)	-	-
Other investment balances	(1,444)	-	-	(1,746)	-	-
	(14,627)	-	-	(2,170)	-	-
Other liabilities						
Creditors	-	-	(24,016)	-	-	(20,559)
Liabilities total	(14,627)	-	(24,016)	(2,170)	-	(20,559)
Total net assets	4,792,150	317,173	(24,016)	5,986,375	278,868	(20,559)
Total net financial instruments			5,085,307			6,244,684
Amounts not classified as financial instruments			348,707			350,746
Total net assets - parent			5,434,014			6,595,430

Notes to the Accounts

20a Classification of financial instruments (cont)

Classification of financial instruments - adjustments to parent to arrive at group

	31 March 2016			31 March 2017		
	Designated as fair value through fund account	Loans and receivables	Financial liabilities at amortised cost	Designated as fair value through fund account	Loans and receivables	Financial liabilities at amortised cost
	£000	£000	£000	£000	£000	£000
Other assets						
Cash	-	4	-	-	84	-
Share Capital	-	-	-	-	(50)	-
Debtors - current	-	33	-	-	27	-
Debtors - non-current	-	36	-	-	117	-
	-	73	-	-	178	-
Assets total	-	73	-	-	178	-
Other liabilities						
Retire. benefit obligation	-	-	(180)	-	-	(685)
Creditors	-	-	(36)	-	-	(32)
Liabilities total	-	-	(216)	-	-	(717)
Total net assets	-	73	(216)	-	178	(717)
Total adjustments to net financial instruments			(143)			(539)
Total net assets - group			5,433,871			6,594,891

20b Net gains and losses on financial instruments

	2015/16	2016/17
	£000	£000
Designated as fair value through fund account	197,274	1,025,354
Loans and receivables	2,119	21,454
Financial liabilities at amortised cost	-	-
Total	199,393	1,046,808
Gains and losses on directly held freehold property	17,253	(1,856)
Change in market value of investments per fund account	216,646	1,044,952

20c Fair Value Hierarchy

The valuation of financial instruments has been classified into three levels, according to the quality and reliability of information used to determine fair values.

Level 1

Financial instruments at Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities and unit trusts.

Quoted investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Notes to the Accounts

20c Fair Value Hierarchy (cont)

Level 2

Financial instruments at Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3

Financial instruments at Level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data. Such instruments would include unquoted equity investments, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investments in unquoted private equity, infrastructure, timber and European real estate are based on valuations provided by the general partners to the funds in which the Fund has invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of International Financial Reporting Standards (IFRS). The valuations are typically undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

	31 March 2017			
	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
Investment assets				
Designated as fair value through fund account	4,269,539	659,316	1,059,690	5,988,545
Non-financial assets at fair value through profit and loss	-	-	350,498	350,498
Loans and receivables	231,877	-	-	231,877
Total investment assets	4,501,416	659,316	1,410,188	6,570,920
Investment liabilities				
Designated as fair value through fund account	(2,171)	-	-	(2,171)
Total investment liabilities	(2,171)	-	-	(2,171)
Net investment assets	4,499,245	659,316	1,410,188	6,568,749

	31 March 2016			
	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
Investment assets				
Designated as fair value through fund account	3,491,275	534,030	781,472	4,806,777
Non-financial assets at fair value through profit and loss	-	-	348,375	348,375
Loans and receivables	258,438	-	-	258,438
Total investment assets	3,749,713	534,030	1,129,847	5,413,590
Investment liabilities				
Designated as fair value through fund account	(14,627)	-	-	(14,627)
Total investment liabilities	(14,627)	-	-	(14,627)
Net investment assets	3,735,086	534,030	1,129,847	5,398,963

Notes to the Accounts

21 Nature and extent of risk arising from financial instruments

Risk and risk management

The Fund's primary aim is to ensure that all members and their dependants receive their benefits when they become payable. Investment strategy A aims to maximise the returns from investments within reasonable risk parameters and hence minimise the long-term cost to employers. It achieves this by investing in a diverse range of assets to reduce risk to an acceptable level. In addition, the Fund ensures that sufficient cash is available to meet all liabilities when they are due to be paid.

Responsibility for the Fund's overall investment strategies rests with the Pensions Committee. The Investment Strategy Panel and the internal investment team monitor investment risks on a regular basis. Investment risk management tools are used to identify and analyse risks faced by the Fund's investments.

Consideration of the Fund's investment risk is part of the overall risk management of the pensions operations. Risks are reviewed regularly to reflect changes in activity and market conditions.

Types of investment risk

There are various ways of considering investment risks for pension funds. For the purposes of this note, market risk is the potential for an investor to experience losses from falls in the prices of investments. All financial instruments, including cash deposits, present a risk of loss of capital and risks vary depending on different asset classes.

Market risk also changes over time as economic conditions and investor sentiment change. The Fund considers overall fluctuations in prices arising from a variety of sources: market risk, foreign exchange risk, interest rate risk, credit risk, etc. The different risks may, to some extent, offset each other.

The overall market risk of the Fund depends on the actual mix of assets and encompasses all the different elements of risk.

The Fund manages these risks in a number of ways:

- assessing and establishing acceptable levels of market risk when setting overall investment strategy. Importantly, risk is considered relative to the liabilities of the Fund
- diversification of investments in terms of type of asset, investment styles, investment managers, geographical and industry sectors as well as individual securities
- taking stewardship responsibilities seriously and pursuing constructive engagement with the companies in which we invest
- monitoring market risk and market conditions to ensure risk remains within tolerable levels
- using equity futures contracts from time to time to manage market risk. Options are not used by the Fund.

Sensitivity analysis

Asset prices have a tendency to fluctuate. The degree of such fluctuation is known as "volatility" and it differs by asset class. The table sets out the long-term volatility assumptions used in the Fund's asset-liability modelling undertaken by the Fund's investment adviser KPMG:

Notes to the Accounts

21 Nature and extent of risk arising from financial instruments (cont)

Asset type	Potential price movement (+ or -)
Equities - Developed Markets	20.5%
Equities - Emerging Markets	30.0%
Private Equity	30.0%
Timber and Gold	18.0%
Secured Loans	8.0%
Fixed Interest Gilts	6.6%
Index-Linked Gilts	10.9%
Infrastructure	18.0%
Property	13.0%
Cash	1.1%

Volatility is the standard deviation of annual returns. Broadly speaking, in two years out of three, the asset's change in value (which could be a gain or a loss) is expected to be lower than the volatility figure, but in one year out of three, the change in value is expected to be higher than the volatility figure.

Asset classes do not always move in line with each other. The extent to which assets move together is known as their "correlation". A lower correlation means that there is less risk of assets losing value at the same time.

The overall Fund benefits from "diversification" because it invests in different asset classes, which don't all move in line with each other. Consequently, the aggregate risk at the Fund level is less than the total risk from all the individual assets in which the Fund invests. The following table shows the risks at the asset class level and the overall Fund level, with and without allowance for correlation.

	Value at 31 March 2017 £m	% of fund %	Potential Change +/- %	Value on increase £m	Value on decrease £m
Equities - Developed Markets	3,855	58.7	20.5	4,645.3	3,064.7
Equities - Emerging Markets	290	4.4	30.0	377.0	203.0
Private Equity	205	3.1	30.0	266.5	143.5
Timber and Gold	152	2.3	18.0	179.4	124.6
Secured Loan	103	1.6	8.0	111.2	94.8
Fixed Interest Gilts	159	2.4	6.6	169.5	148.5
Index-Linked Gilts	505	7.7	10.9	560.0	450.0
Infrastructure	687	10.5	18.0	810.7	563.3
Property	453	6.9	13.0	511.9	394.1
Cash and forward foreign exchange	160	2.4	1.1	161.8	158.2
Total [1]	6,569	100.0	18.6	7,793.3	5,344.7
Total [2]			15.9	7,613.5	5,524.5
Total [3]			15.9	7,613.5	n/a

[1] No allowance for correlations between assets

[2] Including allowance for correlations between assets

[3] Including allowance for correlation between assets and liabilities.

The value on increase/decrease columns illustrate the monetary effect of the percentage change in the volatility column. The actual annual change in value is expected to be lower than this in two years out of three, but higher in one year out of three.

Notes to the Accounts

21 Nature and extent of risk arising from financial instruments (cont)

It can be seen that the risk to the overall Fund assets [2] is lower than the total of the risks to the individual assets.

However, because the purpose of a pension scheme is to make payments to scheme beneficiaries, the true risk of a pension scheme is not measured in absolute terms, but relative to its liabilities [3].

This risk analysis incorporates volatility from market, interest rate, foreign exchange, credit, and all other sources of risk, and, importantly, makes allowance for how these risks may offset each other.

Credit risk

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit risk in their pricing and consequently the risk of loss is implicitly provided for in the value of the Fund's assets and liabilities (as outlined in Market Risk above).

In essence, the Fund's entire investment portfolio is exposed to some sort of credit risk. However, through the selection of counterparties, brokers and financial institutions the Fund reduces the credit risk that may occur through the failure to settle a transaction in a timely manner.

Cash deposits, derivatives and securities lending are the major areas of credit exposure where credit risk is not reflected in market prices.

Cash deposits

At 31 March 2017, cash deposits represented £243.4m, 3.69% of total net assets. This was held with the following institutions:

	Moody's Credit Rating at 31 March 2017	Balances at 31 March 2016 £000	Balances at 31 March 2017 £000
Held for investment purposes			
Northern Trust Global Investment Limited - liquidity funds	Aaa-mf	78,223	83,249
Northern Trust Company - cash deposits	Aa2	66,450	40,697
The City of Edinburgh Council - treasury management	See below	82,736	92,090
Total investment cash		227,409	216,036
Held for other purposes			
The City of Edinburgh Council - treasury management	See below	41,327	27,278
Total cash - parent		268,736	243,314
Cash held by LPFE/LPFI Limited			
Royal Bank of Scotland	A3	4	84
Total cash - group		268,740	243,398

The majority of Sterling cash deposits of the Fund are managed along with those of the administering authority (the City of Edinburgh Council) and other related organisations which are pooled for investment purposes as a treasury cash fund. Management of the cash fund is on a low risk basis, with security of the investments the key consideration.

Notes to the Accounts

21 Nature and extent of risk arising from financial instruments (cont)

	Moody's Credit Rating at 31 March 2017	Balances at 31 March 2016 £000	Balances at 31 March 2017 £000
Money market funds			
Deutsche Bank AG, London	Aaa-mf	117	652
Goldman Sachs	Aaa-mf	16,539	14
Bank call accounts			
Bank of Scotland	A1	8,123	11,911
Royal Bank of Scotland	A3	1,316	169
Santander UK	Aa3	10	30
Barclays Bank	A1	8,395	2
Svenska Handelsbanken	Aa2	8,562	23
HSBC Bank	Aa2	12	4
UK Pseudo-Sovereign risk instruments			
Other Local Authorities [1]	Aa1	24,726	106,563
UK Government Treasury Bills	Aa1	56,263	-
		124,063	119,368

[1] Very few Local Authorities have their own credit rating but they are generally assumed to have a pseudo-sovereign credit rating (which in the UK at 31 March 2017 was 'Aa1').

The Council has in place institutional restrictions on investments and counterparty criteria. These include -

- UK Government and other UK local Authorities with no limit, other public bodies up to £20 million per organisation.
- Money market funds (MMFs) no more than £30 million or 15% with any one Fund.
- Financial Institutions: Banks and Building Societies with multiple criteria based on a range of short and long term credit ratings, as well as any security, provided from maximum of £60 million / 20% of assets under management (AUM) for institutions with the highest criteria to £10 million / 5% of AUM for institutions with the lowest acceptable criteria.

No breaches of the Council's counterparty criteria occurred during the reporting period and the Fund does not expect any losses from non-performance by any of its counterparties in relation to deposits.

Securities lending

The Fund participates in a securities lending programme as described above. The Fund is potentially exposed to credit risk in the event of the borrower of securities defaulting. This risk is mitigated by the contractual commitment that borrowers provide collateral in excess of 100% of the value of the securities borrowed. In addition, Northern Trust has signed an agreement requiring it to make good any losses arising from the lending programme.

Derivatives

The Fund transacts foreign currency derivatives over-the-counter and hence is exposed to credit risk in the event of a counterparty defaulting on the net payment or receipt that remains outstanding. This risk is minimised by the use of counterparties that are recognised financial intermediaries with acceptable credit ratings and by netting agreements. At 31 March 2017, the Fund was owed £0.7m on over-the-counter foreign currency derivatives.

Refinancing risk

Refinancing risk is the risk that the Fund will be bound to replenish a significant proportion of its pension fund financial instruments at a time of unfavourable interest rates. The Fund is not bound by any obligation to replenish its investments and hence is not exposed to refinancing risk.

Notes to the Accounts

21 Nature and extent of risk arising from financial instruments (cont)

Liquidity risk

Liquidity risk reflects the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund therefore ensures that there is adequate cash and liquid resources to meet its commitments. Cash flow projections are prepared on a regular basis to understand and manage the timing of the Fund's cash flows.

The majority (estimated to be approximately 78% (2016 79%)) of the Fund's investments could be converted to cash within three months in a normal trading environment.

22 Actuarial statement

The Scheme Actuary has provided a statement describing the funding arrangements of the Fund. This can be found at the end of this section.

23 Actuarial present value of promised retirement benefits

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standard 19 (IAS19) assumptions, is estimated to be £8,210m (2016 £6,266m). This figure is used for statutory accounting purposes by Lothian Pension Fund and complies with the requirements of IAS26. The assumptions underlying the figure match those adopted for the Administering Authority's FRS17/IAS19 reports at each year end.

The figure is only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

	31 March 2016 % p.a.	31 March 2017 % p.a.
Inflation / pensions increase rate	2.2	2.4
Salary increase rate	4.2	4.4
Discount rate	3.5	2.6

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2012 model, assuming that the current rate of improvements has reached a peak and will converge to a long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies, in years, at age 65 are summarised below:

	31 March 2016		31 March 2017	
	Males	Females	Males	Females
Current pensioners	22.1 years	23.7 years	22.1 years	23.7 years
Future pensioners (assumed to be currently 45)	24.2 years	26.3 years	24.2 years	26.3 years

Commutation assumption

An allowance is included for future retirements to elect to take 50% of the maximum additional tax-free cash up to HMRC limits for pre-April 2009 service and 75% of the maximum tax-free cash for post-April 2009 service.

Notes to the Accounts

24 Non current debtors

	LPF Parent 31 March 2016 £000	LPF Group 31 March 2016 £000	LPF Group 31 March 2017 £000	LPF Group 31 March 2017 £000
Contributions due - employers' cessation	451	451	259	259
	451	451	259	259

Analysis of non current debtor

	LPF Parent 31 March 2016 £000	LPF Group 31 March 2016 £000	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000
Administering Authority	-	-	-	-
Other Scheduled Bodies	-	-	-	-
Community Admission Bodies	451	451	259	259
Transferee Admission Bodies	-	-	-	-
Other Local Authorities	-	-	-	-
Central Government Bodies	-	-	-	-
Other entities and individuals	-	-	-	-
	451	451	259	259

25 Debtors

	LPF Parent 31 March 2016 £000	LPF Group 31 March 2016 £000	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000
Contributions due - employers	10,219	10,219	11,175	11,175
Contributions due - members	2,067	2,067	3,304	3,304
Benefits paid in advance or recoverable	-	-	-	-
Sundry debtors	109	137	160	193
Corporation tax losses utilised by CEC group	-	5	-	1
Prepayments	275	275	283	292
LPFE & LPFI Limited Loan facility - see note 29	-	-	16	-
	12,670	12,703	14,938	14,965

Analysis of debtors

	LPF Parent 31 March 2016 £000	LPF Group 31 March 2016 £000	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000
Administering Authority	6,987	6,992	6,081	6,081
Other Scheduled Bodies	3,526	3,526	6,477	6,477
Community Admission Bodies	1,812	1,812	1,899	1,899
Transferee Admission Bodies	26	26	35	35
Other Local Authorities	-	29	22	56
Central Government Bodies	-	-	-	-
Other entities and individuals	319	318	424	417
	12,670	12,703	14,938	14,965

Notes to the Accounts

26 Creditors

	LPF Parent 31 March 2016 £000	LPF Group 31 March 2016 £000	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000
Benefits payable	8,375	8,375	5,745	5,745
VAT, PAYE and State Scheme premiums	1,399	1,495	2,940	3,052
Contributions in advance	11,845	11,845	8,719	8,719
Miscellaneous creditors and accrued expenses	2,083	2,121	2,760	2,809
Office - operating lease	216	216	266	266
LPFE Loan facility - see note 29	6	-	24	-
Intra group creditor - see note 29	92	-	105	-
	24,016	24,052	20,559	20,591

Analysis of Creditors

	LPF Parent 31 March 2016 £000	LPF Group 31 March 2016 £000	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000
Administering Authority	32	32	51	51
Other Scheduled Bodies	11,900	11,900	11,715	11,715
Community Admission Bodies	39	39	19	19
Transferee Admission Bodies	98	-	-	-
Central Government Bodies	1,359	1,455	2,889	3,001
Other entities and individuals	10,588	10,626	5,885	5,805
	24,016	24,052	20,559	20,591

27 Additional Voluntary Contributions

Active members of the Lothian Pension Fund have the option to pay additional voluntary contributions (AVCs). These AVCs are invested separately from the main funds, securing additional benefits on a money purchase basis for those members that have elected to contribute. The investment of the AVCs is managed by Standard Life and Prudential.

In accordance with regulation 4 (2) (b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010, AVCs are not included in the pension fund financial statements.

	2015/16 £000	2016/17 £000
Total contributions during year for Lothian Pension fund		
Standard Life	395	339
Prudential	1,593	1,816
	1,988	2,155
	31 March 2016 £000	31 March 2017 £000
Total value at year end for Lothian Pension Fund		
Standard Life	5,665	5,041
Prudential	3,863	5,097
	9,528	10,138

Notes to the Accounts

28 Related parties

The City of Edinburgh Council

The Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund are administered by the City of Edinburgh Council. Consequently there is a strong relationship between the Council and the Pension Funds.

The Investment and Pensions Service of the Council is responsible for administering the three Pension Funds. The Service receives an allocation of the overheads of the Council, based on the amount of central services consumed. In turn, the Service allocates its costs to the three Pension Funds. Costs directly attributable to a specific Fund are charged to the relevant Fund; costs that are common to all three Funds are allocated on a defined basis.

Transactions between the Council and the Fund are managed via a holding account. Each month the Fund is paid a cash sum leaving a working balance in the account to cover the month's pension payroll costs and other expected costs.

	31 March 2016 £000	31 March 2017 £000
Year end balance of holding account	4,287	4,467
	4,287	4,467

Part of the Fund's cash holdings are invested on the money markets by the treasury management operations of the Council, through a service level agreement. During the year to 31 March 2017, the fund had an average investment balance of £105.7m (2015/16 £219.0m). Interest earned was £427.4k (2015/16 £1,032.5k).

Year end balance on treasury management account	31 March 2016 £000	31 March 2017 £000
Held for investment purposes	82,736	92,090
Held for other purposes	41,327	27,278
	124,063	119,368

Scheme employers

All scheme employers to the fund are (by definition) related parties, a full list of employers can be found on page 64. The employer contributions for the ten largest scheme employers are as follows -

	31 March 2016 £000	31 March 2017 £000
City of Edinburgh Council	63,459	63,542
West Lothian Council	22,053	22,214
East Lothian Council	12,897	13,267
Midlothian Council	11,096	11,849
Scottish Water	8,419	9,191
Edinburgh Napier University	4,864	5,001
Scottish Police Authority	3,084	3,519
Heriot-Watt University	3,058	3,077
Edinburgh College	2,984	2,924
Audit Scotland	1,826	2,020

Notes to the Accounts

28 Related parties (cont)

Governance

As at 31 March 2017, all members of the Pensions Committee, with the exception of Councillor Bill Cook and Richard Lamont, and all members of the Pensions Board, with the exception of Graham Turnbull, were active members of the Lothian Pension Fund or Lothian Buses Pension Fund.

Each member of the Pensions Committee and Pension Board is required to declare any financial and non-financial interests they have in the items of business for consideration at each meeting, identifying the relevant agenda item and the nature of their interest.

During the period from 1 April 2015 to the date of issuing of these accounts, a number of employees of the City of Edinburgh Council and its wholly owned subsidiary, LPFE Limited, held key positions in the financial management of the Lothian Pension Fund. With effect from 1 May 2015, all the employees listed below, with the exception of the Executive Director of Resources, were employed by LPFE Limited. These employees and their financial relationship with the Fund (expressed as cash-equivalent transfer values or CETV) are set out below:

Name	Position held	Accrued CETV as at 31 March 2016 £000	Accrued CETV as at 31 March 2017 £000
Hugh Dunn*	Acting Executive Director of Resources, City of Edinburgh Council	755	1,251
Clare Scott*	Chief Executive, Lothian Pension Fund	175	221
Bruce Miller	Chief Investment Officer, Lothian Pension Fund	185	267
Struan Fairbairn	Chief Risk Officer, Lothian Pension Fund	30	46
John Burns	Chief Finance Officer, Lothian Pension Fund	474	538
Esmond Hamilton	Financial Controller, Lothian Pension Fund	161	200

* Also disclosed in the financial statements of the City of Edinburgh Council.

Total compensation paid in relation to key management personnel employed by LPFE Limited during the period was as follows:

	31 March 2016 £000	31 March 2017 £000
Short-term employee benefits	318	380
Post-employment benefits - employer pension contributions	65	78

Key management personnel employed by LPFE, had accrued pensions totalling £81,825 (1 April 2016: £68,004) and lump sums totalling £100,185 (1 April 2016: £68,004) at the end of the period.

Staff are either employed by City of Edinburgh Council or LPFE Ltd, and their costs reimbursed by the Pension Fund. The Councillors, who are members of the Pensions Committee, are also remunerated by City of Edinburgh Council.

LPFE Limited & LPFI Limited- loan facility

LPFE & LPFI Limited are wholly owned by the City of Edinburgh Council as administrating authority of Lothian Pension Fund and have entered into a shareholder agreement with the Council to address governance matters. The companies have a loan facility agreement with the City of Edinburgh Council for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the companies return any cash not immediately required and this can result in short periods when the companies have returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Interest payable by LPFE Limited during the period was £720 of which £156 was due at the year end and for LPFI Limited interest payable was £99 of which £30 was due at year end. At 31 March 2017, the balance on the loan facility was £24k due to LPFE Limited and £16k due from LPFI Limited.

Notes to the Accounts

28 Related parties (cont)

LPFE Limited & LPFI Limited- corporation tax losses used by companies under common control

In 2015/16 Lothian Buses Limited (also a member of City of Edinburgh Council's Corporation Tax Group) utilised the £5k tax loss from LPFE limited activity during the year. The tax loss of the company is transferred to another company in the Tax Group in exchange for the cash amount. Due to year end timing differences £1k of the loss is still outstanding to Lothian Buses Limited.

LPFE Limited - staffing services

Staffing services are provided to Lothian Pension Fund for the purposes of administering the Funds under a intra-group resourcing agreement. The agreement also provides for the running costs of the company to be covered as part of a service charge and allows for the provision of staffing services to LPFI Limited. During the year to 31 March 2017, the Fund was invoiced £1,073k (2016 £820k) for the services of LPFE Limited staff, £105k (2016 £92k) of this remained payable at year end.

29a Consolidated Lothian Pension Fund group - LPFE Limited & LPFI Limited - deferred tax

Movement in deferred tax asset (Non-current asset)

	LPF Group 2015/16 £000	LPF Group 2016/17 £000
At 1 April 2016	-	36
Credit for year to Fund Account	36	81
At 31 March 2017	36	117

Elements of closing deferred tax asset

	LPF Group 31 March 2016 £000	LPF Group 31 March 2017 £000
Pension liability	36	117
	36	117

29b Shares in group companies - LPFE Limited & LPFI Limited

	31 March 2016 £	31 March 2017 £
Allotted, called up and fully paid Ordinary shares of £1 each - LPFE Limited*	1	1
Allotted, called up and fully paid Ordinary shares of £1 each - LPFI Limited	-	50,000
	1	50,001

*One ordinary share of £1 was issued to Lothian Pension Fund at par value on incorporation. Due to the low value this does not show on the Net Assets Statement.

30 Retirement benefits obligation - group

The retirement benefit obligation described in this note relates only to the employees of LPFE Limited. This is because obligation in respect of the staff employed by the City of Edinburgh Council is accounted for in the City of Edinburgh Council's Financial Statements.

On 1 May 2015 LPFE Limited commenced trading and its staff transferred their employment from the City of Edinburgh Council to the Company on that date. At that time, the Company also entered into appropriate admission arrangements with the City of Edinburgh Council with respect to the transferring individuals continuing to be members of the Lothian Pension Fund and in relation to its obligations as an employer in that Fund.

The present value of the defined benefit obligation, and related current service cost and past service cost, were measured using the Projected Unit Credit Method.

Notes to the Accounts

30 Retirement benefits obligation - group (cont)

Fund assets

The LPFE Limited's share of the fair value of the Fund's assets which are not intended to be realised in the short term and may be subject to significant change before they are realised, were comprised as follows:

Asset		Fair value at 31 March 2016 £000	% of total 31 March 2016 %	Fair value at 31 March 2017 £000	% of total 31 March 2017 %
Equity securities:	Consumer	319	15.0	425	15.0
	Manufacturing	247	12.0	429	15.2
	Energy and utilities	167	8.0	210	7.4
	Financial institutions	178	8.0	197	7.0
	Health and care	139	7.0	166	5.9
	Information technology	126	6.0	140	4.9
	Other	120	6.0	195	6.9
Debt securities:	Corporate Bonds	-	0.0	-	0.0
	UK Government	135	6.0	284	10.0
	Other	53	3.0	6	0.2
Private equity:	All	92	4.0	91	3.2
Real property	UK property	179	9.0	191	6.7
Investment funds and unit trusts:	Equities	-	0.0	-	0.0
	Commodities	6	0.0	8	0.3
	Bonds	17	1.0	42	1.5
	Infrastructure	139	7.0	253	8.9
	Other	50	2.0	60	2.1
Cash and cash equivalents:	All	130	6.0	131	4.8
		2,097	100.0	2,828	100.0

Amounts recognised in the Net Assets Statement

	LPF Group 31 March 2016 £000	LPF Group 31 March 2017 £000
Fair value of Fund assets	2,097	2,828
Present value of Fund liabilities	(2,277)	(3,513)
	(180)	(685)

Notes to the Accounts

30 Retirement benefits obligation - group (cont)

Movement in the defined benefit obligation during the period

	LPF Group 2015/16 £000	LPF Group 2016/17 £000
Brought forward	2,107	2,277
Current service cost	174	172
Interest cost on obligation	69	86
Fund participants contributions	54	76
Benefits paid	-	-
Actuarial losses arising from changes in financial assumptions	(378)	902
Actuarial losses arising from changes in demographic assumptions	-	-
Other actuarial losses	251	-
Balance at year end	2,277	3,513

Movement in the fair value of Fund assets during the period

	LPF Group 2015/16 £000	LPF Group 2016/17 £000
Brought forward	1,826	2,097
Benefits paid	-	-
Interest income on Fund assets	60	80
Contributions by employer	121	156
Contributions by member	54	76
Contributions in respect of unfunded benefits	-	-
Unfunded benefits paid	-	-
Return on assets excluding amounts included in net interest	36	419
Balance at year end	2,097	2,828

Amounts recognised in the Fund Account

	LPF Group 2015/16 £000	LPF Group 2016/17 £000
Interest received on Fund assets	(60)	(80)
Interest cost on Fund liabilities	69	86
Current service costs	174	172
Transfer of opening retirement benefit obligation on 1 May 2015	281	-
Actuarial gains due to re-measurement of the defined benefit obligation	(127)	902
Return on Fund assets (excluding interest above)	(36)	(419)
Net cost recognised in Fund account	301	661
Less - cash flows	(121)	(156)
Increase in retirement benefit obligations	180	505

Principal actuarial assumptions used in this valuation

	31 March 2016 % p.a.	31 March 2017 % p.a.
Inflation / pensions increase rate	2.2	2.4
Salary increase rate	4.2	4.4
Discount rate	3.6	2.7

Notes to the Accounts

30 Retirement benefits obligation - group (cont)

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice. Best estimate has been interpreted to mean that the proposed assumptions are 'neutral' – there is an equal chance of actual experience being better or worse than the assumptions proposed.

The financial assumptions used for reporting in the financial statements are the responsibility of the employer. These assumptions are largely prescribed at any point and reflect market conditions at the reporting date. Changes in market conditions that result in changes in the net discount rate can have a significant effect on the value of the liabilities reported.

A reduction in the net discount rate will increase the assessed value of liabilities as a higher value is placed on benefits paid in the future. A rise in the net discount rate will have an opposite effect of a similar magnitude. There is also uncertainty around life expectancy of the UK population – the value of current and future pension benefits will depend on how long they are assumed to be in payment.

Life expectancy is based on Fund specific statistical analysis with improvements in line with the CMI 2012 model assuming current rates of improvements have peaked and will converge to a long term rate of 1.25% p.a.

Based on these assumptions, the average future life expectancies at age 65 are summarised below:

	31 March 2016		31 March 2017	
	Males	Females	Males	Females
Current pensioners	22.1 years	23.7 years	22.1 years	23.7 years
Future pensioners	24.2 years	26.3 years	24.2 years	26.3 years

Expected employer contributions to the defined benefit plan for the year ended 31 March 2018 are £157,000, based on a pensionable payroll cost of £764,000.

31 Contractual commitments

Investment commitments

The Fund has commitments relating to outstanding call payments due on unquoted funds held in the private equity, timber, property and infrastructure parts of the portfolio. The amounts 'called' by these funds are irregular in both size and timing, taking place over a number of years from the date of each original commitment. The outstanding commitments at the year end are as follows:

	31 March 2016	31 March 2017
	£000	£000
Outstanding investment commitments	160,891	235,565
	160,891	235,565

Office accommodation - 144 Morrison Street, Edinburgh

The Investment and Pensions Service is committed to making the following future payments.

	31 March 2016	31 March 2017
	£000	£000
Within one year	42	115
Between one and five years	345	345
After five years	992	877
	1,379	1,337
Recognised as an expense during the year	92	92

The above expense has been allocated across the three Funds, Lothian Pension Fund's share is £84.9k.

Notes to the Accounts

32 Contingent assets and liabilities

Infrastructure co-investment

At 31 March 2017 the Fund had entered into negotiations for an infrastructure co-investments in which it is exposed to the potential risk of investment abort costs. At 31 March 2017, Lothian Pension Fund's exposure is approximately £21.4k.

Contribution refunds

At 31st March 2017, Lothian Pension Fund had £473k in unclaimed refunds due to members.

Employer Cessations

The Fund has, in consultation with external advisors, drawn up a funding agreement to address repayment of the cessation debt. In order to avoid employer default or insolvency, the agreement will allow for repayment over longer terms, and if necessary for repayment of less than the cessation debt. In the latter scenario, an appropriate clause will be included which will allow the Fund to revisit the repayment of the remaining debt at a future date. At 31st March 2017, Lothian Pension Fund had £325k unsecured assets due from ceased employers.

EU Tax claims & income recovery

The Fund, in consultation with external advisers participates in various claims to recover withheld income on its investments. For some of these claims there is a high level of uncertainty on the success of these claims so they are not accrued for in the financial statements. The value of these outstanding claims is approximately £9.8m.

33 Impairment losses

During the year the Fund recognised a decrease in impairment losses in respect of specific benefit over payments for which reimbursement has been requested of £23.6k. This decreased the impairment to £22.8k at the year end.

Lothian Pension Fund

Actuarial Statement for 2016/17

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The funding policy is set out in the Administering Authority's Funding Strategy Statement (FSS), dated 16 November 2015. In summary, the key funding principles are as follows:

- To ensure solvency of the Fund;
- to ensure the solvency of each individual employers' share of the Fund based on their expected term of participation in the Fund;
- to minimise the degree of short-term change in employer contribution rates;
- maximise the returns from investments within reasonable and considered risk parameters, and hence minimise the cost to the employer;
- to ensure that sufficient cash is available to meet all liabilities as they fall due for payment;
- to help employers manage their pension liabilities; and
- where practical and cost effective, to make allowance for the different characteristics of different employers and groups of employers.

The FSS sets out how the Administering Authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 32 of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008 was as at 31 March 2014. This valuation revealed that the Fund's assets, which at 31 March 2014 were valued at £4,379 million, were sufficient to meet 91% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2014 valuation was £417 million.

Individual employers' contributions for the period 1 April 2015 to 31 March 2018 were set in accordance with the Fund's funding policy as set out in its FSS.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the valuation report dated 31 March 2015.

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth to retirement or expected earlier date of leaving pensionable membership.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market value.

Lothian Pension Fund

Actuarial Statement for 2016/17

The key financial assumptions adopted for the 2014 valuation were as follows:

Financial assumptions	31 March 2014	
	% p.a.	% p.a.
	Nominal	Real
Discount rate	5.0%	2.3%
Pay increases*	5.0%	2.3%
Price inflation/Pension increases	2.7%	-

*2% p.a. for 2014/15 and 2015/16, reverting to 5.0% thereafter.

The key demographic assumption was the allowance made for longevity. The life expectancy assumptions are based on the Fund's VitaCurves with improvements in line with the CMI_2012 model, assuming the current rate of improvements has reached a peak and will converge to long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	22.1 years	23.7 years
Future Pensioners *	24.2 years	26.3 years

*Future pensioners are assumed to be at the 2014 valuation aged 45.

Copies of the 2014 valuation report and Funding Strategy Statement are available on request from The City of Edinburgh Council, the Administering Authority to the Fund.

Experience over the period since April 2014

The Fund's experience has been worse than expected since the last formal valuation (excluding the effect of any membership movements and any potential changes to assumptions at the 2017 valuation). Real bond yields have fallen sharply which places a higher value on liabilities. The effect of this will have been partially offset by strong asset returns. Funding levels are therefore likely to have worsened and deficits increased over the period.

The next actuarial valuation will be carried out as at 31 March 2017. The Funding Strategy Statement will also be reviewed at that time.

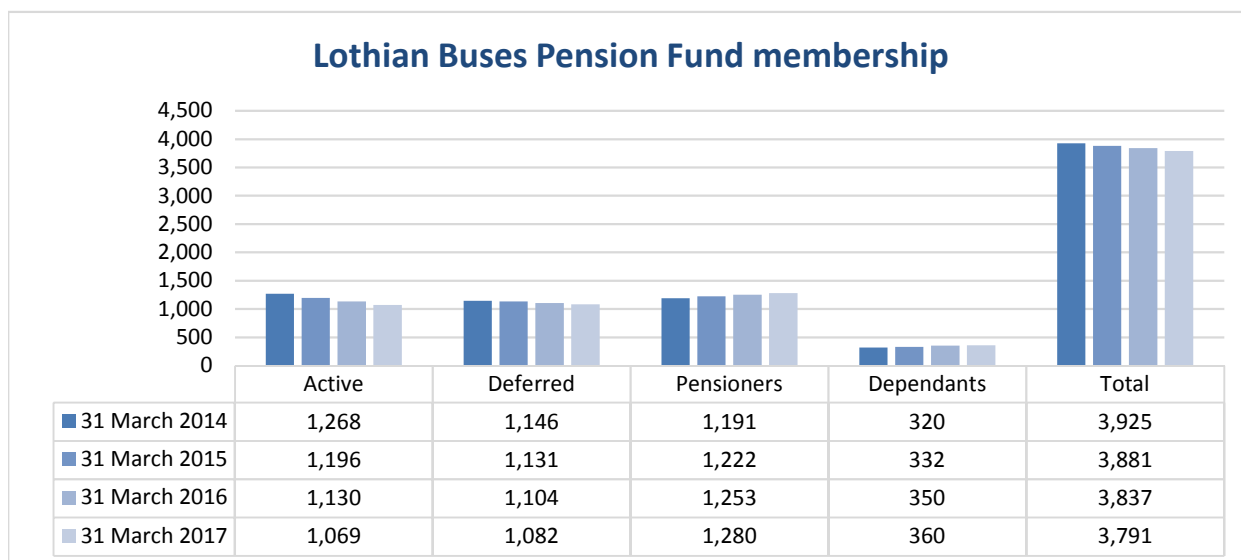
Richard Warden FFA
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
20 Waterloo Street
Glasgow
G2 6DB

28 April 2017

List of active employers at 31 March 2017

Scheduled Bodies	
City of Edinburgh Council (The)	Scottish Police Authority
East Lothian Council	Scottish Water
Edinburgh College	SESTRAN
Heriot-Watt University	Visit Scotland
Midlothian Council	West Lothian College
Scotland's Rural College (SRUC)	West Lothian Council
Scottish Fire and Rescue Service	
Admitted Bodies	
Amey Services	HWU Students Association
Audit Scotland	Improvement Service (The)
Barony Housing Association Ltd	Into Work
Baxter Storey	ISS UK Ltd
Bellrock Property and Facilities Management	Keymoves
Canongate Youth Project	LPFE Ltd
Capital City Partnership	Melville Housing Association
Centre for Moving Image (The)	Mitie PFI
CGI UK Ltd	Morrison Facilities Services Ltd
Children's Hearing Scotland	Museums Galleries Scotland
Children's Hospice Association Scotland	Newbattle Abbey College
Citadel Youth Centre	North Edinburgh Dementia Care
Compass Chartwell	NSL Ltd
Convention of Scottish Local Authorities	Open Door Accommodation Project
Dacoll Limited	Penumbra
Dean Orphanage and Cauvin's Trust	Pilton Equalities Project
Donaldson's Trust	Pilton Youth and Children's Project
EDI Group Ltd	Queen Margaret University
Edinburgh Business School	Queensferry Churches Care in the Community Project
Edinburgh Cyrenians Trust	Royal Edinburgh Military Tattoo
Edinburgh Development Group	Royal Society of Edinburgh
Edinburgh International Festival Society	Scotland's Learning Partnership
Edinburgh Leisure	Scottish Adoption Agency
Edinburgh Napier University	Scottish Futures Trust
Edinburgh World Heritage Trust	Scottish Legal Complaints Commission
ELCAP	Scottish Schools Education Research Centre (SSERC)
Enjoy East Lothian	Skanska UK
Family & Community Development West Lothian	St Andrew's Children's Society Limited
Family Advice and Information Resource	St Columba's Hospice
Festival City Theatres Trust	Stepping Out Project
First Step	Streetwork UK Ltd
Forth and Oban Ltd	University of Edinburgh (Edin College of Art)
Four Square (Scotland)	Victim Support Scotland
Freespace Housing Association	Waverley Care
Granton Information Centre	Weslo Housing Management
Handicabs (Lothian) Ltd	West Granton Community Trust
Hanover (Scotland) Housing Association	West Lothian Leisure
Health in Mind	Wester Hailes Land and Property Trust
Homeless Action Scotland	Young Scot Enterprise
Homes for Life Housing Partnership	Youthlink Scotland

Lothian Buses Pension Fund



Investment Strategy

An in-depth review of Lothian Buses Pension Fund's investment strategy was undertaken by the Investment Strategy Panel over the 2015/16 financial year, supported by asset liability modelling from the Fund's investment adviser. In March 2016, the Pensions Committee approved a revised investment strategy to be implemented over the five years from 2016 to 2021.

The revised strategy reduces the Fund's allocation to equities (including private equity) from 55% to 40% by the end of 2021 and increases the allocation to index-linked gilts from 15% to 20% and fixed income assets from 10% to 22% within the same timeframe.

The review highlighted the potential future funding level volatility on the employing company's balance sheet and contributions. It afforded the opportunity to clarify the funding approach for this increasingly mature pension fund (it is closed to new entrants) in the event of the funding level worsening and also at the point when the last active member leaves the Fund. After discussions with the majority shareholder and company, Lothian Buses has agreed to continue paying deficit contributions (if required) after the last active member has left the Fund. With this clarity, the Fund is able to continue to adopt a long-term investment approach.

A significant allocation to equities is retained because they have historically exhibited higher returns than bonds when held over the long term. Implementation of the strategy will include further de-risking within equities and an increasing exposure to index-linked assets and fixed income assets to provide greater downside protection in the event of further reductions in interest rates (a key driver of liability values).

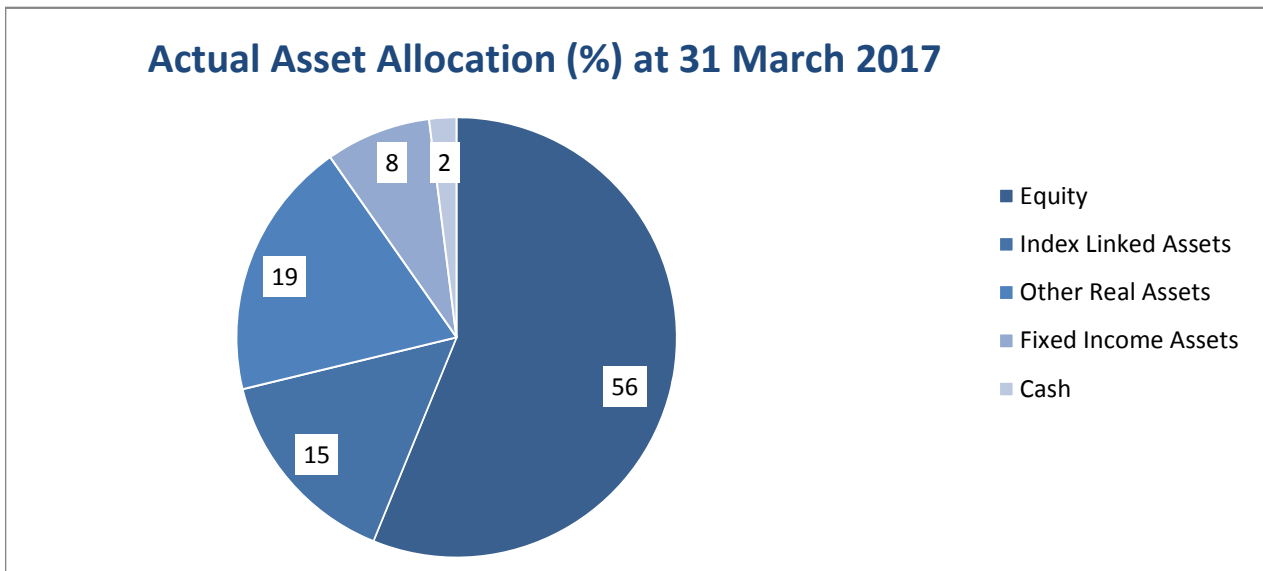
Over the course of 2016/17, the implementation of the investment strategy 2016-21 was initiated. The interim strategy allocation was adjusted over the year with equities reducing from 58.5% to 57%, index-linked gilts increasing from 14% to 15% and other real assets rising from 17.5% to 18%. Further progress will involve the interim strategy allocation and the actual asset allocation changing gradually over time.

In terms of the Fund's actual allocation over the year, equities reduced from 59% to 56%, index-linked assets increased from 12% to 15%, and other real assets and fixed income assets were stable at 19% and 8% respectively. These changes reflected both investment activity and the relative price movements of the various assets.

The investment strategy for 2016-21 is set out in the table below along with the current interim strategy.

	Strategic Allocation 31/03/2017 %	Long term Strategy 2016 - 2021 %
Equities	57.0	40.0
Index Linked Assets	15.0	20.0
Other Real Assets	18.0	18.0
Fixed Income Assets	10.0	22.0
Cash	-	-
Total	100.0	100.0

The investment strategy is now set at the broad asset class level of equities, index-linked assets, other real assets and fixed income assets, the latter two of which had previously been categorised within Alternatives. These broad groupings are the key determinants of investment risk and return. Equities includes listed and unlisted equities; index-linked assets includes index-linked gilts/bonds and gold; other real assets includes property, infrastructure and timber; and fixed income assets includes listed and unlisted debt investments.



Investment performance

The objectives of the Fund are:

- over long-term economic cycles (typically 5 years or more) the achievement of the same return as that generated by the strategic allocation
- over shorter periods, the Fund should perform better than the strategic allocation if markets fall significantly.

The Fund return fell slightly short of the benchmark over the last year, although the absolute return of 23.7% was well above historical averages. Over longer timeframes the Fund has returned more than its benchmark, as shown in the table below. The benchmark returns shown in the table represent the strategic allocations and comprise equity and index-linked gilt indices as well as an inflation-linked index for the other real and fixed income assets.

Annualised returns to 31 March 2016 (% per year)	1 year	5 year	10 years
Lothian Buses Pension Fund	23.7	13.2	9.6
Benchmark	24.2	11.5	8.0
Actuarial Valuation Assumptions *	5.0	5.5	5.8
Retail Price Index (RPI)	3.1	2.3	2.8
Consumer Price Index (CPI)	2.3	1.4	2.3
National Average Earnings	2.4	1.9	2.0

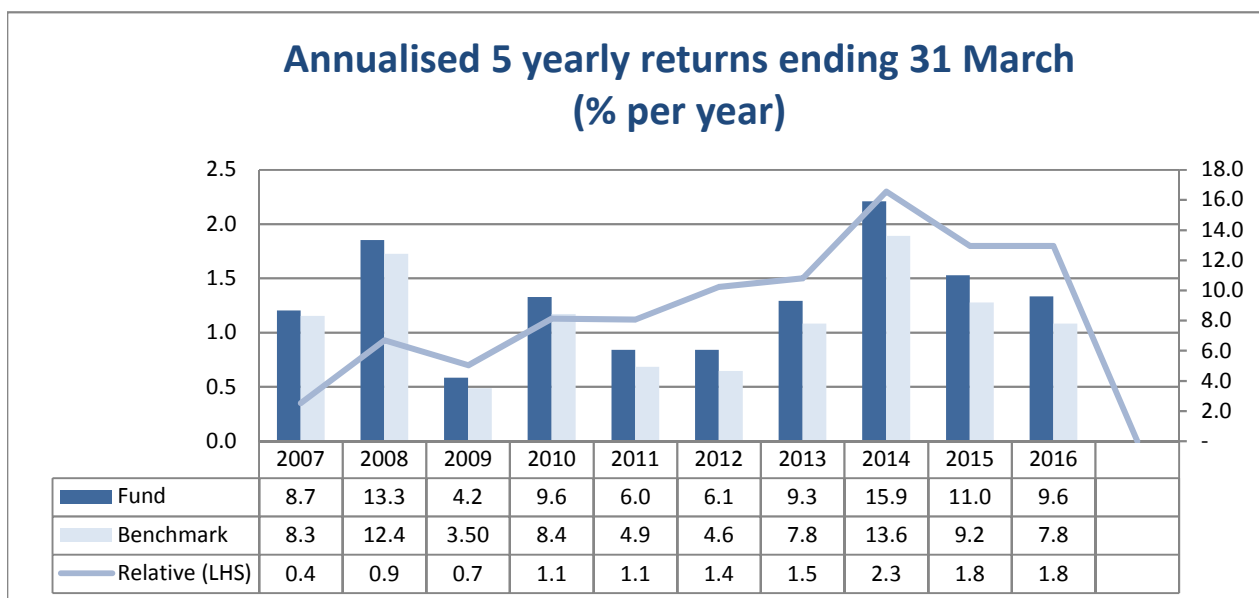
*estimate

The strong absolute return in 2016/17 was largely attributable to the global equity portfolios, one internally managed and one externally managed (by Baillie Gifford), which together rose in value by over 30%. The Fund's index-linked investments were also a significant contributor, driven by the internally-managed assets which rose 26% over the year. The real assets portfolio provided returns of over 6%, with timber and infrastructure assets returning close to 17% and 19% respectively, but offset by a disappointing return from property, which fell over 5% over the period. Fixed income assets returned 10% over the year, led by the corporate bond portfolio managed by Baillie Gifford (+10.2%), though private debt assets partially offset this with a return of 7.6%.

The shortfall in performance (-0.5%) relative to the benchmark over 2016/17 can be largely explained by the Fund's 2% allocation to cash throughout the year. This is a reflection of the fact that risk asset returns (especially equities and index-linked gilts) were so strong. The positive contribution to relative return from fixed income assets (+0.7%), led by the corporate bond portfolio (+0.7%) managed by Baillie Gifford, was offset by small shortfalls from equities (-0.2%), index-linked gilts (-0.1%) and from real assets (-0.4%), driven by weakness in property (-1.2%).

Returns relative to the benchmark over a one year period need to be placed in the context that there are no ideal benchmarks for many of the assets held in the Fund, especially the Alternatives. The Fund's benchmark for real and fixed income assets is inflation plus 3.5% per annum, which makes sense over the long term as the Fund's liabilities are linked to inflation. However, over shorter periods, there is less information content in the relative returns of the Fund because the development of asset prices is much more volatile than that of UK retail or consumer prices. The Investment Strategy Panel assesses the underlying risks of the portfolios that make up the asset allocation to ensure that these are consistent with the long term objectives of the Fund.

The chart below shows the rolling 5 year performance of the Fund against its strategic benchmark over the last 10 years. The Fund has consistently outperformed its benchmark over rolling 5 year periods. Relative returns on a rolling 5 year basis have generally been on an improving trend over the last 10 years, rising from 0.4% pa in 2007 to 1.7% pa in 2016.



Lothian Buses Pension Fund

Fund Account for year ended 31 March 2017

This statement shows a summary of the income and expenditure that the Pension Fund has generated and consumed in delivering the Local Government Pension Scheme. Included is the income generated from employers' and employees' contributions and investment income, as well as the cost of providing benefits and administration of the Fund.

2015/16			2016/17
£000		Note	£000
	Income		
7,538	Contributions from employer	3	7,731
2,129	Contributions from members		2,060
-	Transfers from other schemes		10
9,667			9,801
	Less: expenditure		
8,087	Pension payments including increases		8,425
2,101	Lump sum retirement payments		3,277
530	Lump sum death benefits		295
2	Refunds to members leaving service		9
129	Transfers to other schemes	4	418
102	Administrative expenses	5a	98
10,951			12,522
(1,284)	Net withdrawals from dealing with members		(2,721)
	Returns on investments		
8,076	Investment income	6	7,641
3,532	Change in market value of investments	8, 14b	90,672
(1,677)	Investment management expenses	5b	(1,880)
9,931	Net returns on investments		96,433
8,647	Net increase in the Fund during the year		93,712
385,784	Net assets of the Fund at 1 April 2016		394,431
394,431	Net assets of the Fund at 31 March 2017		488,143

Lothian Buses Pension Fund

Net Assets Statement as at 31 March 2017

This statement provides a breakdown of type and value of all net assets at the year end.

31 March 2016 £000		Note	31 March 2017 £000
	Investment Assets		
19,661	Bonds	7	73,313
236,417	Equities	7	273,603
121,923	Pooled investment vehicles	7	122,566
-	Derivatives - forward foreign exchange	9	-
11,811	Cash Deposits		14,074
1,291	Other investment assets		1,398
391,103			484,954
	Investment Liabilities		
(32)	Derivatives - forward foreign exchange	9	-
(283)	Other investment assets		(18)
(315)			(18)
390,788	Net investment assets	8, 10	484,936
	Current assets		
400	The City of Edinburgh Council	21	385
2,867	Cash balances	15, 21	2,440
828	Debtors	18	744
4,095			3,569
	Current liabilities		
(452)	Creditors	19	(362)
(452)			(362)
3,643	Net current assets		3,207
394,431	Net assets of the Fund at 31 March 2017		488,143

The unaudited accounts were issued on 28 June 2017 and the audited accounts were authorised for issue on 27 September 2017.

JOHN BURNS FCMA CGMA

Chief Finance Officer, Lothian Pension Fund

27 September 2017

Notes to the net asset statement

The financial statements summarise the transactions of the Fund during the year and its net assets at the year end. They do not take account of the obligations to pay pensions and benefits which fall due after the end of the year. The actuarial position of the Fund, which does take account of such obligations, is discussed in the Actuarial Valuation section of this report and these financial statements should be read in conjunction with that information. In addition, as required by IAS26, the Actuarial Present Value of Promised Retirement Benefits is disclosed in the notes to these financial statements.

Notes to the Financial Statements

1 Statement of Accounting Policies

The statement of accounting policies for all three Funds can be found on page 112.

2 Events after the Reporting Date

There have been no events since 31 March 2017, and up to the date when these accounts were authorised, that require any adjustments to these accounts.

3 Contributions from employer

By category	2015/16 £000	2016/17 £000
Normal (ongoing contributions)	7,425	7,516
Deficit contribution	-	-
Strain costs and augmentation contributions	113	215
	7,538	7,731

The Lothian Buses Pension Fund is a single employer pension fund for employees of Lothian Buses Limited. The Lothian Buses Fund was set up in 1986 under the Local Government Superannuation (Funds) (Scotland) Regulations 1986 (SSI 115/1986).

The employer contribution rate was 22.9% for the period from 1 April 2016 to 31 December 2016 then 24.1% for the remainder of the financial year.

Where the employer makes certain decisions which result in additional benefits being paid out to a member, or benefits being paid early, this results in a "strain" on the Fund. The resulting pension strain costs are calculated and recharged in full to the employer.

4 Transfers out to other pension schemes

	2015/16 £000	2016/17 £000
Group transfers	-	-
Individual transfers	129	418
	129	418

Notes to the Financial Statements

5a Administrative expenses

	2015/16 £000	2016/17 £000
Employee Costs	52	55
The City of Edinburgh Council - other support costs	7	6
System costs	13	13
Actuarial fees	13	9
External audit fees	2	2
Legal fees	-	-
Printing and postage	4	4
Depreciation	3	3
Office costs	6	5
Sundry costs less sundry income	2	1
	102	98

The Investment and Pensions Service of the Council is responsible for administering the three pension Funds. The Service receives an allocation of the overheads of the Council. In turn the Service allocates administration and investment costs to the three pension funds. Costs directly attributable to a specific fund are charged to the relevant Fund, costs that are common to all three funds are allocated on a defined basis.

5b Investment management expenses

	2015/16 £000	2016/17 £000
<u>External management fees -</u>		
invoiced	704	616
deducted from capital (direct investment)	329	694
deducted from capital (indirect investment)	368	325
Securities lending fees	43	20
Transaction costs	59	33
Employee costs	70	82
Custody fees	34	33
Engagement and voting fees	6	6
Performance measurement fees	17	19
Consultancy fees	12	5
System costs	13	18
Legal fees	3	9
The City of Edinburgh Council - other support costs	9	8
Depreciation	1	2
Office costs	5	6
Sundry costs less sundry income	4	4
	1,677	1,880

Any costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions or in the proceeds of investment sales (see note 8 - Reconciliation of movements in investments and derivatives).

The external investment management fees above include £0.3m in respect of performance-related fees (2015/16 £0.1m).

Notes to the Financial Statements

5b Investment management expenses (cont)

It should be noted that Lothian Buses Pension Fund's disclosure on investment management fees goes further than CIPFA's LGPS Management Cost revised guidance on cost transparency which came into effect on 1st April 2016. Consistent with recent years, the Fund recognises fees deducted from investments not within its direct control (such as fund of fund fees) to give a full picture of its investment management costs. Further details can be found on page 19. This further disclosure highlights an extra £325k in costs (2015/16 £368k)

5c Total management expenses

	2015/16 £000	2016/17 £000
Administrative costs	80	78
Investment management expenses*	1,621	1,814
Oversight and governance costs	78	86
	1,779	1,978

* as per note 5b, includes £325k (2015/16 £368k) in costs above CIPFA guidance

In accordance with CIPFA, the above analysis looks at the combined administration and investment management expenses in notes 5a and b and splits out the costs to include a third category covering oversight and governance expenditure.

6 Investment income

	2015/16 £000	2016/17 £000
Income from bonds	92	186
Dividends from equities	6,025	7,026
Income from pooled investment vehicles	1,751	452
Interest on cash deposits	53	18
Stock lending and sundries	214	103
	8,135	7,785
Irrecoverable withholding tax	(59)	(144)
	8,076	7,641

Notes to the Financial Statements

7 Analysis of investments

	Region	31 March 2016 £000	31 March 2017 £000
Investment Assets			
Bonds			
Public sector fixed interest securities	Overseas	1,122	-
Public sector index linked gilts quoted	UK	18,539	73,313
		19,661	73,313
Equities			
Quoted	UK	32,849	33,935
Quoted	Overseas	203,568	239,668
		236,417	273,603
Pooled investment vehicles			
Managed funds - property	UK	37,492	38,146
Managed funds - index linked gilts	UK	28,326	-
Managed funds - other bonds	UK	27,221	30,100
Timber funds - unquoted	Overseas	8,023	8,361
Infrastructure - unquoted	UK	4,424	26,636
Infrastructure - unquoted	Overseas	13,583	12,607
Private debt funds - unquoted	UK	1,051	2,266
Private debt funds - unquoted	Overseas	1,803	4,450
		121,923	122,566

8 Reconciliation of movement in investments and derivatives

	Market value at 31 March 2016 £000	Purchases at cost & derivative payments £000	Sales & derivative receipts £000	Change in market value £000	Market value at 31 March 2017 £000
Bonds	19,661	87,284	(49,714)	16,082	73,313
Equities	236,417	15,473	(41,164)	62,877	273,603
Pooled investment vehicles	121,923	18,969	(29,504)	11,178	122,566
Derivatives - fwd foreign exchange	(32)	604	(265)	(307)	-
Derivatives - futures	-	3	(692)	689	-
	377,969	122,333	(121,339)	90,519	469,482
Other financial assets / (liabilities)					
Cash deposits	11,811			69	14,074
Broker balances	(73)			84	(18)
Dividend due etc	1,081			-	1,398
	12,819			153	15,454
Net financial assets	390,788			90,672	484,936

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.

Notes to the Financial Statements

8 Reconciliation of movement in investments and derivatives (cont)

Any costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions and in the proceeds from sales and are therefore included in the tables above.

	Market value at 31 March 2015 £000	Purchases at cost & derivative payments £000	Sales & derivative receipts £000	Change in market value £000	Market value at 31 March 2016 £000
Bonds	13,209	10,193	(4,284)	543	19,661
Equities	242,863	27,541	(31,081)	(2,906)	236,417
Pooled investment vehicles	105,943	12,172	(1,947)	5,755	121,923
Derivatives - fwd foreign exchange	-	31	(7)	(56)	(32)
	362,015	49,937	(37,319)	3,336	377,969
Other financial assets / (liabilities)					
Cash deposits	19,174			112	11,811
Broker balances	(17)			84	(73)
Dividend due etc	991			-	1,081
	20,148			196	12,819
Net financial assets	382,163			3,532	390,788

9 Derivatives - forward foreign exchange

Summary of contracts held at 31 March 2017

Contract settlement within	Currency bought	Currency sold	Local currency bought 000	Local currency sold 000	Asset value £000	Liability value £000
Up to one month	-	-	-	-	-	-
Open forward currency contracts at 31 March 2017					-	-
Net forward currency contracts at 31 March 2017						-
Prior year comparative						
Open forward currency contracts at 31 March 2016					-	(32)
Net forward currency contracts at 31 March 2016						(32)

At the year ended 31 March 2017 the Lothian Buses Pension Fund did not hold any Forward foreign exchange contracts.

Notes to the Financial Statements

10 Investment managers and mandates

Manager	Mandate	Market value at 31 March 2016 £000	% of total 31 March 2016 %	Market value at 31 March 2017 £000	% of total 31 March 2017 %
Baillie Gifford	Global equities	112,761	28.9	124,570	25.7
In-house	Global high dividend	116,638	29.8	142,297	29.3
In-house	Private equity quoted	4,659	1.2	6,287	1.3
Total global equities		234,058	59.9	273,154	56.3
Baillie Gifford	Index linked gilts	28,326	7.2	-	0.0
In-house	Index linked gilts	19,771	5.1	73,793	15.2
Total inflation linked bonds		48,097	12.3	73,793	15.2
Baillie Gifford	Corporate bonds	27,221	7.0	30,100	6.2
In-house	Secured loans quoted	4	0.0	-	0.0
In-house	Secured loans unquoted	2,855	0.7	6,716	1.4
Total fixed income assets		30,080	7.7	36,816	7.6
Standard Life	Property	37,491	9.6	38,146	7.9
In-house	Infrastructure unquoted	18,007	4.6	39,243	8.1
In-house	Infrastructure quoted	6,660	1.7	3,661	0.8
In-house	Timber	8,022	2.1	8,361	1.7
Total other real assets		70,180	18.0	89,411	18.5
In-house	Cash	8,373	2.1	11,762	2.4
Total cash and sundries		8,373	2.1	11,762	2.4
Net financial assets		390,788	100.0	484,936	100.0

11 Investments representing more than 5% of the net assets of the Fund

	Market value at 31 March 2016 £000	% of net assets 31 March 2016	Market value at 31 March 2017 £000	% of net assets 31 March 2017
Standard Life Property Fund	37,491	9.5	38,146	7.9
Baillie Gifford Inv Grade Bond Fund	27,221	6.9	30,100	6.2
Baillie Gifford Index Linked Gilt Fund	28,326	7.2	-	0.0

Notes to the Financial Statements

12 Investments representing more than 5% of any investment class

	Market value at 31 March 2016 £000	% of asset class 31 March 2016	Market value at 31 March 2017 £000	% of asset class 31 March 2017
Bonds				
UK Gov 1.125% Index Linked 22/11/37	1,213	6.2	10,490	14.3
UK Gov 0.125% Index Linked 22/03/44	3,142	16.0	10,003	13.6
UK Gov 1.25% Index Linked 2055	2,341	11.9	8,634	11.8
UK Gov 0.125% Index Linked 22/03/68	1,981	10.1	7,624	10.4
UK Gov 0.625% Index Linked 22/03/40	1,228	6.2	7,225	9.9
UK Gov 0.125% Index Linked 22/03/58	1,847	9.4	6,300	8.6
UK Gov 0.25% Index Linked 22/03/52	1,133	5.8	4,203	5.7
UK Gov 0.375% Index Linked 22/03/62	919	4.7	3,650	5.0
UK Gov 2% Index Linked 26/01/35	1,360	6.9	3,405	4.6
Pooled funds				
Standard Life Property Fund	37,491	30.8	38,146	31.0
Baillie Gifford Inv Grade Bond Fund	27,221	22.3	30,100	24.4
Baillie Gifford Index Linked Gilt Fund	28,326	23.2	-	0.0

13 Securities lending

During the year Lothian Buses Pension Fund participated in a securities lending arrangement with the Northern Trust Company. As at 31 March 2017, £17.4m (2016 £10.4m) of securities were released to third parties. Collateral valued at 105.24% (2016 110.26%) of the market value of the securities on loan was held at that date.

14 Financial Instruments

14a Classification of financial instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the fair value amounts of financial assets and liabilities by category and net assets statement heading. No financial assets were reclassified during the accounting period.

All financial instruments are marked to market (at fair value) in the Fund's accounting records, hence there is no difference between the carrying value and fair value.

Notes to the Financial Statements

14a Classification of financial instruments

	31 March 2016			31 March 2017		
	Designated as fair value through fund account £000	Loans and receivables £000	Financial liabilities at amortised cost £000	Designated as fair value through fund account £000	Loans and receivables £000	Financial liabilities at amortised cost £000
Financial assets						
Investment assets						
Bonds	19,661	-	-	73,313	-	-
Equities	236,417	-	-	273,603	-	-
Pooled investments	121,923	-	-	122,566	-	-
Cash	-	11,811	-	-	14,074	-
Other balances	-	1,291	-	-	1,398	-
	378,001	13,102	-	469,482	15,472	-
Other assets						
City of Edinburgh Council	-	400	-	-	385	-
Cash	-	2,867	-	-	2,440	-
Debtors	-	828	-	-	744	-
	-	4,095	-	-	3,569	-
Assets total	378,001	17,197	-	469,482	19,041	-
Financial liabilities						
Investment liabilities						
Derivative contracts	(32)	-	-	-	-	-
Other investment balances	-	-	(283)	-	-	(18)
	(32)	-	(283)	-	-	(18)
Other liabilities						
Creditors	-	-	(452)	-	-	(362)
Liabilities total	(32)	-	(735)	-	-	(380)
Total net assets	377,969	17,197	(735)	469,482	19,041	(380)

Total net financial assets	394,431	488,143
-----------------------------------	---------	---------

14b Net gains and losses on financial instruments

	2015/16 £000	2016/17 £000
Designated as fair value through fund account	3,336	90,519
Loans and receivables	196	153
Financial liabilities at amortised cost	-	-
Total	3,532	90,672

Notes to the Financial Statements

14c Valuation of financial instruments carried at fair value

The valuation of financial instruments has been classified into three levels, according to the quality and reliability of information used to determine fair values.

Level 1

Financial instruments at Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities and unit trusts.

Quoted investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Level 2

Financial instruments at Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3

Financial instruments at Level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data. Such instruments would include unquoted equity investments, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investments in unquoted private debt, infrastructure and timber are based on valuations provided by the general partners to the funds in which the Fund has invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of International Financial Reporting Standards (IFRS). The valuations are typically undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

Notes to the Financial Statements

14c Valuation of financial instruments carried at fair value (cont)

	31 March 2017			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Investment assets				
Designated as fair value through fund account	341,849	73,313	54,320	469,482
Loans and receivables	15,472	-	-	15,472
Total investments assets	357,321	73,313	54,320	484,954
Investment liabilities				
Designated as fair value through fund account	(18)	-	-	(18)
Total investment liabilities	(18)	-	-	(18)
Net Investment assets	357,303	73,313	54,320	484,936

	31 March 2016			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Investment assets				
Designated as fair value through fund account	329,457	19,661	28,883	378,001
Loans and receivables	13,102	-	-	13,102
Total investments assets	342,559	19,661	28,883	391,103
Investment liabilities				
Designated as fair value through fund account	(315)	-	-	(315)
Total investment liabilities	(315)	-	-	(315)
Net Investment assets	342,244	19,661	28,883	390,788

14d Reconciliation of fair value measurements within level 3

	Market value at 31 March 2016	Level 3 transfers		Purchases at cost & derivative payments	Sales & derivative receipts	Unrealised gains / (losses)	Realised gains / (losses)	Market value at 31 March 2017
		in	out					
Pooled investments								
Infrastructure	18,007	-	-	18,781	(2,306)	4,456	305	39,243
Timber	8,022	-	-	-	(889)	188	1,040	8,361
Secured loans	2,854	-	-	3,953	(291)	3	197	6,716
	28,883	-	-	22,734	(3,486)	4,647	1,542	54,320

Unrealised and realised gains and losses are recognised in the profit and losses on disposal and changes in the market value of investments line of the fund account.

Notes to the Financial Statements

15 Nature and extent of risk arising from financial instruments

Risk and risk management

The Fund's primary aim is to ensure that all members and their dependants receive their benefits when they become payable. The investment strategy aims to maximise the returns from investments within reasonable risk parameters and hence minimise the long-term cost to employers. The Fund achieves this by investing in a diverse range of assets to reduce risk to an acceptable level. In addition, the Fund ensures that sufficient cash is available to meet all liabilities when they are due to be paid.

Responsibility for the Fund's overall investment strategy rests with the Pensions Committee. The Investment Strategy Panel and the internal investment team monitor investment risks on a regular basis. Investment risk management tools are used to identify and analyse risks faced by the Fund's investments.

Consideration of the Fund's investment risk is part of the overall risk management of the pensions operations. Risks are reviewed regularly to reflect changes in activity and market conditions.

Types of investment risk

There are various ways of considering investment risks for pension funds. For the purposes of this note, market risk is the potential for an investor to experience losses from falls in the prices of investments. All financial instruments, including cash deposits, present a risk of loss of capital and risks vary depending on different asset classes.

Market risk also changes over time as economic conditions and investor sentiment change. The Fund considers overall fluctuations in prices arising from a variety of sources: market risk, foreign exchange risk, interest rate risk, credit risk, etc. The different risks may, to some extent, offset each other.

The overall market risk of the Fund depends on the actual mix of assets and encompasses all the different elements of risk.

The Fund manages these risks in a number of ways:

- assessing and establishing acceptable levels of market risk when setting overall investment strategy. Importantly, risk is considered relative to the liabilities of the Fund
- diversification of investments in terms of type of asset, investment styles, investment managers, geographical and industry sectors as well as individual securities
- taking stewardship responsibilities seriously and pursuing constructive engagement with the companies in which we invest
- monitoring market risk and market conditions to ensure risk remains within tolerable levels
- using equity futures contracts from time to time to manage market risk. Options are not used by the Fund.

Notes to the Financial Statements

15 Nature and extent of risk arising from financial instruments (cont)

Sensitivity analysis

Asset prices have a tendency to fluctuate. The degree of such fluctuation is known as “volatility” and it differs by asset class. The table sets out the long-term volatility assumptions used in the Fund’s asset-liability modelling undertaken by the Fund’s investment adviser KPMG:

Asset type	Potential price movement (+ or -)
Equities - Developed Markets	20.5%
Private Equity	30.0%
Timber and Gold	18.0%
Secured Loans	8.0%
Corporate Bonds	5.5%
Index-Linked Gilts	10.9%
Infrastructure	18.0%
Property	13.0%
Cash	1.1%

Volatility is the standard deviation of annual returns. Broadly speaking, in two years out of three, the asset’s change in value (which could be a gain or a loss) is expected to be lower than the volatility figure, but in one year out of three, the change in value is expected to be higher than the volatility figure.

Asset classes do not always move in line with each other. The extent to which assets move together is known as their “correlation”. A lower correlation means that there is less risk of assets losing value at the same time.

The overall Fund benefits from “diversification” because it invests in different asset classes, which don’t all move in line with each other. Consequently, the aggregate risk at the Fund level is less than the total risk from all the individual assets in which the Fund invests. The following table shows the risks at the asset class level and the overall Fund level, with and without allowance for correlation.

	Value at 31 March 2017 £000	% of fund %	Potential Change +/- %	Value on increase £000	Value on decrease £000
Equities - Developed Markets	266,867	55.1	20.5	321,575	212,159
Private Equity	6,287	1.3	30.0	8,173	4,401
Timber and Gold	8,361	1.7	18.0	9,866	6,856
Secured Loan	6,717	1.4	8.0	7,254	6,180
Corporate Bonds	30,100	6.2	5.5	31,764	28,436
Index-Linked Gilts	73,793	15.2	10.9	81,801	65,785
Infrastructure	42,903	8.8	18.0	50,626	35,180
Property	38,146	7.9	13.0	43,105	33,187
Cash and forward foreign exchange	11,762	2.4	1.1	11,892	11,632
Total [1]	484,936	100.0	16.7	566,055	403,817
Total [2]			13.9	552,240	417,632
Total [3]			13.9	552,287	n/a

[1] No allowance for correlations between assets

[2] Including allowance for correlations between assets

[3] Including allowance for correlation between assets and liabilities.

Notes to the Financial Statements

15 Nature and extent of risk arising from financial instruments (cont)

The value on increase/decrease columns illustrate the monetary effect of the percentage change in the volatility column. The actual annual change in value is expected to be lower than this in two years out of three, but higher in one year out of three.

It can be seen that the risk to the overall Fund assets [2] is lower than the total of the risks to the individual assets.

However, because the purpose of a pension scheme is to make payments to scheme beneficiaries, the true risk of a pension scheme is not measured in absolute terms, but relative to its liabilities [3].

This risk analysis incorporates volatility from market, interest rate, foreign exchange, credit, and all other sources of risk, and, importantly, makes allowance for how these risks may offset each other.

Credit risk

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit risk in their pricing and consequently the risk of loss is implicitly provided for in the value of the Fund's assets and liabilities (as outlined in Market Risk above).

In essence, the Fund's entire investment portfolio is exposed to some sort of credit risk. However, through the selection of counterparties, brokers and financial institutions the Fund reduces the credit risk that may occur through the failure to settle a transaction in a timely manner.

Cash deposits, derivatives and securities lending are the major areas of credit exposure where credit risk is not reflected in market prices.

Cash deposits

At 31 March 2017, cash deposits represented £16.5m, 3.3% of total net assets. This was held with the following institutions:

	Moody's Credit Rating at 31 March 2017	Balances at 31 March 2016 £000	Balances at 31 March 2017 £000
Held for investment purposes			
Northern Trust Global Investment Limited - liquidity funds	Aaa-mf	2,384	3,270
Northern Trust Company - cash deposits	Aa2	8,509	9,882
The City of Edinburgh Council - treasury management	See below	918	922
Total investment cash		11,811	14,074
Held for other purposes			
The City of Edinburgh Council - treasury management	See below	2,867	2,440
Total cash		14,678	16,514

The majority of Sterling cash deposits of the Fund are managed along with those of the administering authority (the City of Edinburgh Council) and other related organisations which are pooled for investment purposes as a treasury cash fund. Management of the cash fund is on a low risk basis, with security of the investments the key consideration.

Notes to the Financial Statements

15 Nature and extent of risk arising from financial instruments (cont)

The Council has in place institutional restrictions on investments and counterparty criteria. These include -

- (a) UK Government and other UK local Authorities with no limit, other public bodies up to £20 million per organisation.
- (b) Money market funds (MMFs) no more than £30 million or 15% with any one Fund.
- (c) Financial Institutions: Banks and Building Societies with multiple criteria based on a range of short and long term credit ratings, as well as any security provided, from maximum of £60 million / 20% of assets under management (AUM) for institutions with the highest criteria to £10 million / 5% of AUM for institutions with the lowest acceptable criteria.

	Moody's Credit Rating at 31 March 2017	Balances at 31 March 2016 £000	Balances at 31 March 2017 £000
Money market funds			
Deutsche Bank AG, London	Aaa-mf	505	18
Goldman Sachs	Aaa-mf	4	-
Bank call accounts			
Bank of Scotland	A1	248	336
Royal Bank of Scotland	A3	40	5
Santander UK	Aa3	-	1
Barclays Bank	A1	256	-
Svenska Handelsbanken	Aa2	261	1
UK Pseudo-Sovereign risk instruments			
Other Local Authorities [1]	Aa1	1,717	3,001
UK Government Treasury Bills	Aa1	754	-
		3,785	3,362

[1] Very few Local Authorities have their own credit rating but they are generally assumed to have a pseudo-sovereign credit rating (which in the UK at 31 March 2017 was 'Aa1').

No breaches of the Council's counterparty criteria occurred during the reporting period and the Fund does not expect any losses from non-performance by any of its counterparties in relation to deposits.

Securities lending

The Fund participates in a securities lending programme as described above. The Fund is potentially exposed to credit risk in the event of the borrower of securities defaults. This risk is mitigated by the contractual commitment that borrowers provide collateral in excess of 100% of the value of the securities borrowed. In addition, Northern Trust has signed an agreement requiring it to make good any losses arising from the lending programme.

Derivatives

The Fund transacts foreign currency derivatives over-the-counter and hence is exposed to credit risk in the event of a counterparty defaulting on the net payment or receipt that remains outstanding. This risk is minimised by the use of counterparties that are recognised financial intermediaries with acceptable credit ratings and by netting agreements. At 31 March 2017, the Fund had no over-the-counter foreign currency derivatives.

Refinancing risk

Refinancing risk is the risk that the Fund will be bound to replenish a significant proportion of its pension fund financial instruments at a time of unfavourable interest rates. The Fund is not bound by any obligation to replenish its investments and hence is not exposed to refinancing risk.

Notes to the Financial Statements

15 Nature and extent of risk arising from financial instruments (cont)

Liquidity risk

Liquidity risk reflects the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund therefore ensures that there is adequate cash and liquid resources to meet its commitments. Cash flow projections are prepared on a regular basis to understand and manage the timing of the Fund's cash flows.

The majority (estimated to be approximately 89% (2016 93%)) of the Fund's investments could be converted to cash within three months in a normal trading environment.

16 Actuarial statement

The Scheme Actuary has provided a statement describing the funding arrangements of the Fund. This can be found at the end of this section.

17 Actuarial present value of promised retirement benefits

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standard 19 (IAS19) assumptions, is estimated to be £488m (2016 £374m). This figure is used for statutory accounting purposes by Lothian Buses Pension Fund and complies with the requirements of IAS26.

The figure is only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

Financial assumptions	31 March 2016	31 March 2017
	% p.a.	% p.a.
Inflation/pensions increase rate	2.2	2.4
Salary increase rate	4.2	4.4
Discount rate	3.5	2.6

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2012 model, assuming that the current rate of improvements has reached a peak and will converge to a long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies, in years, at age 65 are summarised below:

	31 March 2016		31 March 2017	
	Males	Females	Males	Females
Current pensioners	20.4 years	22.9 years	20.4 years	22.9 years
Future pensioners (assumed to be currently 45)	23.5 years	25.9 years	23.5 years	25.9 years

Commutation assumption

An allowance is included for future retirements to elect to take 50% of the maximum additional tax-free cash up to HMRC limits for pre-April 2009 service and 75% of the maximum tax-free cash for post-April 2009 service.

Notes to the Financial Statements

18 Debtors

	2015/16 £000	2016/17 £000
Contributions due - employer	576	581
Contributions due - members	158	153
Sundry debtors	94	10
	828	744

Analysis of debtors

	31 March 2016 £000	31 March 2017 £000
Administering Authority	1	1
Lothian Buses Limited	818	733
Other entities and individuals	9	10
	828	744

19 Creditors

	31 March 2016 £000	31 March 2017 £000
Benefits payable	275	201
Miscellaneous creditors and accrued expenses	177	161
	452	362

Analysis of creditors

	31 March 2016 £000	31 March 2017 £000
Other entities and individuals	452	362
	452	362

20 Additional Voluntary Contributions

Active members of the Lothian Buses Pension Fund have the option to pay additional voluntary contributions (AVCs). These AVCs are invested separately from the main funds, securing additional benefits on a money purchase basis for those members that have elected to contribute. The investment of the AVCs is managed by Standard Life and Prudential.

In accordance with regulation 4 (2) (b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010, AVCs are not included in the pension fund financial statements.

Total contributions during year	2015/16 £000	2016/17 £000
Standard Life	6	8
Prudential	61	70
	67	78

Total value at year end	31 March 2016 £000	31 March 2017 £000
Standard Life	170	155
Prudential	315	294
	485	449

Notes to the Financial Statements

21 Related party transactions

The City of Edinburgh Council

The Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund are administered by the City of Edinburgh Council. Consequently there is a strong relationship between the Council and the Pension Funds.

The Investment and Pensions Service of the Council is responsible for administering the three Pension Funds. The Service receives an allocation of the overheads of the Council, based on the amount of central services consumed. In turn, the Service allocates its costs to the three Pension Funds. Costs directly attributable to a specific Fund are charged to the relevant Fund; costs that are common to all three Funds are allocated on a defined basis.

Transactions between the Council and the Fund are managed via a holding account. Each month the Fund is paid a cash sum leaving a working balance in the account to cover the month's pension payroll costs and other expected costs.

	31 March 2016 £000	31 March 2017 £000
Year end balance of holding account	400	385
	400	385

Part of the Fund's cash holdings are invested on the money markets by the treasury management operations of the Council, through a service level agreement. During the year to 31 March 2017, the fund had an average investment balance of £3.0m (2016 £9.5m). Interest earned was £12.1k (2016 £12.2k).

Year end balance on treasury management account	31 March 2016 £000	31 March 2017 £000
Held for investment purposes	918	922
Held for other purposes	2,867	2,440
	3,785	3,362

Scheme employer - Lothian Buses Limited

Lothian Buses Limited are (by definition) a related party to the scheme. The employer contributions to the Fund can be found in note 3 (page 70) of the notes to the Financial Statements.

Governance

As at 31 March 2017, all members of the Pensions Committee, with the exception of Councillor Bill Cook and Richard Lamont, and all members of the Pensions Board, were members of the Lothian Pension Fund or Lothian Buses Pension Fund, with one member of the Pensions Board in receipt of pension benefits from Lothian Pension Fund.

Each member of the Pensions Committee and Pension Board is required to declare any financial and non-financial interests they have in the items of business for consideration at each meeting, identifying the relevant agenda item and the nature of their interest.

Notes to the Financial Statements

21 Related party transactions (cont)

With effect from 1 May 2015, all the employees listed below, with the exception of the Executive Director of Resources, were employed by LPFE Limited. These employees and their financial relationship with the Fund (expressed as cash-equivalent transfer values or CETV) are set out below:

Name	Position held	Accrued CETV as at 31 March 2016	Accrued CETV as at 31 March 2017
		£000	£000
Hugh Dunn*	Acting Executive Director of Resources, City of Edinburgh Council	755	1,251
Clare Scott*	Chief Executive Officer, Lothian Pension Fund	175	221
Bruce Miller	Chief Investment Officer, Lothian Pension Fund	185	267
Struan Fairbairn	Chief Risk Officer, Lothian Pension Fund	30	46
John Burns	Chief Finance Officer, Lothian Pension Fund	474	538
Esmond Hamilton	Financial Controller, Lothian Pension Fund	161	200

* Also disclosed in the financial statements of the City of Edinburgh Council.

Total compensation paid in relation to key management personnel employed by LPFE Limited during the period was as follows:

	31 March 2016	31 March 2017
	£000	£000
Short-term employee benefits	318	380
Post-employment benefits - employer pension contributions	65	78

Key management personnel employed by LPFE, had accrued pensions totalling £81,825 (1 April 2016: £68,004) and lump sums totalling £100,185 (1 April 2016: £68,004) at the end of the period.

Staff are either employed by City of Edinburgh Council or LPFE Limited, and their costs reimbursed by the Pension Funds. The Councillors, who are members of the Pensions Committee, are also remunerated by City of Edinburgh Council.

22 Contractual commitments

The Fund has commitments relating to outstanding call payments due on unquoted funds invested in private debt, timber and infrastructure. The amounts 'called' by these funds are irregular in both size and timing, taking place over a period of years from the date of each original commitment. The outstanding commitments at the year end are as follows:

	31 March 2016	31 March 2017
	£000	£000
Outstanding investment commitments	6,722	12,462
	6,722	12,462

Notes to the Financial Statements

23 Contingent assets and liabilities

At 31 March 2017 the Fund had entered into negotiations for an infrastructure co-investments in which it is exposed to the potential risk of investment abort costs. Lothian Buses Pension Fund's exposure to this is approximately £1.6k.

There were no contingent assets at year end.

24 Impairment losses

No impairment losses have been identified during the year.

Lothian Buses Pension Fund

Actuarial Statement for 2016/17

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The funding policy is set out in the Administering Authority's Funding Strategy Statement (FSS), dated 16 November 2015. In summary, the key funding principles are as follows:

- To ensure solvency of the Fund;
- To minimise the degree of short-term change in employer contribution rates;
- Reduce risk of the investment strategy over time;
- To ensure that sufficient cash is available to meet all liabilities as they fall due for payment

The FSS sets out how the Administering Authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 32 of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008 was as at 31 March 2014. This valuation revealed that the Fund's assets, which at 31 March 2014 were valued at £337 million, were sufficient to meet 117% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting surplus at the 2014 valuation was £48 million.

On the more prudent gilts basis, the Fund's assets as at 31 March 2014 were sufficient to meet 88% of the liabilities accrued to that date. The resulting deficit at the 2014 valuation, on the gilts basis, was £45 million.

The employer contributions for the period 1 April 2015 to 31 March 2018 were set in accordance with the Fund's funding policy as set out in its Funding Strategy Statement.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the valuation report dated 31 March 2014.

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth to retirement or expected earlier date of leaving pensionable membership.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market value.

Lothian Buses Pension Fund

Actuarial Statement for 2016/17

The key financial assumptions adopted for the 2014 valuation were as follows:

Financial assumptions	31 March 2014	
	% p.a.	% p.a.
	Nominal	Real
Discount rate	5.0%	2.3%
Pay increases*	5.0%	2.3%
Price inflation/Pension increases	2.7%	-

*2% p.a. for 2014/15 and 2015/16, reverting to 5.0% thereafter.

The key demographic assumption was the allowance made for longevity. The life expectancy assumptions are based on the Fund's VitaCurves with improvements in line with the CMI_2012 model, assuming the current rate of improvements has reached a peak and will converge to long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	20.4 years	22.6 years
Future Pensioners *	23.5 years	25.9 years

*Future pensioners are assumed to be at the 2014 valuation aged 45.

Copies of the 2014 valuation report and Funding Strategy Statement are available on request from The City of Edinburgh Council, the Administering Authority to the Fund.

Experience over the period since April 2014

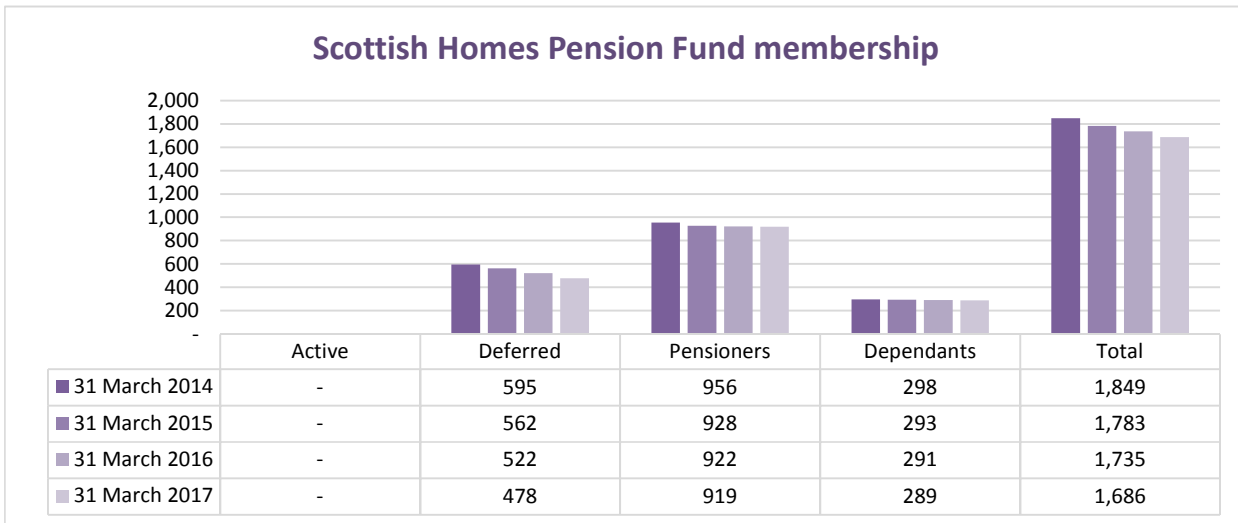
The Fund's experience has been worse than expected since the last formal valuation (excluding the effect of any membership movements and any potential changes to assumptions at the 2017 valuation). Real bond yields have fallen sharply which places a higher value on liabilities. The effect of this will have been partially offset by strong asset returns. The funding level is therefore likely to have worsened over the period.

The next actuarial valuation will be carried out as at 31 March 2017 with the results signed off within 12 months. The Funding Strategy Statement will also be reviewed at that time.

Richard Warden FFA
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
20 Waterloo Street
Glasgow
G2 6DB

28 April 2017

Scottish Homes Pension Fund



Investment strategy

The funding agreement with the Scottish Government and the investment strategy are designed to reduce investment risk as the Fund is closed to new members and the liabilities will mature over time. Both allow for acceleration in the sale of equities and property and purchase of bonds if the actual funding level improves to the target funding level. The 2014 Actuarial Valuation showed that the actual funding level (88.8%) was below the target funding level (91.5%).

Following the results of the 2014 Actuarial Valuation, the Pensions Committee approved a revised investment strategy for Scottish Homes Pension Fund in December of that year, with a reducing equity allocation, and corresponding increases in the bond allocation dependent on the funding level. The target funding levels from 2014 to 2026 are shown in the table below along with the corresponding target equity allocations.

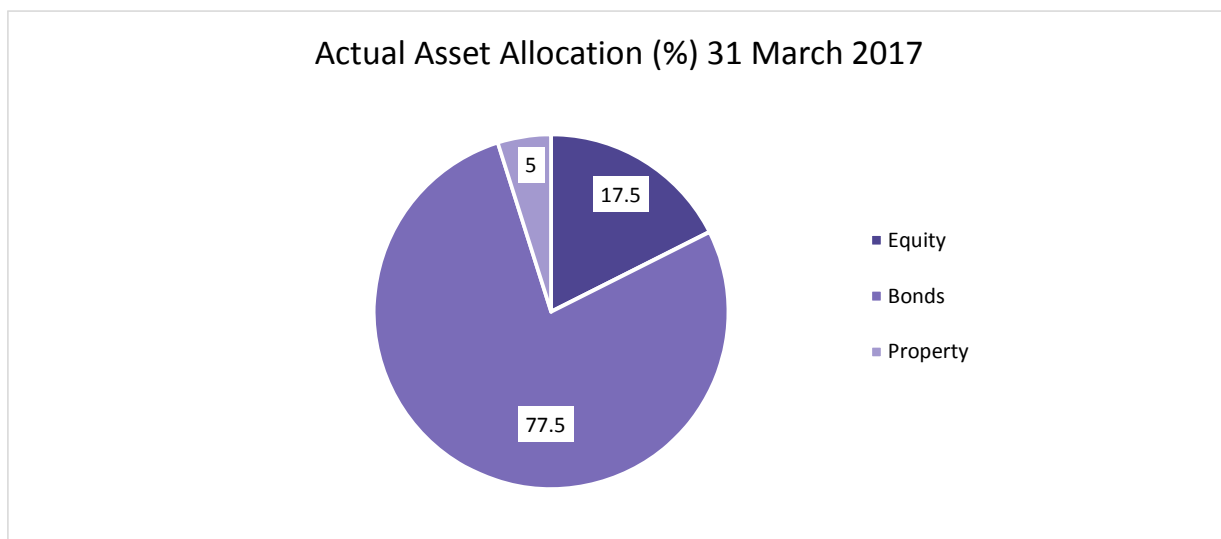
Year [1]	Target Funding Level	Target Equity Allocation
	%	%
2014	91.5	30
2017	93.0	25
2020	94.5	20
2023	95.5	15
2026	96.5	10

[1] The Scottish Government guarantee agreement sets out the increasing target funding levels every 3 years until 2044.

Over 2016/17, the actual funding level fluctuated above and below the target funding level reflecting movements in market interest rates and fund asset prices. Action was taken to vary the equity allocation between 30% and 17.5% over the year, consistent with the funding approach. The strategic asset allocation at the end of the 2016 and 2017 financial years are shown below.

	Strategic Allocation	Strategic Allocation
	31 March 2016	31 March 2017
	%	%
Equities	30.0	17.5
Bonds	65.0	77.5
Property	5.0	5.0
Cash	-	-
Total	100.0	100.0

During 2016/17, the equity allocation was reduced on four occasions from 30% to 17.5%. These changes were made to take advantage of movements in financial markets, which caused the funding level to trend higher over the course of the year. The actual allocations at 31 March 2017 are shown in the pie chart below.



Due to the requirement to divest on a regular basis, an analysis of a cash flow based strategy was undertaken which looked at alternative asset portfolios to demonstrate the effect on future cash flows for the Fund. As a result, the Fund implemented changes within the current funding approach to enhance income generation and to improve matching of cash flows from bond investments with the expected timing of pension payments. Management of the equity and bond portfolios was brought in-house.

These changes followed on from a review of the investment strategy during 2015/16 and further work undertaken in relation to the proposals to the Scottish Government to change and update its funding agreement. The Scottish Government has agreed to consider alternatives to the existing funding approach. The current bond-focused investment strategy provides income yield of less than 2%, and so the Fund is required to sell assets on a regular basis to pay pensions. The latest work concluded that a less prescriptive investment and funding strategy would allow a higher-yielding investment strategy and a more flexible approach to setting contributions. Further development of the alternative funding strategies will be taken forward in 2017/18 as part of the 2017 actuarial valuation.

Investment performance

The objectives of the Fund are:

- over long-term economic cycles (typically 5 years or more), the achievement of the same return as that generated by the strategic allocation;
- over shorter periods, the Fund should perform better than the strategic allocation if markets fall significantly.

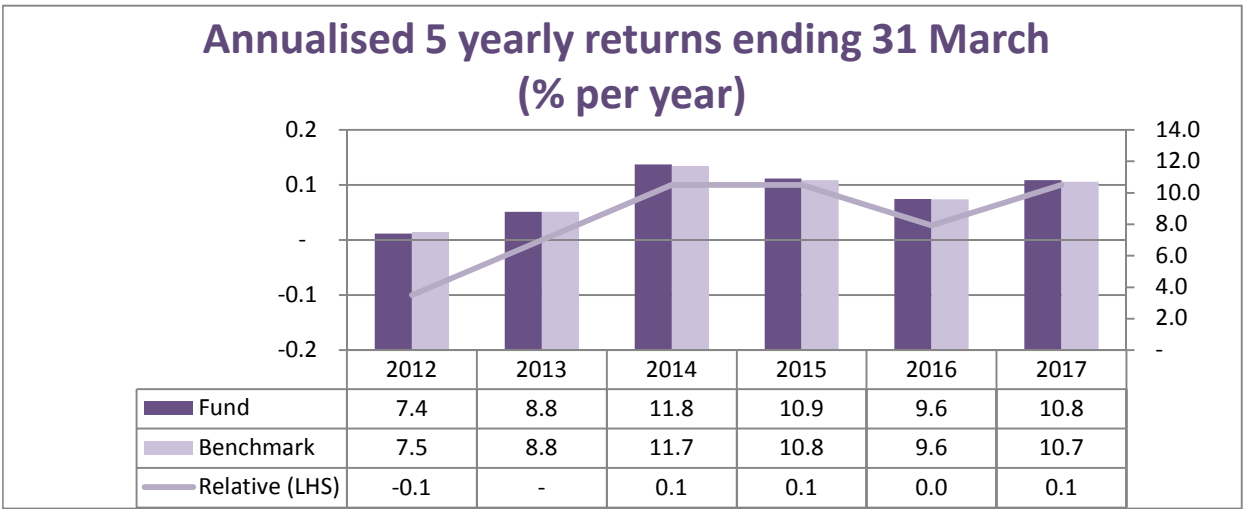
The Fund's annualised performance over the year and longer-term periods is shown in the table below. The Fund has performed broadly in line with its benchmark over all time periods.

Annualised returns to 31 March 2017 (% per year)	1 year	5 years	10 years
Scottish Homes Pension Fund	18.9	10.8	9.1
Benchmark	18.7	10.7	9.1
Actuarial Valuation Assumptions *	3.4	3.8	4.1
Retail Price Index (RPI)	3.1	2.3	2.8
Consumer Price Index (CPI)	2.3	1.4	2.3
National Average Earnings	2.4	1.9	2.0

* estimated

The absolute performance of Scottish Homes Pension Fund over the 12-month period was 18.9% and 5 year performance was 10.8% per annum. Over 2016/17, all asset classes generated healthy positive returns of 22.7%, 14.5%, and 6.2% from equities, bonds and property, respectively. While equities and bonds performed in line with their benchmarks, property outperformed during the

property, respectively. While equities and bonds performed in line with their benchmarks, property outperformed during the period. The Fund's risk has been marginally lower than that of the benchmark over the last year and 5 years. Since inception in July 2005, the Fund has returned +9.3% per annum, in line with its benchmark but well ahead of broad measures of inflation and national average earnings.



Scottish Homes Pension Fund

Fund Account for year ended 31 March 2017

This statement shows a summary of the income and expenditure that the Pension Fund has generated and consumed in delivering the Local Government Pension Scheme. Included is the income generated from the Scottish Government's contributions and investment income, as well as the cost of providing benefits and administration of the Fund.

2015/16			2016/17
£000		Note	£000
	Income		
675	Contributions from the Scottish Government	3	675
-	Transfers from other schemes		-
675			675
	Less: expenditure		
6,890	Pension payments including increases		6,789
472	Lump sum retirement payments		563
7	Lump sum death benefits		-
290	Transfers to other schemes	4	120
53	Administrative expenses	5b	68
7,712			7,540
(7,037)	Net withdrawals from dealing with members		(6,865)
	Returns on investments		
799	Investment income	6	877
1,962	Change in market value of investments	7, 10b	26,569
(169)	Investment management expenses	5c	(212)
2,592	Net returns on investments		27,234
(4,445)	Net increase/(decrease) in the Fund during the year		20,369
154,720	Net assets of the Fund at 1 April 2016		150,275
150,275	Net assets of the Fund at 31 March 2017	10	170,644

Scottish Homes Pension Fund

Net Assets Statement as at 31 March 2017

This statement provides a breakdown of type and value of all net assets at the year end.

31 March 2016 £000	Note	31 March 2017 £000
Investment Assets		
59,749	Bonds	127,970
-	Equities - UK	4,450
-	- Overseas	23,771
88,661	<u>Pooled investment vehicles</u>	7,998
7,788	- UK managed fund - Property	7,998
44,928	- UK managed fund - Equity	-
35,945	- UK managed fund - Gilts	-
11	Cash Deposits	3,602
177	Other investment assets	459
148,598		168,250
Investment Liabilities		
-	Other investment assets	-
-		-
148,598	Net investment assets	168,250
	8	
Current assets		
95	The City of Edinburgh Council	146
1,610	Cash balances	2,232
22	Debtors	31
1,727		2,409
Current liabilities		
(50)	Creditors	(15)
(50)		(15)
1,677	Net current assets	2,394
150,275	Net assets of the Fund at 31 March 2017	170,644
	10	

The unaudited accounts were issued on 28 June 2017 and the audited accounts were authorised for issue on 27 September 2017.

JOHN BURNS FCMA CGMA

Chief Finance Officer, Lothian Pension Fund

27 September 2017

Note to the net asset statement

The financial statements summarise the transactions of the Fund during the year and its net assets at the year end. They do not take account of the obligations to pay pensions and benefits which fall due after the end of the year. The actuarial position of the Fund, which does take account of such obligations, is discussed in the Actuarial Valuation section of this report and these financial statements should be read in conjunction with that information. In addition, as required by IAS26, the Actuarial Present Value of Promised Retirement Benefits is disclosed in the notes to these financial statements.

Notes to the Financial Statements

1 Statement of Accounting Policies

The statement of accounting policies for all Funds can be found on page 112.

2 Events after the Reporting Date

There have been no events since 31 March 2017, and up to the date when these Financial Statements were authorised, that require any adjustments to these Financial Statements.

3 Contributions from the Scottish Government

	2015/16 £000	2016/17 £000
Deficit funding	575	575
Administration expenses	100	100
	675	675

The Scottish Homes Pension Fund is a single employer pension fund for former employees of Scottish Homes. The Scottish Homes Pension Fund was set up under (Scottish) Statutory Instrument 315/2005, when Scottish Homes became Communities Scotland, an agency of the Scottish Government.

Following the actuarial valuation at 31 March 2014, deficit funding of £575,000 per year is being paid by the Scottish Government over the period April 2015 to March 2018. In addition, the Scottish Government agreed to pay £100,000 every year towards the cost of ongoing administration.

Where the Scottish Government makes certain decisions which result in additional benefits being paid out to a member, or benefits being paid early, this results in a "strain" on the Fund. The resulting pension strain costs are calculated and recharged in full.

The Fund consists of only deferred and pensioner members, hence no employee contributions were paid during the year.

4 Transfers out to other pension schemes

	2015/16 £000	2016/17 £000
Group transfers	-	-
Individual transfers	290	120
	290	120

5a Total Management expenses

	2015/16 £000	2016/17 £000
Administrative costs	38	38
Investment management expenses	149	149
Oversight and governance costs	35	93
	222	280

This analysis of costs for the Scottish Homes Pension Fund has been prepared in accordance with CIPFA guidance. The analysis looks at the combined administration and investment management expenses in note 5b and c and splits out the costs to include a third heading covering oversight and governance expenditure.

Notes to the Financial Statements

5b Administrative expenses

	2015/16 £000	2016/17 £000
Employee Costs	23	26
The City of Edinburgh Council - other support costs	3	3
System costs	7	7
Actuarial fees	12	24
External audit fees	1	1
Printing and postage	2	2
Depreciation	1	1
Office costs	2	3
Sundry costs less sundry income	2	1
	53	68

The Investment and Pensions Service of the Council is responsible for administering the three Pension Funds. The Service receives an allocation of the overheads of the Council. In turn the Service apportioned administration and investment costs to the three pension funds. Costs directly attributable to a specific fund are charged to the relevant Fund, costs that are common to all three funds are apportioned on a defined basis.

5c Investment management expenses

	2015/16 £000	2016/17 £000
External management fees - invoiced	52	50
External management fees - deducted from capital (direct)	52	55
External management fees - deducted from capital (indirect)	-	-
Transaction costs	1	40
Employee costs	25	29
Custody fees	17	14
Engagement and voting fees	2	2
Performance measurement fees	5	5
Consultancy fees	2	2
System costs	5	6
Legal fees	-	3
The City of Edinburgh Council - other support costs	3	3
Office costs	2	2
Sundry costs less sundry income	3	1
	169	212

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions or in the proceeds of investment sales (see note 7a - Reconciliation of movements in investments).

The Fund has not incurred any performance-related investment management fees in 2016/17 or 2015/16.

Notes to the Financial Statements

6 Investment income	2015/16	2016/17
	£000	£000
Income from fixed interest securities	512	536
Dividends from Equities	-	62
Income from pooled investments - property	277	265
Interest on cash deposits and sundries	10	16
	799	879
Irrecoverable withholding tax	-	(2)
	799	877

7 Reconciliation of movement in investments	Market value at 31 March 2016	Purchases at cost	Sales & proceeds	Change in market value	Market value at 31 March 2017
	£000	£000	£000	£000	£000
Bonds	59,749	97,017	(37,319)	8,523	127,970
Equities	-	28,285	-	(64)	28,221
Pooled investment vehicles	88,661	9,569	(108,262)	18,030	7,998
	148,410	134,871	(145,581)	26,489	164,189
Other financial assets / (liabilities)					
Cash deposits	11			80	3,602
Dividend due etc	177			-	459
	188			80	4,061
Net financial assets	148,598			26,569	168,250

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.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions and in the proceeds from sales and are therefore included in the tables above.

	Market value at 31 March 2015	Purchases at cost	Sales & proceeds	Change in market value	Market value at 31 March 2016
	£000	£000	£000	£000	£000
Bonds	54,147	5,698	-	(96)	59,749
Pooled investment vehicles	97,503	13,987	(24,887)	2,058	88,661
	151,650	19,685	(24,887)	1,962	148,410
Other financial assets / (liabilities)					
Cash deposits	244			-	11
Dividend due etc	173			-	177
	417			-	188
Net financial assets	152,067			1,962	148,598

Notes to the Financial Statements

8 Investment managers and mandates

Manager	Mandate	Market value at 31 March 2016 £000	% of total 31 March 2016 %	Market value at 31 March 2017 £000	% of total 31 March 2017 %
State Street	UK equities	10,060	6.8	-	-
Total UK equities		10,060	6.8	-	-
State Street	N American equities	13,752	9.2	-	-
State Street	European (ex UK) equities	8,994	6.1	-	-
State Street	Pacific (ex Japan) equities	3,617	2.4	-	-
State Street	Japanese equities	4,834	3.3	-	-
State Street	Emerging markets equities	3,672	2.5	-	-
Total regional overseas equities		34,869	23.5	-	-
In-house	High Div Equity	-	-	29,037	17.3
Total global equities		-	-	29,037	17.3
In-house	UK Index linked gilts	59,937	40.3	128,477	76.4
State Street	UK Fixed interest gilts	19,777	13.3	-	-
State Street	UK Index linked gilts	16,167	10.9	-	-
Total fixed interest and inflation linked bonds		95,881	64.5	128,477	76.4
Schroders	Property	7,788	5.2	7,998	4.8
Total property		7,788	5.2	7,998	4.8
In-house	Cash	-	-	2,738	1.5
Total cash		-	-	2,738	1.5
Net financial assets		148,598	100.0	168,250	100.0

Notes to the Financial Statements

9a Investments representing more than 5% of the net assets of the Fund

	Market value at 31 March 2016 £000	% of total 31 March 2016 %	Market value at 31 March 2017 £000	% of total 31 March 2017 %
UK Gov 1.25% Index Linked 22/11/27	-	-	11,905	7.0
UK Gov 4.125% Index Linked 22/11/17	-	-	10,955	6.4
UK Gov 2.5% Index Linked 17/07/24	-	-	10,637	6.2
UK Gov 2.5% Index Linked 16/04/20	-	-	10,538	6.2
UK Gov 1.875% Index Linked 22/11/22	-	-	10,517	6.2
UK Gov 1.125% Index Linked 22/11/27	26,386	17.4	9,003	5.3
State Street UK Index Linked Gilts Over 15 Years	16,167	10.8	-	-
State Street UK Conventional Gilts Over 15 Years	19,777	13.2	-	-
UK Gov 1.25% Index Linked 22/11/32	16,380	10.9	7,614	4.5
State Street MPF North America Equity Index	13,752	9.2	-	-
UK Gov 1.125% Index Linked 22/11/37	11,321	7.5	7,800	4.6
State Street MPF UK Equity Index	10,060	6.7	-	-
State Street MPF Europe ex-UK Equity Index	8,994	6.0	-	-
Schroders UK Real Estate Income Units	7,788	5.2	7,998	4.7

9b Investments representing more than 5% of asset class

	Market value at 31 March 2016 £000	% of total 31 March 2016 %	Market value at 31 March 2017 £000	% of total 31 March 2017 %
Bonds				
UK Gov 1.25% Index Linked 22/11/27	-	-	11,905	9.3
UK Gov 4.125% Index Linked 22/11/17	-	-	10,955	8.6
UK Gov 2.5% Index Linked 17/07/24	-	-	10,637	8.3
UK Gov 2.5% Index Linked 16/04/20	-	-	10,538	8.2
UK Gov 1.875% Index Linked 22/11/22	-	-	10,517	8.2
UK Gov 1.125% Index Linked 22/11/27	26,386	44.2	9,003	7.0
UK Gov 1.125% Index Linked 22/11/37	11,321	18.9	7,800	6.1
UK Gov 1.25% Index Linked 22/11/32	16,380	27.4	7,614	5.9
UK Gov 0.75% Index Linked 22/03/34	3,472	5.8	3,315	2.6
Pooled funds				
Schroders UK Real Estate Income Units	7,788	8.8	7,998	100.0
State Street UK Index Linked Gilts Over 15 Years	16,167	15.5	-	-
State Street UK Conventional Gilts Over 15 Years	19,777	22.3	-	-
State Street MPF North America Equity Index	13,752	15.5	-	-
State Street MPF UK Equity Index	10,060	11.3	-	-
State Street MPF Europe ex-UK Equity Index	8,994	10.1	-	-
State Street MPF Japan	4,834	5.5	-	-

Notes to the Financial Statements

10 Financial Instruments

10a Classification of financial instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the fair value amounts of financial assets and liabilities by category and net assets statement heading. No financial assets were reclassified during the accounting period.

All financial instruments are marked to market (at fair value) in the Fund's accounting records hence there is no difference between the carrying value and fair value.

	31 March 2016			31 March 2017		
	Designated as fair value through fund account £000	Loans and receivables £000	Financial liabilities at amortised cost £000	Designated as fair value through fund account £000	Loans and receivables £000	Financial liabilities at amortised cost £000
Financial assets						
Investment assets						
Bonds	59,749	-	-	127,970	-	-
Equities	-	-	-	28,221	-	-
Pooled investments	88,661	-	-	7,998	-	-
Cash	-	11	-	-	3,602	-
Other balances	-	177	-	-	459	-
	148,410	188	-	164,189	4,061	-
Other assets						
City of Edinburgh Council	-	95	-	-	146	-
Cash	-	1,610	-	-	2,232	-
Debtors	-	22	-	-	31	-
	-	1,727	-	-	2,409	-
Assets total	148,410	1,915	-	164,189	6,470	-
Financial liabilities						
Other liabilities						
Creditors	-	-	(50)	-	-	(15)
Liabilities total	-	-	(50)	-	-	(15)
Total net assets	148,410	1,915	(50)	164,189	6,470	(15)

Total net financial instruments	150,275		170,644
--	---------	--	---------

10b Net gains and losses on financial instruments

	2015/16 £000	2016/17 £000
Designated as fair value through fund account	1,962	26,569
Loans and receivables	-	-
Financial liabilities at amortised cost	-	-
Total	1,962	26,569

Notes to the Financial Statements

10c Valuation of financial instruments carried at fair value

The valuation of financial instruments has been classified into three levels, according to the quality and reliability of information used to determine fair values.

Level 1

Financial instruments at Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities and unit trusts.

Quoted investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Level 2

Financial instruments at Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3

Financial instruments at Level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data. Such instruments would include unquoted equity investments, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investments in unquoted private equity, infrastructure, timber and real estate are based on valuations provided by the general partners to the funds in which the Fund has invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of International Financial Reporting Standards (IFRS). The valuations are typically undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

	31 March 2017			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Investment assets				
Designated as fair value through fund account	36,219	127,970	-	164,189
Loans and receivables	4,061	-	-	4,061
Total investment assets	40,280	127,970	-	168,250
Investment liabilities				
Designated as fair value through fund account	-	-	-	-
Total investment liabilities	-	-	-	-
Net investment assets	40,280	127,970	-	168,250

Notes to the Financial Statements

10c Valuation of financial instruments carried at fair value (cont)

	31 March 2016			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial assets				
Designated as fair value through fund account	88,661	59,749	-	148,410
Loans and receivables	188	-	-	188
Total financial assets	88,849	59,749	-	148,598
Financial liabilities				
Designated as fair value through fund account	-	-	-	-
Total financial liabilities	-	-	-	-
Net financial assets	88,849	59,749	-	148,598

11 Nature and extent of risk arising from financial instruments

Risk and risk management

The Fund's primary aim is to ensure that all members and their dependants receive their benefits when they become payable. The investment strategy aims to maximise the returns from investments within reasonable risk parameters and hence minimise the long-term cost to employer. The Fund achieves this by investing in a diverse range of assets to reduce risk to an acceptable level. In addition, the Fund ensures that sufficient cash is available to meet all liabilities when they are due to be paid

Responsibility for the Fund's overall investment strategy rests with the Pensions Committee. The Investment Strategy Panel and the internal investment team monitor investment risks on a regular basis. Investment risk management tools are used to identify and analyse risks faced by the Fund's investments.

Types of investment risk

There are various ways of considering investment risks for pension funds. For the purposes of this note, market risk is the potential for an investor to experience losses from falls in the prices of investments. All financial instruments, including cash deposits, present a risk of loss of capital and risks vary depending on different asset classes.

Market risk also changes over time as economic conditions and investor sentiment change. The Fund considers overall fluctuations in prices arising from a variety of sources: market risk, foreign exchange risk, interest rate risk, credit risk, etc. The different risks may, to some extent, offset each other. The overall market risk of the Fund depends on the actual mix of assets and encompasses all the different elements of risk.

The Fund manages these risks in a number of ways:

- assessing and establishing acceptable levels of market risk when setting overall investment strategy. Importantly, risk is considered relative to the liabilities of the Fund
- diversification of investments in terms of type of asset, investment styles, investment managers, geographical and industry sectors as well as individual securities
- taking stewardship responsibilities seriously and pursuing constructive engagement with the companies in which we invest
- monitoring market risk and market conditions to ensure risk remains within tolerable levels.

Notes to the Financial Statements

11 Nature and extent of risk arising from financial instruments (cont)

Sensitivity analysis

Asset prices have a tendency to fluctuate. The degree of such fluctuation is known as “volatility” and it differs by asset class. The table sets out the long-term volatility assumptions used by the Fund’s investment adviser KPMG:

Asset type	Potential price movement (+ or -)
Equities - Developed Markets	20.5%
Index-Linked Gilts	10.9%
Property	13.0%
Cash	1.1%

Volatility is the standard deviation of annual returns. Broadly speaking, in two years out of three, the asset’s change in value (which could be a gain or a loss) is expected to be lower than the volatility figure, but in one year out of three, the change in value is expected to be higher than the volatility figure.

Asset classes don’t always move in line with each other. The extent to which assets move together is known as their "correlation". A lower correlation means that there is less risk of assets losing value at the same time. The overall Fund benefits from "diversification" because it invests in numerous different asset classes, which don’t all move in line with each other. Consequently, the aggregate risk at the Fund level is less than the total risk from all the individual assets in which the Fund invests.

The following table shows the risks at the asset class level and the overall Fund level.

	Value at 31 March 2017 £000	% of fund %	Potential Change +/- %	Value on increase £000	Value on decrease £000
Equities - Developed Markets	29,037	17.3	20.5	34,990	23,084
Index-Linked Gilts	128,476	76.4	10.9	142,418	114,534
Property	7,998	4.8	13.0	9,038	6,958
Cash	2,739	1.5	1.1	2,769	2,709
Total [1]	168,250	100.0	12.5	189,214	147,286
Total [2]			9.5	184,192	152,308
Total [3]			8.6	182,767	n/a

[1] No allowance for correlations between assets

[2] Including allowance for correlations between assets

[3] Including allowance for correlation between assets and liabilities.

The value on increase/decrease columns illustrate the monetary effect of the percentage change in the volatility column. The actual annual change in value is expected to be lower than this in two years out of three, but higher in one year out of three.

It can be seen that the risk to the overall Fund assets [2] is lower than the total of the risks to the individual assets [1].

Notes to the Financial Statements

11 Nature and extent of risk arising from financial instruments (cont)

However, because the purpose of a pension scheme is to make payments to scheme beneficiaries, the true risk of a pension scheme is not measured in absolute terms, but relative to its liabilities [3]. The risk is lower than the absolute asset risk, due to the impact of correlation with the discount rate used to value the liabilities.

This risk analysis incorporates volatility from market, interest rate, foreign exchange, credit, and all other sources of risk, and, importantly, makes allowance for how these risks may offset each other.

Credit risk

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit risk in their pricing and consequently the risk of loss is implicitly provided for in the value of the Fund's assets and liabilities (as outlined in Market Risk above).

In essence, the Fund's entire investment portfolio is exposed to some sort of credit risk. However, through the selection of counterparties, brokers and financial institutions the Fund reduces the credit risk that may occur through the failure to settle a transaction in a timely manner.

Cash deposits are the major areas of credit exposure where credit risk is not reflected in market prices.

Cash deposits

At 31 March 2017, cash deposits represented £5.8m, 3.4% of total net assets. This was held with the following institutions:

	Moody's Credit Rating at 31 March 2017	Balances at 31 March 2016 £000	Balances at 31 March 2017 £000
Held for investment purposes			
Northern Trust Company - cash deposits	A2	11	3,602
Held for other purposes			
The City of Edinburgh Council - treasury management	See below	1,610	2,232
Total cash		1,621	5,834

The majority of Sterling cash deposits of the Fund are managed along with those of the administering authority (the City of Edinburgh Council) and other related organisations which are pooled for investment purposes as a treasury cash fund. Management of the cash fund is on a low risk basis, with security of the investments the key consideration. The Council has in place counterparty criteria.

The Council has in place institutional restrictions on investments and counterparty criteria. These include -

- UK Government and other UK local Authorities with no limit, other public bodies up to £20 million per organisation.
- Money market funds (MMFs) no more than £30 million or 15% with any one Fund.
- Financial Institutions: Banks and Building Societies with multiple criteria based on a range of short and long term credit ratings, as well as any security provided, from maximum of £60 million / 20% of assets under management (AUM) for institutions with the highest criteria to £10 million / 5% of AUM for institutions with the lowest acceptable criteria.

Notes to the Financial Statements

11 Nature and extent of risk arising from financial instruments (cont)

	Moody's Credit Rating at 31 March 2017	Balances at 31 March 2016 £000	Balances at 31 March 2017 £000
Money market funds			
Deutsche Bank AG, London	Aaa-mf	215	12
Goldman Sachs	Aaa-mf	2	-
Bank call accounts			
Bank of Scotland	A1	105	223
Royal Bank of Scotland	A3	17	3
Santander UK	Aa3	-	1
Barclays Bank	A1	109	-
Svenska Handelsbanken	Aa2	111	-
UK Pseudo-Sovereign risk instruments			
Other Local Authorities [1]	Aa1	730	1,993
UK Government Treasury Bills	Aa1	321	-
		1,610	2,232

[1] Very few Local Authorities have their own credit rating but they are generally assumed to have a pseudo-sovereign credit rating (which in the UK at 31 March 2017 was 'Aa1').

No breaches of the Council's counterparty criteria occurred during the reporting period and the Fund does not expect any losses from non-performance by any of its counterparties in relation to deposits.

Refinancing risk

Refinancing risk is the risk that the Fund will be bound to replenish a significant proportion of its pension fund financial instruments at a time of unfavourable interest rates. The Fund is not bound by any obligation to replenish its investments and hence is not exposed to refinancing risk.

Liquidity risk

Liquidity risk reflects the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund therefore ensures that there is adequate cash and liquid resources to meet its commitments. Cash flow projections are prepared on a regular basis to understand and manage the timing of the Fund's cash flows.

All of the Fund's investments could be converted to cash within three months in a normal trading environment.

12 Actuarial statement

The Scheme Actuary has provided a statement describing the funding arrangements of the Fund. This can be found at the end of this section.

13 Actuarial present value of promised retirement benefits

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standard 19 (IAS19) assumptions, is estimated to be £145m (2016 £130m). This figure is used for statutory accounting purposes by Scottish Homes Pension Fund and complies with the requirements of IAS26. The assumptions underlying the figure match those adopted for the Administering Authority's FRS17/IAS19 reports at each year end.

Notes to the Financial Statements

13 Actuarial present value of promised retirement benefits (cont)

The figure is only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

	31 March 2016 % p.a.	31 March 2017 % p.a.
Inflation/pensions increase rate	2.2%	2.4%
Discount rate	3.5%	2.6%

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2012 model, assuming that the current rate of improvements has reached a peak and will converge to a long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies, in years, at age 65 are summarised below:

	31 March 2016		31 March 2017	
	Males	Females	Males	Females
Current pensioners	24.5 years	25.4 years	24.5 years	25.4 years
Future pensioners (assumed to be currently 45)	26.8 years	28.6 years	26.8 years	28.6 years

Commutation assumption

An allowance is included for future retirements to elect to take 50% of the maximum additional tax-free cash up to HMRC limits for pre-April 2009 service and 75% of the maximum tax-free cash for post-April 2009 service.

14 Debtors

	31 March 2016 £000	31 March 2017 £000
Sundry debtors	22	31
	22	31

Analysis of debtors

	31 March 2016 £000	31 March 2017 £000
Administering Authority	1	1
Other entities and individuals	21	30
	22	31

15 Creditors

	31 March 2016 £000	31 March 2017 £000
Benefits payable	8	-
Miscellaneous creditors and accrued expenses	42	15
	50	15

Analysis of creditors

	31 March 2016 £000	31 March 2017 £000
Other entities and individuals	50	15
	50	15

Notes to the Financial Statements

16 Related party transactions

The City of Edinburgh Council

The Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund are administered by the City of Edinburgh Council. Consequently there is a strong relationship between the Council and the Pension Funds.

The Investment and Pensions Service of the Council is responsible for administering the three Pension Funds. The Service receives an allocation of the overheads of the Council, based on the amount of central services consumed. In turn, the Service allocates its costs to the three Pension Funds. Costs directly attributable to a specific Fund are charged to the relevant Fund; costs that are common to all three Funds are allocated on a defined basis.

Transactions between the Council and the Fund are managed via a holding account. Each month the Fund pays a cash sum to the Council leaving a working balance in the account.

	31 March 2016 £000	31 March 2017 £000
Year end balance of holding account	95	146
	95	146

Part of the Fund's cash holdings are invested on the money markets by the treasury management operations of the Council, through a service level agreement. During the year to 31 March 2017, the fund had an average investment balance of £2.1m (2016 £2.2m). Interest earned was £8k (2016 £10.5k).

	31 March 2016 £000	31 March 2017 £000
Year end balance on treasury management account		
Held for investment purposes	-	-
Held for other purposes	1,610	2,232
	1,610	2,232

Scheme Guarantor

As the scheme guarantor (by definition) a related party to the scheme. The Scottish Government's contributions to the Fund can be found in note 3 (page 96) of the notes to the Financial Statements.

Governance

As at 31 March 2017, all members of the Pensions Committee, with the exception of Councillor Bill Cook and Richard Lamont, and all members of the Pensions Board, were members of the Lothian Pension Fund or Lothian Buses Pension Fund, with one member of the Pensions Board in receipt of pension benefits from Lothian Pension Fund.

Each member of the Pensions Committee and Pensions Board is required to declare any financial and non-financial interests they have in the items of business for consideration at each meeting, identifying the relevant agenda item and the nature of their interest.

With effect from 1 May 2015, all the employees listed below, with the exception of the Executive Director of Resources, were employed by LPFE Limited. These employees and their financial relationship with the Fund (expressed as cash-equivalent transfer values or CETV) are set out below:

Notes to the Financial Statements

16 Related party transactions (cont)

Name	Position held	Accrued CETV as at 31 March 2016	Accrued CETV as at 31 March 2017
		£000	£000
Hugh Dunn*	Acting Executive Director of Resources, City of Edinburgh Council	755	1,251
Clare Scott*	Chief Executive, Lothian Pension Fund	175	221
Bruce Miller	Chief Investment Officer, Lothian Pension Fund	185	267
Struan Fairbairn	Chief Risk Officer, Lothian Pension Fund	30	46
John Burns	Chief Finance Officer, Lothian Pension Fund	474	538
Esmond Hamilton	Financial Controller, Lothian Pension Fund	161	200

* Also disclosed in the financial statements of the City of Edinburgh Council.

Total compensation paid in relation to key management personnel employed by LPFE Limited during the period was as follows:

	31 March 2016	31 March 2017
	£000	£000
Short-term employee benefits	318	380
Post-employment benefits - employer pension contributions	65	78

Key management personnel employed by LPFE, had accrued pensions totalling £81,825 (1 April 2016: £68,004) and lump sums totalling £100,185 (1 April 2016: £68,004) at the end of the period.

Staff are either employed by City of Edinburgh Council or LPFE Limited, and their costs reimbursed by the Pension Funds. The Councillors, who are members of the Pensions Committee are also remunerated by City of Edinburgh Council.

17 Contingent assets/liabilities and contractual commitments

There were no contingent liabilities or contractual commitments at the year end.

18 Impairment losses

No impairment losses have been identified during the year.

Scottish Homes Pension Fund

Actuarial Statement for 2016/17

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The administering authority's Funding Strategy Statement, dated 16 November 2015, states that a bespoke funding strategy has been adopted for the Fund.

The strategy aims for the Fund to be 100% solvent by 2044 using a discount rate based on government bonds. It includes target funding levels at each actuarial valuation. Contributions from the Scottish Government are determined by reference to the target funding levels. The deficit recovery period is 8 years.

The Funding strategy is designed to reduce investment risk as the Fund is closed to new members and the liabilities will mature over the time, with a reducing allocation to equities over time reflecting the requirements of the Scottish Government to lock away any surpluses that may occur over time by accelerating the transfer into bonds.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 32 of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008 was as at 31 March 2014. This valuation revealed that the Fund's assets, which at 31 March 2014 were valued at £136 million, were sufficient to meet 89% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2014 valuation was £17 million.

The Guarantor's contributions for the period 1 April 2015 to 31 March 2018 were set in accordance with the Fund's funding policy as set out in its Financial Strategy Statement.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the valuation report dated 4 December 2014.

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund's assets at their market value.

The key financial assumptions adopted for the 2014 valuation were as follows:

Assumption	Description
Price Inflation (CPI) (deferreds and pensioners)	Bank of England implied (RPI) curve less 0.8% p.a.
Discount rate (deferreds and pensioners)	Bank of England nominal yield curve

Scottish Homes Pension Fund

Actuarial Statement for 2016/17

The key demographic assumption was the allowance made for longevity. The life expectancy assumptions are based on the Fund's VitaCurves with improvements in line with the CMI_2012 model, assuming the current rate of improvements has reached a peak and will converge to long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	24.5 years	25.4 years
Future Pensioners *	26.8 years	28.6 years

*Future pensioners are assumed to be aged 45 at the 2014 valuation

Copies of the 2014 valuation report and Funding Strategy Statement are available on request from The City of Edinburgh Council, the Administering Authority to the Fund.

Experience over the period since April 2014

The administering authority monitors the funding position on a regular basis as part of its risk management programme. The funding level at 31 March 2017 is estimated to be 96%, an increase of 7% since the formal funding valuation at 31 March 2014.

The next actuarial valuation will be carried out as at 31 March 2017 with the results signed off within 12 months. The Funding Strategy Statement will also be reviewed at that time.

Richard Warden FFA
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
20 Waterloo Street
Glasgow
G2 6DB

28 April 2017

Statement of Accounting Policies and General Notes

1 Basis of preparation

The Financial Statements have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

The Financial Statements summarise the transactions of the Funds for the 2016/17 financial year and report on the net assets available to pay pension benefits as at 31 March 2017. The Financial Statements do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present values of promised retirement benefits, valued on an International Accounting Standard (IAS) 19 basis, are disclosed in the Notes to the Financial Statements.

2 Summary of significant accounting policies

General

a) Basis of consolidation

Commencing with the year ended 31 March 2016, Consolidated Financial Statements have been prepared for Lothian Pension Fund. The Financial Statements of Lothian Buses Pension Fund and Scottish Homes Pension Fund continue to be prepared on a single entity basis.

The Consolidated Financial Statements for Lothian Pension Fund are prepared by combining the Financial Statements of the Fund (the parent entity) and its controlled entities (LPFE Limited and LPFI Limited) as defined in accounting standard IAS27 - Consolidated and Separate Financial Statements. Consistent accounting policies are employed in the preparation and presentation of the Consolidated Financial Statements. All inter-entity balances and transactions between entities, including any unrealised profits or losses, have been eliminated on consolidation.

As LPFE Limited commenced trading on 1 May 2015, the prior year comparative figures consist only of the results of Lothian Pension Fund. Further details of the consolidation are provided in the Notes to the Financial Statements of Lothian Pension Fund.

LPFE Limited and LPFI Limited are wholly owned by the City of Edinburgh Council in its capacity as administering authority for the Local Government Pension Scheme in the Lothian area. The purpose of LPFE Limited is to provide staff services in respect of investment and general management of the Funds. LPFI Limited's purpose is to provide FCA regulated services to the Funds and other Local Government Pension Scheme funds in Scotland and Northern Ireland. It is considered appropriate to consolidate the Financial Statements of the two companies with those of Lothian Pension Fund.

Fund account - revenue recognition

b) Contribution income

Normal contributions, both from the members and from employers, are accounted for on an accruals basis at the rate certified by the Scheme Actuary in the payroll period to which they relate.

Similarly, employer deficit funding contributions are accounted for on the due date on which they are payable as certified by the Scheme Actuary.

Employers' pensions strain contributions are accounted for in the period in which the liability arises. Any amount due but unpaid will be classed as a current financial asset. Amounts not due until future years are classed as long-term financial assets.

c) Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Funds during the financial year and are calculated in accordance with the Local Government Pension Scheme Regulations.

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

Transfers in from members wishing to use the proceeds of their additional voluntary contributions to purchase scheme benefits are accounted for on a receipts basis and are included in transfers in.

Bulk (group) transfers are accounted for on an accruals basis in accordance with the terms of the transfer agreement.

d) Investment income

i) Interest income

Interest income is recognised in the Funds accounts as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination. Income includes the amortisation of any discount or premium, transaction costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

ii) Dividend income

Dividend income is recognised on the date the shares are quoted ex-dividend. Any amount not received by the end of the reporting period is disclosed in the Net Assets Statement as a current financial asset.

iii) Distributions from pooled funds

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the Net Assets Statement as a current financial asset.

iv) Income from unquoted private equity and infrastructure investments

Income from the above sources is recognised when it is notified by the manager. Distributions are split into capital and income elements with the latter being included under investment income in the Fund Account.

v) Property related income

Property-related income consists primarily of rental income. Rental income from operating leases on properties owned by Lothian Pension Fund is recognised on a straight-line basis over the term of the lease. Any lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

Rental income is reported gross with the operational costs of the properties included in investment management expenses.

Contingent rents based on the future amount of a factor that changes other than with the passage of time, such as turnover rents, are only recognised when contractually due.

vi) Movement in the net market value of investments

Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during the year.

Fund Account - expense items

e) Benefits payable

Pensions and lump sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the Net Assets Statement as current liabilities.

f) Taxation

i) Pension Funds

The Local Government Pension Scheme is a registered public service scheme under section 1(1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax is accounted for as a fund expense as it arises.

ii) Controlled entities - LPFE Limited and LPFI Limited

The Companies are mutual traders and are therefore not liable to corporation tax on any surpluses generated from services provided in respect of the Funds. The tax charges for the period are based on any profit for the period from non-mutual trade, adjusted for any non-assessable or disallowed items. They are calculated using tax rates that have been enacted or are substantively enacted by the period end date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Financial Statements. No deferred tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

g) Administrative expenses

All administrative expenses are accounted for on an accruals basis. The Investment and Pensions Division of the Council is responsible for administering the three Funds. The Division's costs include charges from LPFE Limited and LPFI Limited for services rendered. The Division receives an allocation of the overheads of the Council, this is based on the amount of central services consumed. In turn, the Division allocates its costs to the three Funds.

Costs directly attributable to a specific fund are charged to the relevant Fund. Investment management costs that are common to all three Funds are allocated in proportion to the value of the Funds as at the end of the year. Other administration costs are allocated in proportion to the number of members in each of the Funds at the end of the year.

h) Investment management expenses

All investment management expenses are accounted for on an accruals basis.

Fees of the external investment managers and custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments change. For some investment managers, an element of their fee is performance related. The amount of any performance related fees paid is disclosed in the note to the accounts on investment management expenses provided for each Fund.

The cost of administering the Local Government Pension Scheme in the UK has come under increasing scrutiny in recent years. As a result, it has been decided to recognise investment management costs that are deducted from the value of an investment and recognised this as a cost in the Fund Account rather than as a reduction in the change in market value of investments. Investment transaction costs that are added to an investment purchase price or deducted from the proceeds of a sale are also recognised as a cost in the Fund Account rather than as a reduction in the change in market value of investments.

h) Investment management expenses (cont'd)

In June 2016, CIPFA revised and updated its guidance "Accounting for Local Government Pension Scheme Management Costs". Whilst the underlying principle of transparency of investment costs remains unchanged, there has been a degree of relaxation to full cost disclosure. Specifically, for complex "fund of funds" structures, the new guidance states that "Investment costs incurred by a separate legal entity, or in respect of investment decisions over which the pension fund has no control, should not be included in the (Pension) Fund Account.....If pension funds wish to provide information about the total cost of "fund of fund" investments, this should be included as part of the Investments section in the Annual Report". The impact of this is that investment management costs deducted from any underlying fund in a "fund of funds" investment would not be included in the costs disclosed in the Fund Account. As this would significantly under-report investment management costs the decision has been made not to adopt this element of the CIPFA guidance. However, this type of cost is separately identified as "external management fees - deducted from capital (indirect)" in the notes on investment management expenses.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are not treated as an expense. Such costs are accounted for as part of the acquisition costs or sale proceeds.

The cost of obtaining investment advice from external consultants is included in investment management charges.

The costs of the in-house investment management team are charged to the Funds. The basis of allocation is as described in section g.

Securities lending revenue is reported gross and their fees are disclosed in investment management expenses.

i) Operating lease

Lease payments under an operating lease are recognised as an expense on a straight-line basis over the term of the lease. In accordance with SIC 15, lease incentives are recognised as a reduction in the lease expense over the term of the lease on a straight-line basis.

Net Assets Statement

j) Financial assets

Financial assets are included in the Net Assets Statement on a fair value basis as at the reporting date. A financial asset is recognised in the Net Assets Statement on the date the fund becomes party to the contractual acquisition of the asset. From this date, any gains or losses arising from changes in the fair value of asset are recognised by the fund.

The values of investments as shown in the Net Assets Statement have been determined at fair value in accordance with the requirements of the Code and IFRS13. For the purposes of disclosing levels of fair value hierarchy, the Funds has adopted the classification guidelines recommended in Practical Guidance on Investment Disclosures (PRAG/Investment Association, 2016).

The basis of the valuation of each class of investment assets is set out below. There has been no change in the valuation techniques used during the year. All assets have been valued using fair value techniques which represent the highest and best price available at the reporting date.

Description of asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivity affecting the valuations provided
Market quoted investments - Equities	Level 1	Closing bid value on published exchanges	Not required	Not required
Exchange traded pooled investments	Level 1	Closing bid value on published exchanges	Not required	Not required
Future derivative contracts	Level 1	Determined using exchange prices at the reporting date. Amounts due from or owed to the broker are the amounts outstanding in respect of the initial margin and variation margin.	Not required	Not required

Description of asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivity affecting the valuations provided
Forward foreign exchange derivatives	Level 1	Based on market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year-end with an equal and opposite contract.	Not required	Not required
Government bonds - fixed interest / index linked gilts	Level 2	Recorded at net market value based on their current yields.	Evaluated price feeds	Not required
Unquoted Pooled investments - unitised	Level 2	Closing bid price where bid offer prices are published. Closing single price where single price published.	NAV-based pricing set on a forward pricing basis	Not required
Freehold and leasehold properties	Level 3	Valued at fair value at the year-end using the investment method of valuation by John Finley FRICS of independent valuers, Carrott-Jones LLP in accordance with RICS Valuation Standards (9th Edition)	Existing lease terms and rentals. Independent market research. Nature of tenancies. Covenant strength for existing tenants. Assumed vacancy levels. Estimated rental growth. Discount rate.	Significant changes in rental growth, vacancy levels or the discount rate could affect valuations as could more general changes to market price
Unquoted Pooled investments – Private Equity, Infrastructure, Timber, Private Secured Loans & Property	Level 3	Comparable valuation of similar companies in accordance with International Private Equity and Venture Capital Guidelines (2012)	EBITDA multiple Revenue multiple. Discount for lack of marketability. Control premium.	Valuations could be affected by material events occurring between the date of the financial statements provided and the Funds' own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts.

Sensitivity of assets valued at level 3

Having analysed historical data and current market trends, and consulted with independent investment advisers, the Funds have determined that the valuation methods described above are likely to be accurate to within the following ranges, and has set out below the consequent potential impact on the closing value of investments held at 31 March 2017.

Lothian Pension Fund	Assessed Valuation range (+ or -)	Value at 31 March 2017	Value on increase	Value on decrease
Unquoted		£m	£m	£m
Private Equity	30%	129.3	168.1	90.5
Infrastructure	18%	663.2	782.4	543.8
Timber	18%	132.5	156.4	108.2
Private Secured Loans	8%	89.2	96.3	82.1
Property	13%	389.7	440.4	339.0
		1,403.9	1,643.6	1,163.6

Lothian Buses Pension Fund	Assessed Valuation range (+ or -)	Value at 31 March 2017	Value on increase	Value on decrease
Unquoted		£m	£m	£m
Infrastructure	18%	39.2	46.3	32.1
Timber	18%	8.4	9.9	6.9
Private Secured Loans	8%	6.7	7.2	6.2
		54.3	63.4	45.2

Scottish Homes Pension Fund has no assets valued at Level 3.

k) Foreign currency transactions and balances

Dividends, interest and purchases and sales of investments in foreign currencies have been accounted for at the spot market rates at the date of the transaction. End-of-year spot market exchange rates are used to value cash balances held in foreign currency bank accounts, market values of overseas investments and purchases and sales outstanding at the end of the reporting period.

l) Cash and cash equivalents

Cash comprises cash in hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal risk of changes in value.

m) Financial liabilities

The Funds recognise financial liabilities at fair value as at the reporting date. A financial liability is recognised in the Net Assets Statement on the date the Funds becomes party to the liability. From this date, any gains or losses arising from changes in the fair value of the liability are recognised.

n) Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits of each of the Funds is assessed on an annual basis by the Scheme Actuary in accordance with the requirements of IAS 19 and relevant actuarial standards.

As permitted under IAS26, the Funds have opted to disclose the actuarial present value of promised retirement benefits by way of a note to the Net Assets Statements.

o) Additional voluntary contributions

The Lothian Pension Fund and Lothian Buses Pension Fund provide an additional voluntary contributions (AVC) scheme for their members, the assets of which are invested separately from those of the Funds. The Funds have appointed Standard Life and Prudential as their AVC providers. AVCs are paid to the AVC providers by employers and are specifically for providing additional benefits for individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and the movements in the year.

In accordance with regulation 5(2)(b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 1998, AVCs are not included in pension fund financial statements. Details of contributions paid and the total value of funds invested are disclosed by way of note.

p) Contingent assets and contingent liabilities

A contingent liability arises where an event has taken place prior to the year-end giving rise to a possible financial obligation whose existence will only be confirmed or otherwise by the occurrence of future events. Contingent liabilities can also arise in circumstances where a provision would be made, except that it is not possible at the balance sheet date to measure the value of the financial obligation reliably.

A contingent asset arises where an event has taken place giving rise to a possible asset whose existence will only be confirmed or otherwise by the occurrence of future events.

Contingent assets and liabilities are not recognised in the Net Assets Statement but are disclosed by way of narrative in the notes.

q) Employee benefits

i) Investment and Pensions service division

Staff working on the administration of the Funds that are employed by the City of Edinburgh Council are eligible to join Lothian Pension Fund. As these people are employees of the Council, it's the Council that accounts for the benefits of the defined benefits scheme under IAS19. The Council recharges employment costs to the Funds, including employer contributions to Lothian Pension Fund.

ii) Controlled entity - LPFE Limited

The employees of LPFE Limited are eligible to participate in Lothian Pension Fund.

In the Consolidated Financial Statements the current service cost for the period is charged to the Fund Account. The assets of Lothian Pension Fund are held separately from those of the Company. The Company has fully adopted the accounting principles as required by IAS19 – Employee Benefits.

The liability recognised in the Net Asset Statement in respect of the defined benefit pension plan is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs. The defined benefit obligation is calculated annually by the Scheme Actuary using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in a currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to the Fund Account in the period in which they arise.

Past-service costs are recognised immediately in the Fund Account, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

3 Accounting Standards that have been issued but not yet adopted

The Code requires the disclosure of information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted. This applies to the adoption of the following new or amended standards within the 2017/18 Code:

- IAS 12, Income Taxes
- IAS 39, Financial Instruments: Recognition and Measurement
- IFRS 7, Financial Instruments: Disclosures
- IFRS 9, Financial Instruments
- IFRS 15, Revenue from Contracts with Customers
- IFRS 16, Leases

The amendments are generally minor or principally providing clarification. Overall, these new or amended standards are not expected to have a significant impact on the financial statements.

4 Critical judgements in applying accounting policies

Unquoted private equity and infrastructure investments

It is important to recognise the highly subjective nature of determining the fair value of private equity and infrastructure investments. They are inherently based on forward-looking estimates and judgements involving many factors. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of IFRS.

For the Lothian Pension Fund, the value of unquoted private equity, infrastructure, timber and secured loan investments at 31 March 2017 was £1,014.2m (2016 £716.2m).

For the Lothian Buses Pension Fund, the value of unquoted private equity, infrastructure and timber investments at 31 March 2017 was £54.3m (2016 £26.0m).

Actuarial present value of promised retirement benefits

Each Fund is required to disclose the estimated actuarial present value of promised retirement benefits as at the end of the financial year. These estimates are prepared by the Funds' Actuary. These values are calculated in line with International Accounting Standard 19 (IAS19) assumptions and comply with the requirements of IAS26. However, the results are subject to significant variances based on changes to the underlying assumptions.

The figures are only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Funds.

5 Assumptions made about the future and other major sources of estimation uncertainty

The Financial Statements contain estimated figures that are based on assumptions made by the Council; private equity and infrastructure managers; other providers of valuation information; and the Scheme Actuary about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because amounts cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

The items in the Net Assets Statement at 31 March 2017 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

a) Actuarial present value of promised retirement benefits

Uncertainties

Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on the Funds assets. The Funds' Actuary advises on the assumptions to be applied and prepares the estimates.

Effect if actual results differ from assumptions - Lothian Pension Fund

The effects on the net pension liability of changes in individual assumptions can be illustrated as follows:

Change in assumptions - year ended 31 March 2017	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in discount rate	11	913
1 year increase in member life expectancy	4	320
0.5% increase in salary increase rate	4	320
0.5% increase in pensions increase rate	7	565

Effect if actual results differ from assumptions - Lothian Buses Pension Fund

The effects on the net pension liability of changes in individual assumptions can be illustrated as follows:

Change in assumptions - year ended 31 March 2017	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in discount rate	11	54
1 year increase in member life expectancy	4	18
0.5% increase in salary increase rate	4	18
0.5% increase in pensions increase rate	7	34

Effect if actual results differ from assumptions - Scottish Homes Pension Fund

The effects on the net pension liability of changes in individual assumptions can be illustrated as follows:

Change in assumptions - year ended 31 March 2017	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in discount rate	6	9
1 year increase in member life expectancy	4	6
0.5% increase in pensions increase rate	6	9

b) Valuation of unquoted private equity and infrastructure investments

Uncertainties

These investments are not publicly listed and therefore there is a degree of estimation involved in their valuation, see 2j above for more details on the valuation methodology.

Effect if actual results differ from assumptions

There is a risk that these investments may be under or overstated in the accounts at any point in time. The actual financial return of this type of investment is only known with certainty when they reach the end of their lifecycles and the final distributions are made to investors. A sensitivity analysis can be found in note 2j above.

c) Quantifying the cost of investment fees deducted from capital

Uncertainties

Section 2 h) describes the accounting policy for investment management expenses in relation to expenses deducted from the capital value of investments. Quantification of these costs involves asking the relevant managers for information and only some of this information can be independently verified. In cases where the charges relate to an investment as a whole, an estimate needs to be made of the costs applicable to the holding owned by the relevant Fund.

Effect if actual results differ from assumptions

There is a risk that the cost of investment fees deducted from capital may be under or overstated. However, as the costs are included in the Fund Account by adjusting the change in market value of investments, any inaccuracy in the cost estimate will not change the reported net change in the Fund for the year.

Statement of responsibilities for the Statement of Accounts

The responsibilities of the Administering Authority

The Administering Authority's responsibilities require it to:

- Make arrangements for the proper administration of the financial affairs of the Funds in its charge and to secure that one of its officers has the responsibility for the administration of those affairs. The Head of Finance serves as the Section 95 Officer for all the Council's accounting arrangements, including those of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund. For the Funds, this Section 95 responsibility has been delegated to the Chief Finance Officer, Lothian Pension Fund.
- Manage its affairs to secure economic, efficient and effective use of its resources and safeguard its assets.
- Ensure the Annual Accounts are prepared in accordance with legislation (The Local Authority Accounts (Scotland) Regulations 2014), and so far as is compatible with that legislation, in accordance with proper accounting practices (section 12 of the Local Government in Scotland Act 2003)
- Approve the Annual Accounts for signature.

HUGH DUNN

Head of Finance of the City of Edinburgh Council

27 September 2017

The responsibilities of the Chief Finance Officer, Lothian Pension Fund

The Chief Finance Officer, Lothian Pension Fund, is responsible for the preparation of the Funds' Financial Statements which, in terms of the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the Code of Practice), is required to present a true and fair view of the financial position of the Funds at the accounting date and their income and expenditure for the year (ended 31 March 2017).

In preparing this statement of accounts, the Chief Finance Officer, Lothian Pension Fund, has:

- Selected suitable accounting policies and then applied them consistently
- Made judgements and estimates that were reasonable and prudent
- Complied with the Code of Practice.

The Chief Finance Officer, Lothian Pension Fund, has also:

- Kept proper accounting records which were up to date
- Taken reasonable steps for the prevention and detection of fraud and other irregularities.

The Statement of Accounts presents a true and fair view of the financial position of the Funds as at 31 March 2017, and their income and expenditure for the year ended 31 March 2017.

JOHN BURNS, FCMA CGMA

Chief Finance Officer, Lothian Pension Fund

27 September 2017

Independent auditor's report to the members of City of Edinburgh Council as administering authority for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund and the Accounts Commission

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 120 of the Code of Audit Practice approved by the Accounts Commission, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Report on the audit of the financial statements

Opinion on financial statements

We certify that we have audited the financial statements in the annual accounts of Lothian Pension Fund and its group, Lothian Buses Pension Fund and Scottish Homes Pension Fund (the funds) for the year ended 31 March 2017 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Lothian Pension Fund Group Fund Account, the Lothian Pension Fund Group Net Assets Statement, the Lothian Buses Fund Account, the Lothian Buses Net Asset Statement, the Scottish Homes Fund Account, the Scottish Homes Net Asset Statement and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the 2016/17 Code).

In our opinion the accompanying financial statements:

- give a true and fair view in accordance with applicable law and the 2016/17 Code of the financial transactions of the funds during the year ended 31 March 2017 and of the amount and disposition at that date of their assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2016/17 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Basis of opinion

We conducted our audit in accordance with applicable law and International Standards on Auditing in the UK and Ireland (ISAs (UK&I)). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the funds in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standards for Auditors, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of the Chief Finance Officer for the financial statements

As explained more fully in the Statement of Responsibilities, the Chief Finance Officer is responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Chief Finance Officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibilities for the audit of the financial statements

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable legal requirements and ISAs (UK&I) as required by the Code of Audit Practice approved by the Accounts Commission. Those standards require us to comply with the Financial Reporting Council's Ethical Standards for Auditors. 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 circumstances of the funds and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Chief Finance Officer; and the overall presentation of the financial statements.

Our objectives are to achieve reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK&I) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Other information in the annual accounts

The Chief Finance Officer is responsible for the other information in the annual accounts. The other information comprises the information other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except on matters prescribed by the Accounts Commission to the extent explicitly stated later in this report.

In connection with our audit of the financial statements in accordance with ISAs (UK&I), our responsibility is to read all the financial and non-financial information in the annual accounts 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.

Report on other requirements

Opinions on other prescribed matters

We are required by the Accounts Commission to express an opinion on the following matters.

In our opinion, based on the work undertaken in the course of the audit

- the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with statutory guidance issued under the Local Government in Scotland Act 2003;
- the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016); and
- the information given in the Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations 2014.

Matters on which we are required to report by exception

We are required by the Accounts Commission to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Nick Bennett, (for and on behalf of Scott-Moncrieff)
Exchange Place 3
Semple Street
Edinburgh EH3 8BL

27 September 2017

Annual Governance Statement

Roles and responsibilities

The City of Edinburgh Council (the “Council”) has statutory responsibility for the administration of the Local Government Pension Scheme (LGPS) in the Lothian area of Scotland. This responsibility is for three separate Funds: Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund (the “Funds”).

The main functions of the Administering Authority are administration of scheme benefits and the investment of the assets of the Funds. These functions are conducted in accordance with the Local Government Pension Scheme (Scotland) Regulations which are statutory instruments made under the Superannuation Act 1972.

The role of Administering Authority is carried out via:

- The Pensions Committee and the Pensions Audit Sub-Committee
- The Pension Board
- The Investment and Pensions Division of the Resources Directorate of the Council
- Investment Strategy Panel
- LPFE Limited and LPFI Limited, wholly owned subsidiaries of the Council in its capacity as Administering Authority of Lothian Pension Fund.

Further details on the above arrangements can be found in the Governance section of the Management Commentary towards the front of this document.

Scope of responsibility

As the Administering Authority of the Funds, the City of Edinburgh Council is responsible for ensuring that its business, including that of the Funds, is conducted in accordance with the law and appropriate standards, and that monies are safeguarded, properly accounted for, and used economically, efficiently and effectively. The Council also has a statutory duty under the Local Government in Scotland Act 2003, to make arrangements to secure best value, which is defined as continuous improvement in the way its functions are carried out.

In discharging these overall responsibilities, elected members and senior officers are responsible for implementing effective arrangements for governing the Council’s affairs, and facilitating the effective exercise of its functions, including arrangements for the management of risk. The Pensions Committee has delegated responsibility for additional arrangements specific to the Funds.

To this end, the Council has adopted a Local Code of Corporate Governance that is consistent with the principles of the Chartered Institute of Public Finance and Accountancy (CIPFA) and Society of Local Authority Chief Executives (SOLACE) framework ‘Delivering Good Governance in Local Government’. This statement explains how the City of Edinburgh Council delivers good governance and reviews the effectiveness of those arrangements.

This statement explains how the Council has complied with the Local Code of Corporate Governance and how it meets the CIPFA Code of Practice on Local Authority Accounting in the United Kingdom.

The governance framework

The Funds operate within the wider governance framework of the Council to which is added arrangements specific to the Funds themselves. The governance framework comprises the systems, processes, cultures and values by which the Funds are directed and controlled. It also describes the way the Funds engage with and accounts to its stakeholders. It enables the Funds to monitor the achievement of their objectives and consider whether those objectives have led to the delivery of appropriate, cost-effective services. The framework also applies to any subsidiary companies including LPFE Limited and LPFI Limited which are members of the Council’s Group.

The Council's Local Code of Corporate Governance is supported by evidence of compliance which is regularly reviewed and considered by the Governance, Risk & Best Value Committee. The rest of the Group observes the principles of the code.

The Council has implemented arrangements for monitoring each element of the framework and providing evidence of compliance. The Council's Governance and Democratic Services Manager reviewed the arrangements and is satisfied that the Code continues to be adequate and effective. Internal Audit has also reviewed the annual assurance questionnaire process in relation to Arms-Length Companies and has found that this provides the Chief Executive with a level of assurance on the adequacy of the governance arrangements. The Council's Corporate governance framework meets the principles of effective governance.

The Funds place reliance upon the internal financial controls within the Council's financial systems and the monitoring in place to ensure the effectiveness of these controls. The relevant key elements of the Council's corporate governance framework, with specific additional reference as appropriate to the arrangements for the Funds, are set out below:

Elements of the governance framework specific to the Funds include:

- Identifying the objectives of the Funds in the Funding Strategy Statement, Statement of Investment Principles and Service Plan.
- With effect from April 2015 the Pensions Regulator is responsible for setting standards of governance and administration for the Local Government Pension Scheme. The Funds have taken steps to fully integrate compliance with these standards within the overall governance framework operated by the Funds.
- A systematic approach to monitoring service performance by the Pensions Committee, Pensions Audit Sub-Committee, senior officers and stakeholders, including the Pension Board and Independent Professional Observer.
- A structured programme to ensure that Pensions Committee members have the required standard of knowledge and understanding of Local Government Pension Scheme matters.
- Operating within clearly established investment guidelines defined by the Local Government Pension Scheme Investment Regulations and the Funds' Statement of Investment Principles.
- Compliance with the CIPFA Principles for Investment Decision Making and Disclosure in the Local Government Pension Scheme.
- With the exception of managed funds, unlisted investments and property, all investments are held under custody by a global custodian. The Funds benefit from the custodian's extensive internal control framework.
- Benchmarking of services in terms of standards and cost against other pension funds.
- LPFE Limited and LPFI Limited operating within their respective constitutional documentation and the relevant companies regulations.
- LPFI Limited operating within the relevant governance policies and procedures to ensure compliance with the Financial Conduct Authority regulations.

Elements of the governance framework of the Council that are relevant to the Funds include:

- The Council's key corporate vision and priorities are set out and published in the City of Edinburgh Council Business Plan 2016-2020.
- A performance management framework, incorporating internal and public performance reporting, which focuses on continuous improvement of our services, applying reliable improvement methods to ensure that services are consistently well designed based on the best evidence are a delivered on a right first time basis.
- The Council is embedding a culture of commercial excellence to ensure that our services always deliver Best Value. Focused work is underway to further improve standards in buying practices and processes across the Council.

Elements of the governance framework of the Council that are relevant to the Funds include (cont'd):

- The submission of reports, findings and recommendations from the external auditor, other inspectorates and internal audit, to the Corporate Leadership Group, Governance, Risk and Best Value Committee and Council, and to the Pensions Committee and Pensions Audit Sub-Committee for all matters affecting the Funds, where appropriate, supports effective scrutiny and service improvement activities.
- The roles and responsibilities of Elected Members and Officers are defined in Procedural Standing Orders, Committee Terms of Reference and Delegated Functions, Contract Standing Orders, Scheme of Delegation to Officers, the Member/officer protocol and Financial Regulations. These are subject to annual review.
- The Chief Executive has overall responsibility to Council, for all aspects of operational management and overall responsibility for ensuring the continued development and improvement of systems and processes concerned with ensuring appropriate direction, accountability and control.
- The Section 95 Officer has overall responsibility for ensuring appropriate advice is given to the Council and Group on all financial matters, keeping proper financial records of accounts and maintaining an effective system of internal financial control. For the Funds, the Section 95 officer responsibility has sub-delegated to the Chief Finance Officer, Lothian Pension Fund.
- The Chief Internal Auditor has overall responsibility to review, appraise and report to management and the Governance, Risk and Best Value Committee, and for Fund matters to the Pensions Committee and Pensions Audit Sub-Committee, on the adequacy of the Council's internal control and corporate governance arrangements and on risks relating to approved policies, programmes and projects.
- The Council's Governance and Democratic Services Manager, reporting to the Head of Strategy and Insight, has responsibility for advising the Council on corporate governance arrangements.
- The Governance, Risk and Best Value Committee, and for Fund matters, the Pensions Committee and Pensions Audit Sub-Committee, provides the Council with independent assurance of the adequacy of the governance and risk management frameworks and internal control environment. Also providing independent scrutiny of financial and non-financial performance, approving and monitoring the progress of the Internal Audit risk based plan, and monitoring performance of the internal audit service.
- The risk management policy and framework set out the responsibilities of elected members, Governance, Risk and Best Value Committee, and for pension fund matters, the Pensions Committee and Pensions Audit Sub-Committee, management and staff for the identification and management of risks to corporate and service related priorities;
- The Service Area Risk Register, Resources Senior Management Team Risk Register and Council Risk Register all identify risks and proposed treatment and actions. These registers are regularly reviewed, updated and reported to the Corporate Leadership Group, which reviews Council-wide risk and reports to the Governance, Risk and Best Value Committee for scrutiny and challenge. For fund matters, the Pensions Committee and Pensions Audit Sub-Committee are responsible for scrutiny and challenge.
- Resilience and business continuity plans are in place for all essential Council services. These set out arrangements for continuing to deliver essential services in the event of an emergency or other disruption.
- Senior management and Heads of Service have formal objectives, with performance reviewed by the appropriate chief officer. Officers have personal work objectives, and receive feedback on their performance through the Council-wide performance review and development process.
- An Elected Members remuneration and expenses scheme is in place and is consistent with the Scottish Government's 'Councillors Remuneration: allowances and expenses – Guidance'. Information on the amounts and composition of elected members salaries, allowances and expenses is published on the Council's website.
- The Council's Governance and Democratic Services Manager ensures that induction training on roles and responsibilities, and ongoing development opportunities, are provided for Elected Members. For the Pension Funds, a policy on Committee and Board member training has been adopted.

Elements of the governance framework of the Council that are relevant to the Pension Funds include (cont'd):

- Mandatory training for councillors newly appointed to the Pensions Committee is programmed within the Induction and Training programme for Elected Members following the 2017 Local Government Election. This focuses on Governance, Investment management and strategy and how the Pension Scheme works. Committee members will also be reminded of the requirement to undertake a minimum of 21 hours of training per financial year to fulfil their role on the Pension Committee.
- Codes of Conduct, that set out the standards of behaviour expected from Elected Members and officers, are in place.
- The Employee Code of Conduct, Anti Bribery Policy and Policy on Fraud Prevention set out the responsibilities of officers and Elected Members in relation to fraud and corruption, and are reinforced by the Councillors' Code of Conduct, the Code of Ethical Standards and the Financial Regulations.
- The Whistleblowing policy provides a process for disclosure in the public interest about the Council and its activities by officers, Elected Members and others.
- A Register of Members' Interests and Registers of Officers' interests are maintained and available for public inspection.
- The directors of LPFE Limited and LPFI Limited have obligations to report to the Council/Pensions Committee being the sole shareholder. In addition, the Board and staff of LPFI Limited are each individually regulated by the Financial Conduct Authority and so bound by the associated Principles and Standards of governance best practice.

A significant element of the governance framework is the system of internal controls, which is based on an ongoing process to identify and prioritise risks to the achievement of the Council's objectives, including those relevant to the Pension Funds. Following the establishment of the wholly-owned subsidiary companies, LPFE Limited and LPFI Limited, the Council continues to have appropriate assurance processes and procedures in relation to the responsible officers involved in the administration of the Funds.

Review of Effectiveness

The Local Code of Governance details the Council's arrangements for monitoring each element of the framework and providing evidence of compliance. The Council's Governance and Democratic Services Manager has reviewed the effectiveness of the Code.

The Chief Internal Auditor has also provided an assurance statement on the effectiveness of the system of internal control. The opinion in the assurance statement states: "Internal Audit have not identified any fundamental weaknesses in the framework of governance, risk management and control at the Funds. We consider the Funds' framework to be operating at the higher end of the 'generally adequate but with enhancements required' category."

In compliance with standard accounting practice, the then Acting Executive Director of Resources has provided the Chief Executive with a statement of the effectiveness of the Group's internal financial control system for the year ended 31st March 2017. It is the then Acting Executive Director of Resources' opinion that "reasonable assurance can be placed upon the adequacy and effectiveness of the Group's systems of internal control".

The Chief Finance Officer of Lothian Pension Fund has provided a statement of the effectiveness of the internal financial control system for the year ended 31st March 2017 for the Funds. It is the Chief Finance Officer's opinion "that reasonable assurance can be placed upon the adequacy and effectiveness of the system of internal control for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund."

Certification

It is our opinion, in light of the foregoing, that reasonable assurance can be placed upon the adequacy and effectiveness of the systems of governance that operate within the Group in its administration of the Funds. We consider the governance and internal control environment operating during the financial year from 1 April 2016 to 31 March 2017 to provide reasonable and objective assurance that any significant risks impacting on the Group and its ability to achieve its objectives in properly administering the Funds have and will continue to be identified and actions have and will be taken to avoid or mitigate the impact of any such risks.

Where areas for improvement have been identified and action plans agreed, we will ensure that they are treated as priority and progress towards implementation is reviewed through the governance structures and processes established for the Group and summarised herein. We will continue to review and enhance, as necessary, our governance arrangements.

ANDREW KERR
Chief Executive
of the City of Edinburgh Council
27 September 2017

HUGH DUNN
Head of Finance
of the City of Edinburgh Council
27 September 2017

CLARE SCOTT
Chief Executive Officer
of Lothian Pension Fund
27 September 2017

Governance Compliance Statement

The Regulations that govern the management of Local Government Pension Scheme in Scotland require that a Governance Compliance Statement is published. This statement sets out the extent to which governance arrangements comply with best practice.

The statement below describes arrangements at 31 March 2017 and since the introduction of new governance arrangements on 1 April 2015.

Principle		Full Compliance	Comments
Structure	The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing Council.	Yes	<p>The City of Edinburgh Council acts as administering authority and delegates all pension scheme matters to a committee of seven members (Pensions Committee) made up as follows:</p> <ul style="list-style-type: none"> - Five City of Edinburgh elected members - Two external members, one drawn from the membership of the Funds and one drawn from the employers that participate in the Funds.
	That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.	Yes	<p>The Pensions Committee includes two external places for pension fund stakeholders i.e. one each from the employer and member representatives.</p> <p>Fund members and employers are also represented within the Funds' Pension Board. Membership includes five employer representatives and five member representatives.</p> <p>All members of the Pension Board are invited to attend the meeting of the Pensions Committee and receive the relevant papers prior to those meetings.</p> <p>Two members of the Pension Board attend the Pensions Audit Sub Committee.</p>
	That where a secondary committee or board has been established, the structure ensures effective communication across both levels.	Yes	<p>The Pensions Audit Sub-Committee, consisting of three members of the Pensions Committee, report to the Pensions Committee on their findings and recommendations. Two members of the Pension Board attend the Pensions Audit Sub-Committee in a non-voting capacity. The Pension Board attends the Pensions Committee meetings and takes part in training events.</p> <p>Implementation of investment strategy is delegated to the Executive Director of Resources, who takes advice from the Investment Strategy Panel. The Panel meets quarterly and reports to the Pensions Committee annually.</p> <p>The Investment Strategy Panel consists of the Executive Director of Resources, Chief Executive of the Lothian Pension Fund, Chief Finance Officer, Chief Investment Officer and three experienced external industry advisers.</p> <p>The Pensions Committee receives annual updates from LPFE Limited and LPFI Limited.</p>

Principle		Full Compliance	Comments
Representation	That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include employing authorities (including non-scheme employers, e.g. admitted bodies) and scheme members (including deferred and pensioner scheme members).	Yes	<p>The Pension Board consists of a mix of representatives:</p> <ul style="list-style-type: none"> - Five employer representatives from non-administering authority employers; - Five member representatives appointed by the Trade Unions in accordance with the approach required under Scottish statute.
	Where appropriate, independent professional observers, and expert advisers (on an ad-hoc basis).	Yes	<p>An Independent Professional Observer was appointed in March 2013 to help Committee scrutinise advice.</p> <p>Three external investment advisers sit on the Investment Strategy Panel.</p> <p>A separate specialist Pensions Audit Sub-Committee consisting of three members (including at least two elected members from the City of Edinburgh Council) undertake the audit scrutiny of the funds.</p> <p>A non-executive director was appointed to the board of LPFI Limited on 7 February 2017.</p>
	That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.	Yes	<p>The Pension Board attends the Pensions Committee meetings to help ensure that the operation of the pension funds is in accordance with the applicable law and regulation. The Pension Board takes part in all Committee training events.</p> <p>The Pensions Committee takes account of the views of the Pension Board when making decisions.</p>
Selection and Role of Lay Members	That committee or board members are made fully aware of the status, role and function that they are required to perform on either a main or secondary committee.	Yes	<p>A comprehensive training programme including induction is in place. Members of the Pensions Committee and Pension Board are expected to attend no less than three days of training (21 hours) per year.</p> <p>The non-elected members confirm that they have read, signed and will abide by a Code of Conduct (specifically tailored for the Committee and Board) prior to their appointment to the Pensions Committee and Pension Board. The elected members are required to read, sign and abide by the Councillors' Code of Conduct.</p>
	That at the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.	Yes	<p>The declaration of members' interests is a standard item on the agenda for meetings of the Pensions Committee, Pensions Audit Sub-Committee and Pension Board.</p> <p>A Code of Conduct also applies to all members of the Pensions Committee and the Pension Board.</p>

Voting	The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees.	Yes	Five of the seven places of the Pensions Committee are held by elected members of the City of Edinburgh Council, which is required to retain a 2/3 majority in line with the Local Government (Scotland) Act 1973. The Nomination and Appointments Policy of the Funds, available on the Funds' website, clearly documents how employer and member representatives will be elected to the Pensions Committee and Pension Board.
Training / Facility Time / Expenses	a) That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process.	Yes	A Training and Attendance Policy is in place covering training requirements and reimbursement of expenses. The policy is available on the Funds' website www.lpf.org.uk . Board members and staff working for LPFI Limited also attend separate training for the purposes of their knowledge, understanding and compliance with Financial Conduct Authority regulations.
	b) That where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	Yes	The Training and Attendance Policy applies to both the Pensions Committee and the Pension Board. Advisers have their own professional development obligations.
	c) That the administering authority considers the adoption of annual training plans for committee and board members and maintains a log of all such training.	Yes	Each Pensions Committee and Pension Board member is expected to attend no less than three days training per year (21 hours) per year. Attendance at meetings and training is monitored and reported.
Meetings frequency	a) That an administering authority's main committee or committees meet at least quarterly.	Yes	The Pensions Committee meets at least four times a year.
	b) That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committees sits.	Yes	The Pensions Audit Sub-Committee is held before the Pensions Committee at least three times a year with further meetings held if necessary. The Investment Strategy Panel meets quarterly or more frequently as required. The Pension Board attends all the Pensions Committee meetings and separately meets in advance of each such meetings. Further meetings are held if necessary.
	c) That an administering authority who does not include lay members in their formal governance arrangements must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	Not applicable	

Access	That subject to any rules in the council's constitution, all members of main and secondary committees or boards have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	Yes	Committee papers and minutes are publicly available on the Council's website and all Committee and Pension Board members have equal access. Members of the Pensions Committee and Pension Board have equal access to the Independent Professional Observer who holds surgeries ahead of Committee meetings.
Scope	That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Yes	The Pensions Committee deals with all matters relating to both the administration and investment of the Funds. A separate specialist Pensions Audit Sub-Committee consisting of three members (including at least two elected members from the City of Edinburgh Council) undertake the audit scrutiny of the Funds. The Convener of the Pensions Committee is also a member of the Scottish LGPS Scheme Advisory Board which considers matters on a national level.
Publicity	That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express an interest in wanting to be part of those arrangements.	Yes	Governance documents, policies and details of Pension Board membership are on the Funds' website. The Funds also communicates regularly with employers and scheme members.

ANDREW KERR
Chief Executive
of the City of Edinburgh Council
27 September 2017

HUGH DUNN
Head of Finance
of the City of Edinburgh Council
27 September 2017

CLARE SCOTT
Chief Executive Officer
of the Lothian Pension Fund
27 September 2017

Additional information

Key documents online

You can find further information on what we do and how we do it, on our website at www.lpf.org.uk.

- Actuarial Valuation reports
- Pension Board constitution
- Annual Report and Accounts
- Statement of Investment Principles
- Pension Administration Strategy
- Communications strategy
- Funding Strategy Statement
- Service Plan
- Training and attendance policy

Fund advisers

Actuaries:	Hymans Robertson LLP
Auditor:	Nick Bennett, Scott Moncrieff
Bankers:	Royal Bank of Scotland
Investment consultancy:	KPMG LLP, Gordon Bagot and Scott Jamieson
Investment custodians:	The Northern Trust Company
Investment managers:	Details can be found in the notes to the accounts.
Additional Voluntary Contributions (AVC) managers:	Standard Life and Prudential
Property valuations:	CB Richard Ellis Limited
Solicitors:	Dedicated in-house resource

Comments and suggestions

We appreciate your comments and suggestions on this report. Please let us know which sections you found useful and if you have any suggestions for items to be included in the future. Please email your comments to pensions@lpf.org.uk.

Accessibility

You can get this document on tape, in Braille, large print and various computer formats if you ask us. Please contact the Interpretation and Translation Service (ITS) on 0131 242 8181 and quote reference number 00819. The ITS can also give information on community language translations.

Contact details

If you would like further information about Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Home Pension Fund, please contact us.

Email: pensions@lpf.org.uk
Telephone: 0131 529 4638
Web: www.lpf.org.uk
Fax: 0131 529 6229

Address: Lothian Pension Fund, Atria One, 144 Morrison Street, Edinburgh EH3 8EX



Lothian Pension Fund
Atria One
144 Morrison Street
Edinburgh
EH3 8EX



LPFE Limited

Financial Statements

For the year ended 31 March 2017

Registered number SC497543

LPFE LIMITED

Financial statements

For the year ended 31 March 2017

Contents	Page
Company Information	1
Directors' Report	2 – 4
Independent Auditor's Report to the members of LPFE Limited	5 – 6
Statement of Profit or Loss and Other Comprehensive Income	7
Statement of Financial Position	8
Statement of Changes in Equity	9
Statement of Cash Flows	10
Notes to the Financial Statements	11 – 26

LPFE LIMITED

Company information

Board of Directors:

Chairman

Hugh Dunn

Executive Directors

Clare Scott
Alasdair Rankin
Katy Miller

Company Secretaries:

D.W Company Services Limited
Struan Fairbairn

Registered office

4th Floor Saltire Court
20 Castle Terrace
Edinburgh
Lothian
EH1 2EN

Bankers:

The Royal Bank of Scotland plc
Barclays Bank plc

Auditor:

Scott-Moncrieff
Chartered Accountants
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

LPFE LIMITED

Directors' report

For the year ended 31 March 2017

The directors present their report and audited financial statements for the year ending 31 March 2017.

Principal Activity

The principal activity of the company is the provision of seconded staff to the City of Edinburgh Council and LPFI Limited in support of the administration of the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund (the "Funds") and, separately, to Falkirk Council in its capacity as the administering authority of the Falkirk Council Pension Fund. All these pension funds are part of the Local Government Pension Scheme in Scotland.

Results, Dividends and Mutual Trading Surplus

The profit for the year after tax was £6,275 (2016 - £60,454 loss) and after allowing for items included under "Other comprehensive income" a loss of £396,275 (2016 - £142,454). The directors do not recommend payment of a dividend.

The company's aim is to make a modest trading surplus before adjustments required under IFRS. After allowing for an addition to costs of £2,464 (2016 - £26,697) in respect of accrued holiday pay and £22,000 (2016 - £62,000) for adjustments to pension costs under IAS19, the underlying trading profit is £30,739 (2016 - £28,243). The additional costs recognised under "Other comprehensive income" amounting to £402,550 (2016 - £82,000) all relate to further adjustments required by IAS19 and the related deferred tax.

Under the mutual trading agreement with the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund), the company is required to consider if any of profit arising from the mutual trade can be returned to the Council. Although there was an underlying trading profit of £30,739 (2016 - £28,243), Company Law requires that only "distributable profits" are available for distribution. The company's auditor has confirmed that the various adjustments required under IFRS must be taken into account when determining if profits are distributable. As a result, there are no distributable profits available for return to the Council (acting in its capacity as the administering authority of the Lothian Pension Fund) in respect of the period.

Business Review

The company is wholly owned by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) and has entered into a shareholder agreement with the Council to appropriately address certain governance matters. The company also has a loan facility provided by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) for the purpose of the provision of short term working capital.

Staffing services are provided to the City of Edinburgh Council for the purposes of administering the Funds under an intra-group resourcing agreement. The agreement also provides for the running costs of the company to be covered as part of a service charge and anticipates the provision of staffing services to LPFI Limited, also wholly owned by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund).

The company has entered into appropriate admission arrangements with the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) to enable the employees of the company to be members of the Lothian Pension Fund and in relation to the company's obligations as an employer in that fund.

HMRC has agreed that any profits arising as a result from trade between the company and the City of Edinburgh Council will be covered by the "Mutual Trading" rules and so not subject to Corporation Tax.

The company also has a secondment agreement with the Falkirk Council to provide investment staff to assist with certain aspects of the administration of the Falkirk Council Pension Fund as part of a mutually beneficial collaboration between those LGPS funds.

LPFE LIMITED

Directors' report (continued)

For the year ended 31 March 2017

Future Prospects

The company's future prospects are primarily linked to the needs of the City of Edinburgh Council in its administration of the Funds. The company is securely funded by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) which means that it is able to adapt to any future staffing requirements.

At its meeting on 20 March 2017, Pensions Committee agreed that the remaining pension fund staff, employed by the City of Edinburgh Council, should be transferred to LPFE Limited subject to the appropriate consultation with staff and trades unions and any legal and risk analysis being concluded to the Executive Director of Resources' satisfaction.

Directors

The directors who served during the period were:

Hugh Dunn	
Clare Scott	
Alasdair Rankin	
Martin Glover	(resigned 19 August 2016)
Katy Miller	(appointed 25 October 2016)

Statement of directors' responsibilities

The directors are responsible for preparing the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of its results for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

LPFE LIMITED

Directors' report (continued)

For the year ended 31 March 2017

Disclosure of information to auditor

As far as each of the directors at the time the report is approved are aware:

- a) there is no relevant information of which the company's auditor is unaware, and
- b) the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of the information

Auditor

The auditor, Scott-Moncrieff, is deemed to be reappointed under Section 487 (2) of the Companies Act 2006.

Small company provisions

This report has been prepared in accordance with the special provisions for small companies under Part 15 of the Companies Act 2006.

This report was approved by the board and signed on its behalf by:

Date: 2017

**Hugh Dunn
Chairman**

LPFE LIMITED

Independent auditor's report to the members of LPFE Limited

For the year ended 31 March 2017

We have audited the financial statements of LPFE Limited for the year ended 31 March 2017 which comprise the Statement of Profit or Loss and Other Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows and related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them 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 company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective Responsibilities of the Directors and the Auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 3, the directors are responsible for the preparation of the financial statements and for being satisfied that they 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 (APB's) Ethical Standards for Auditors.

Scope of the Audit on the Financial Statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on Financial Statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2017 and of its results for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on Other Matter(s) Prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements and the Directors' Report has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the company and its environment obtained during the course of our audit, we have not identified any material misstatements in the Directors' Report.

LPFE LIMITED

Independent auditor's report to the members of LPFE Limited (continued)

For the year ended 31 March 2017

Matters on Which We Are Required to Report by Exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- the company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not entitled to prepare the financial statements in accordance with the small companies regime and take advantage of the small companies' exemption in preparing the directors' report; or
- the directors were not entitled to take advantage of the small companies exemption from the requirement to prepare a strategic report.

Nick Bennett, Senior Statutory Auditor
For and on behalf of Scott-Moncrieff, Statutory Auditor
Chartered Accountants
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

Date:2017

LPFE LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2017

	Note	2017 £	2016 £
Continuing Operations			
Revenue	1e	1,189,855	904,074
Gross profit		<u>1,189,855</u>	<u>904,074</u>
Administrative expenses		(1,176,881)	(959,895)
Profit/(loss) from operations	2	12,974	(55,821)
Finance costs	3	(6,720)	(9,968)
Profit/(loss) before tax		<u>6,254</u>	<u>(65,789)</u>
Corporation tax credit	4	21	5,335
Profit/(loss) for the year		<u>6,275</u>	<u>(60,454)</u>
 Other comprehensive income:			
Those that are not recyclable net of tax:			
Recognition of opening retirement benefit obligation	15	-	(281,000)
Actuarial (losses)/gains on retirement benefit obligation period	15	(483,000)	163,000
Deferred tax charge thereon	10	80,450	36,000
Total comprehensive loss for the year		<u>(396,275)</u>	<u>(142,454)</u>

The accompanying notes on pages 11 to 26 form part of these financial statements

LPFE LIMITED

Statement of Financial Position

As at 31 March 2017

	Note	As at 31 March 2017 £	As at 31 March 2016 £
Non-current assets			
Deferred tax asset	10	116,450	36,000
Total non-current assets		116,450	36,000
Current assets			
Trade and other receivables	7	166,801	129,681
Cash and cash equivalents	8	13,381	5,065
Total current assets		180,182	134,746
Total assets		296,632	170,746
Equity and Liabilities			
Equity attributable to equity holders of the parent			
Share capital	11	1	1
Retained earnings	12	(538,729)	(142,454)
		(538,728)	(142,453)
Liabilities			
Non-current liabilities			
Retirement benefits obligation	15	685,000	180,000
Total non-current liabilities		685,000	180,000
Current liabilities			
Trade and other payables	9	150,360	133,199
Total current liabilities		150,360	133,199
Total liabilities		835,360	313,199
Total equity and liabilities		296,632	170,746

The financial statements were authorised for issue by the Board of Directors on 2017 and were signed on its behalf by:

.....
Director

Registered number SC497543

The accompanying notes on pages 11 to 26 form part of these financial statements

LPFE Limited
Statement of Changes in Equity
As at 31 March 2017

	Note	Share Capital £	Retained Earnings £	Total £
Comprehensive income				
Loss for the year		-	(60,454)	(60,454)
Other comprehensive income				
Share capital issued	11	1	-	1
Recognition of opening retirement benefit obligation	15	-	(281,000)	(281,000)
Actuarial gains on retirement benefit obligation in period	15	-	163,000	163,000
Deferred tax on retirement benefit obligation	10	-	36,000	36,000
Balance at 31 March 2016		<u>1</u>	<u>(142,454)</u>	<u>(142,453)</u>

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2016		1	(142,454)	(142,453)
Comprehensive income				
Profit for the year		-	6,275	6,275
Other comprehensive income				
Actuarial losses on retirement benefit obligation in year	15	-	(483,000)	(483,000)
Deferred tax on retirement benefit obligation	10	-	80,450	80,450
Balance at 31 March 2017		<u>1</u>	<u>(538,729)</u>	<u>(538,728)</u>

The accompanying notes on pages 11 to 26 form part of these financial statements

LPFE LIMITED
Statement of Cash Flows

For the year ended 31 March 2017

	2017	2016
	£	£
Cash flow from operating activities		
Profit for the period	6,275	(60,454)
Adjustments for:		
Defined benefit pension – current service cost	172,000	174,000
Defined benefit pension – employer contribution	(156,000)	(121,000)
Defined benefit pension – finance costs	6,000	9,000
Other finance costs	720	968
Changes in assets and liabilities:		
(Increase)/decrease in receivables and other financial assets	(19,008)	(123,524)
Increase/(decrease) in payables	17,342	133,005
	<hr/>	<hr/>
Cash flows from operations	27,329	11,995
Interest paid	(901)	(774)
	<hr/>	<hr/>
Net cash flows from operating activities	26,428	11,221
	<hr/>	<hr/>
Cash flow from investing activities	-	-
	<hr/>	<hr/>
Net cash flows from investing activities	-	-
	<hr/>	<hr/>
Cash flow from financing activities		
Share capital issued		1
Movement in loan facility	(18,112)	(6,157)
	<hr/>	<hr/>
Net cash flows from financing activities	(18,112)	(6,156)
	<hr/>	<hr/>
Net increase in cash and cash equivalents	8,316	5,065
Cash and cash equivalents at beginning of year	5,065	-
	<hr/>	<hr/>
Cash and cash equivalents at end of year	13,381	5,065
	<hr/> <hr/>	<hr/> <hr/>
Cash at bank and in hand	13,381	5,065
	<hr/> <hr/>	<hr/> <hr/>

The accompanying notes on pages 11 to 26 form part of these financial statements

LPFE LIMITED

Notes to the Financial Statements

For the year ended 31 March 2017

1. Statement of significant accounting policies

The financial statements of LPFE Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU), IFRIC Interpretations and the Companies Act 2006 applicable to companies reporting under IFRS.

Adoption of new and revised standards

The Company has adopted the following new and amended IFRSs as of 1 April 2016.

- IAS1, Presentation of Financial Statements
- IAS19, Employee Benefits
- IFRS7, Financial Instruments: Disclosures

None of these have materially impacted the financial statements of the company.

Guidance in issue but not in force

IAS 8 requires disclosure of guidance in issue but not in force. The minimum disclosure relates to guidance issued by 31 March 2017, and with potential effect.

International Accounting Standards and Interpretations	Effective for annual periods beginning on or after
IAS 7, Statement of Cash Flows*	1 January 2017
IAS 12, Income Taxes*	1 January 2017
IAS 39, Financial Instruments: Recognition and Measurement	1 January 2018
IFRS 7, Financial Instruments: Disclosures	1 January 2018
IFRS 9, Financial Instruments	1 January 2018
IFRS 15, Revenue from Contracts With Customers	1 January 2018
IFRS 16, Leases*	1 January 2019

*Not yet adopted for use in the European Union

The directors have reviewed the requirements of the new standards and interpretations listed above and they are not expected to have a material impact on the company's financial statements in the period of initial application.

Basis of preparation

The financial statements are presented in Sterling (£) as that is the company's functional currency and the currency in which the majority of the company's accounting policies.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the company's accounting policies.

The following significant accounting policies, which are consistent with the previous period unless otherwise stated, have been adopted in the preparation of this report:

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

1. Statement of significant accounting policies (continued)

a. Going concern

The directors are of the opinion that the company has adequate resources to enable it to undertake its planned activities for a period of at least one year from the date that the financial statements are approved.

b. Current and deferred income tax

The company is a mutual trader and is therefore not liable to corporation tax on surpluses generated from mutual trade. The tax charge for the period is based on the profit for the year from non-mutual trade, adjusted for any non-assessable or disallowed items. It is calculated using tax rates that have been enacted or are substantively enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred income tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

c. Impairment

The carrying value of all assets are reviewed for impairment at each reporting date, with the recoverable amount being estimated when events or changes in circumstances indicate that the carrying value may be impaired.

The recoverable amount of all assets is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which it belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of the asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 December 2017

1. Statement of significant accounting policies (continued)

d. Cash and cash equivalents

For the purposes of the statement of cash flows, cash includes cash on hand and at call deposits with banks or financial institutions, investments in money market instruments maturing within less than two months and is net of bank overdrafts.

e. Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty.

Revenue is derived wholly from the provision of seconded staff in the United Kingdom. Revenue is recognised upon the delivery of the service to the customer.

All revenue is stated net of the amount of value added tax (VAT).

f. Value added tax

Revenues, expenses and assets are recognised net of the amount of value added tax (VAT), except:

- i. Where the amount of VAT incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
- ii. For receivables and payables, which are recognised inclusive of VAT.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Cash flows are included in the statement of cash flows on a gross basis. The VAT component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

g. Share capital

Ordinary shares are classified as equity.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

1. Statement of significant accounting policies (continued)

h. Employee benefits

The company contributes to a defined benefits scheme operated on behalf of its employees.

The employees of LPFE Limited participate in the Lothian Pension Fund, which is part of the Local Government Pension Scheme in Scotland and is administered by the City of Edinburgh Council.

The current service cost for the period is charged to the Statement of Profit or Loss and Other Comprehensive Income. The assets of the scheme are held separately from those of the company in independently administered funds. The company has fully adopted the accounting principles as required by International Accounting Standard 19 – Employee Benefits.

The liability recognised in the balance sheet in respect of defined benefit pension plan is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in a currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity through other comprehensive income in the period in which they arise.

Past-service costs are recognised immediately in income, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

i. Financial instruments

Financial assets and financial liabilities are recognised when the company has become party to the contractual provisions of the instrument.

Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is recognised in the statement of comprehensive income.

Trade payables

Trade payables are initially recognised at fair value and subsequently at amortised cost using the effective interest method.

Financial liabilities

Financial liabilities are classified according to the substance of the contractual arrangements entered into.

An instrument will be classified as a financial liability when there is a contractual obligation to deliver cash or another financial asset to another enterprise.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

1. Statement of significant accounting policies (continued)

i. Financial instruments (continued)

Loans

All interest bearing loans and other borrowings are initially recorded at fair value, which represents the fair value of the consideration received, net of any issue costs associated with other borrowings. Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs.

Finance charges, including premiums payable on settlement or redemption, are accounted for on an amortised cost basis to the statement of comprehensive income using the effective interest method, being recognised in the statement of comprehensive income over the term of such instruments at a constant rate on the carrying amount of the instrument to the extent that they are not settled in the year in which they arise.

Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

j. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

k. Critical accounting estimates and judgements

The directors evaluate estimates and judgements incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the company.

Key estimates – defined benefit pension obligation

IAS 19, Employee Benefits requires that certain assumptions are made in order to determine the amount to be recorded for retirement benefit obligations and pension plan assets. These are mainly actuarial assumptions such as expected inflation rates, long-term increase in health care costs, employee turnover, expected return on plan assets and discount rates. Substantial changes in the assumed development of any one of these variables may significantly change the Group's retirement benefit obligation and pension assets (see note 15 for further details).

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

2. Profit/(loss) from operations

	2017	2016
	£	£
Profit/(loss) from operations has been determined after deducting:		
Auditors' remuneration:		
Audit services	4,800	4,750
Non-Audit services	3,798	2,250
	3,798	2,250

3. Finance costs

	2017	2016
	£	£
Loan interest payable to group entities (note 14)	720	968
Pension interest costs (note 15)	6,000	9,000
	6,720	9,968

4. Corporation tax credit

	2017	2016
	£	£
Current tax:		
Corporation tax credit	(21)	(5,335)
	(21)	(5,335)

Corporation tax credit is calculated at 20% of the assessable profits for the year.

The credit for the year can be reconciled to the loss per the income statement as follows:

	2017	2016
	£'000	£'000
Profit/(loss) for the year before taxation	6,254	(65,789)
Profit/(loss) for the year at the effective rate of corporation tax of 20% (2016 – 20%)	1,251	(13,158)
Effects of:		
Mutual trade adjustment	(1,753)	6,406
Expenses not deductible for tax purposes	438	1,466
Trading losses carried forward	42	-
Other adjustments	1	(49)
Current tax credit	(21)	(5,335)

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 December 2017

5. Employee benefits expense

The average number of persons employed by the company (including directors) during the year was 11 (2016: 11).

The aggregate payroll costs were as follows:

	2017	2016
	£	£
Wages and salaries	849,767	675,817
Social security costs	104,078	67,389
Defined benefit pension obligation - current service cost	172,000	174,000
	<u>1,125,845</u>	<u>917,206</u>

6. Directors' remuneration

One director received emoluments from the company during the period. The director's emoluments for the period were as follows:

	2017	2016
	£	£
Aggregate emoluments	92,000	78,384
Employer pension contributions	18,860	16,068
	<u>110,860</u>	<u>94,452</u>

The director had an accrued pension of £16,799 (2016: £13,919) and a lump sum of £11,843 (2016: £10,973) at the end of the year.

All other directors are employed by the City of Edinburgh Council.

7. Trade and other receivables

	2017	2016
	£	£
Trade receivables	29,433	27,295
Amounts due from group entities	137,354	102,366
Prepayments and accrued income	14	20
	<u>166,801</u>	<u>129,681</u>

The directors consider the fair value of receivables to be in line with carrying values.

8. Cash and cash equivalents

	2017	2016
	£	£
Cash at bank and in hand	<u>13,381</u>	<u>5,065</u>

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 December 2017

9. Current liabilities

	2017	2016
	£	£
Trade payables	3,109	308
Accruals and deferred income	39,813	36,581
Social security and other taxes	107,425	96,116
Amounts due to group entities	13	194
	150,360	133,199
	150,360	133,199

10. Deferred tax

	2017	2016
	£	£
At 31 March 2016	36,000	-
Charge for the year to other comprehensive income	80,450	36,000
	116,450	36,000
	116,450	36,000
The elements of deferred tax are as follows:		
Defined benefit pension scheme liability	116,450	36,000
	116,450	36,000
	116,450	36,000

11. Share Capital

	2017	2016
	£	£
<i>Allotted, called up and fully paid</i>		
Ordinary shares of £1 each	1	1
	1	1
	1	1

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

12. Reserves

	Retained Earnings £
Loss for the period	(60,454)
Transfer of opening retirement benefit obligation	(281,000)
Actuarial gains on retirement benefit obligation	163,000
Deferred tax on retirement benefit obligation	36,000
	<hr/>
At 31 March 2016	(142,454)
Profit for the year	6,275
Actuarial loss on pension plan	(483,000)
Deferred tax on retirement benefit obligation	80,450
	<hr/>
At 31 March 2017	<u>(538,729)</u>

13. Controlling interest

The City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) owns all the issued share capital of the company. The company itself has been established to support the administration of the Lothian Pension Fund. Administering authorities are required to prepare separate financial statements for the Local Government Pension Scheme funds that they administer and so it is considered appropriate to consolidate the company's individual financial statement into Lothian Pension Fund's consolidated financial statements.

Group accounts are available to the public from the following address:

Account Dept.
Lothian Pension Fund
Atria One
144 Morrison Street
Edinburgh
EH3 8EX

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

14. Related party transactions

	2017	2016
	£	£
Lothian Pension Fund (pension fund administered by City of Edinburgh Council)		
Sale of services during the period	1,073,448	819,720
Receivables at the period end	104,803	90,874
Loan facility balance receivable at the period end	24,269	6,157
Interest payable during the period	720	968
Interest payable but still accruing at the period end	13	194
Lothian Buses Limited (company under common control)		
Balance receivable for group tax losses surrendered	1,321	5,335
LPFI Limited (company under common control)		
Sale of services during the period	6,940	-
Receivables at the period end	6,940	-
Balance receivable for group tax losses surrendered	21	-

The company has a loan facility agreement with Lothian Pension Fund for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the company returns any cash not immediately required and this can result in short periods when the company has returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Total compensation paid in relation to key management personnel during the period was as follows:

	2017	2016
	£	£
Short-term employee benefits	380,321	318,192
Post-employment benefits - employer pension contributions	77,616	65,228
	457,937	383,420
	457,937	383,420

Key management personnel had accrued pensions totalling £81,825 (2016: £68,004) and lump sums totalling £100,185 (2016: £92,156) at the end of the period.

All other key management personnel are employed by the City of Edinburgh Council.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

15. Retirement benefits obligation

The Lothian Pension Fund, which is administered by the City of Edinburgh Council, is part of the Local Government Pension Scheme in Scotland. This is a pension scheme providing benefits based on final pensionable pay, contributions being charged to the profit or loss so to spread the cost of pensions over employees' working lives. The contributions are determined by a qualified actuary.

The valuation of the pension fund is carried out triennially. The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at 31 December 2014 by Hymans Robertson LLP. The present value of the defined benefit obligation, and related current service cost and past service cost, were measured using the Projected Unit Credit Method.

Scheme assets

The group's share of the fair value of the scheme's assets which are not intended to be realised in the short term and may be subject to significant change before they are realised, were comprised as follows:

	%	2017 £'000	%	2016 £'000
Equity Securities:				
Consumer	15%	425	15%	319
Manufacturing	15%	429	12%	247
Energy and Utilities	7%	210	8%	167
Financial Institutions	7%	197	8%	178
Health and Care	6%	166	7%	139
Information Technology	5%	140	6%	126
Other	7%	195	6%	120
Debt Securities:				
Corporate Bonds (investment grade)	0%	0	0%	0
UK Government	10%	284	6%	135
Other	0%	6	3%	53
Private Equity:				
All	3%	91	4%	92
Real Estate				
UK Property	7%	191	9%	179
Investment Funds and Unit Trusts:				
Equities	0%	0	0%	0
Commodities	0%	8	0%	6
Bonds	1%	42	1%	17
Infrastructure	9%	253	7%	139
Other	2%	60	2%	50
Cash and Cash Equivalents:				
All	5%	131	6%	130
	<u>100%</u>	<u>2,828</u>	<u>100%</u>	<u>2,097</u>

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 December 2017

15. Retirement benefits obligation (continued)

The amounts recognised in the statement of financial position are determined as follows:	2017	2016
	£'000	£'000
Fair value of plan assets	2,828	2,097
Present value of scheme liabilities	(3,513)	(2,277)
	<hr/>	<hr/>
Net pension liability	(685)	(180)
	<hr/> <hr/>	<hr/> <hr/>

The movement in the defined benefit obligation over the year is as follows:

	2017	2016
	£'000	£'000
Brought forward	2,277	2,107
Current service cost	172	174
Interest cost on obligation	86	69
Plan participants contributions	76	54
Benefits paid	0	0
Actuarial losses arising from changes in financial assumptions	902	(378)
Actuarial losses arising from changes in demographic assumptions	0	0
Other actuarial (gains)	0	251
	<hr/>	<hr/>
Balance at year end	3,513	2,277
	<hr/> <hr/>	<hr/> <hr/>

The movement in the fair value of plan assets of the year is as follows:

	2017	2016
	£'000	£'000
Brought forward	2,097	1,826
Benefits paid	0	0
Interest income on plan assets	80	60
Contributions by employer	156	121
Contributions by member	76	54
Return on assets excluding amounts included in net interest	419	36
	<hr/>	<hr/>
Balance at year end	2,828	2,097
	<hr/> <hr/>	<hr/> <hr/>

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

15. Retirement benefits obligation (continued)

The amounts recognised in the Statement of Profit or Loss are as follows:

	2017	2016
	£'000	£'000
Interest received on pension scheme assets	(80)	(60)
Interest cost on pension scheme liabilities	86	69
	<hr/>	<hr/>
Finance (income)/cost	6	9
Current service cost	172	174
	<hr/>	<hr/>
	178	183
	<hr/> <hr/>	<hr/> <hr/>

Amounts recognised in other comprehensive income:

	2017	2016
	£'000	£'000
Transfer of opening retirement benefit obligation on 1 May 2015	-	(281)
Actuarial (losses) in the defined benefit obligation	(902)	127
Actuarial gains in the fair value of defined benefit assets	419	36
	<hr/>	<hr/>
	(483)	(118)
	<hr/> <hr/>	<hr/> <hr/>

The principal actuarial assumptions used in this valuation were:

	2017	2016
Inflation/pension increase rate	2.4%	2.2%
Salary increase rate	4.4%	4.2%
Discount rate	2.7%	3.6%

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice. Best estimate has been interpreted to mean that the proposed assumptions are 'neutral' – there is an equal chance of actual experience being better or worse than the assumptions proposed.

The financial assumptions used for reporting in the financial statements are the responsibility of the employer. These assumptions are largely prescribed at any point and reflect market conditions at the reporting date. Changes in market conditions that result in changes in the net discount rate can have significant effect on the value of the liabilities reported.

A reduction in the net discount rate will increase the assessed value of liabilities as a higher value is placed on benefits paid in the future. A rise in the net discount rate will have the opposite effect of a similar magnitude. There is also uncertainty around life expectancy of the UK population – the value of current and future pension benefits will depend on how long they are assumed to be in payment.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

15. Retirement benefits obligation (continued)

The sensitivity of the overall pension liability to changes in the weighted principal assumptions is:

Change in assumption	Approximate % increase to employer liability		Approximate increase to employer liability (£'000)	
	2017	2016	2017	2016
0.5% decrease in real discount rate	14%	14%	508	319
0.5% increase in the salary increase rate	7%	7%	237	156
0.5% increase in the pension increase rate	7%	7%	252	155

Mortality rates:

Life expectancy is based on the Fund's Vita Curves with improvements in line with the CMI 2012 model assuming current rates of improvements have peaked and will converge at to a long term rate of 1.25% p.a.

Based on these assumptions, the average future life expectancy at age 65 are summarised below:

	Male	Female
Current pensioners	22.1	23.7
Future pensioners	24.2	26.3

Expected employer contributions to the benefit plans for the year ended 31 March 2018 are £157,000, based on a pensionable payroll cost of £764,000.

16. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable.

The company did not enter into any transactions that would be classed derivative financial instruments during the period.

The totals for each category of financial instruments, measured in accordance with IAS 39 and detailed in the accounting policies, are as follows:

	Note	2017 £	2016 £
Financial Assets			
Cash and cash equivalents	8	13,381	5,065
Trade and other receivables	7	166,801	129,681
Total Financial Assets		<u>180,182</u>	<u>134,746</u>
Financial Liabilities			
Financial liabilities at amortised cost:			
Trade and other payables	9	150,360	133,199
Total Financial Liabilities		<u>150,360</u>	<u>133,199</u>

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

16. Financial Risk Management (continued)

Financial Risk Management Policies

The company aims to manage its overall capital structure to ensure it continues to operate as a going concern. The company's capital structure represents the equity attributable to the shareholders of the company together with cash equivalents.

The Board is charged with the overall responsibility of establishing and monitoring the company's risk management policies and processes in order to identify, analyse and monitor the risks that are faced by the company. The company does not enter into or trade financial instruments for speculative purposes.

The main risks that the company is exposed to through its financial instruments are credit risk, liquidity risk and market risk. These are managed as follows:

a. Credit risk

Exposure to credit risk relating to financial assets arises from the potential non-performance by counterparties of contractual obligations that could lead to a financial loss to the company.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance sheet date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the Statement of Financial Position and notes to the financial statements. As at 31 March 2017 none of the company's financial assets were past due or impaired.

Credit risk is managed and reviewed regularly by senior management. It mainly arises from amounts owed by customers.

The nature of the company's business means that it currently only has two customers. By far the largest customer is the City of Edinburgh Council and the company is securely funded by the Council. The smaller customer is Falkirk Council. Given the financial stature of both Councils the credit risk faced by the company is considered to be very small.

b. Liquidity Risk

Liquidity risk arises from the possibility that the company might encounter difficulty in settling its debts or otherwise meeting its financial obligations as they fall due. The company manages this risk through the following mechanisms:

- preparing forward-looking cash flow analysis in relation to its operational, investing and financing activities; and
- ensuring that adequate unutilised borrowing facilities are maintained.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

16. Financial Risk Management (continued)

b. Liquidity Risk (continued)

The tables below reflect an undiscounted contractual maturity analysis for financial liabilities.

Financial liability and financial asset maturity analysis

	Note	Within 1 Year 2017 £	1 to 5 Years 2017 £	Total 2017 £
Financial liabilities due for payment				
Trade and other payables	9	(150,360)	-	(150,360)
		<u>(150,360)</u>	<u>-</u>	<u>(150,360)</u>
Financial assets — cash flows realisable				
Cash and cash equivalents	8	13,381	-	13,381
Trade and other receivables	7	166,801	-	166,801
		<u>180,182</u>	<u>-</u>	<u>180,182</u>
Net inflow of financial instruments		<u>29,822</u>	<u>-</u>	<u>29,822</u>

Cash flows realised from financial assets reflect management's expectation as to the timing of realisation. Actual timing may therefore differ from that disclosed. The timing of cash flows as presented in the table (to settle financial liabilities) reflects the earliest contractual settlement dates.

The company has been granted a £250,000 unsecured revolving loan facility by its parent, The City of Edinburgh Council. The ceiling of the facility has been set at a level to ensure sufficient cash is available to meet the company's short-term cash flow needs, should there be a delay in the City of Edinburgh Council settling invoices for seconded staff.

c. Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the company's financial position. The company has no direct exposure to movements in foreign exchange or equity prices, and has very little exposure to interest rate movements, due to the low level of borrowing. The company monitors this risk but the directors are of the opinion that it is very unlikely to have a significant effect on the company's financial position.

LPFI Limited

Financial Statements

For the year ended 31 March 2017

Registered number SC497542

LPFI LIMITED

Financial statements

For the year ended 31 March 2017

Contents	Page
Company Information	1
Directors' Report	2 – 3
Independent Auditor's Report to the Members of LPFI Limited	4 – 5
Statement of Profit or Loss and Other Comprehensive Income	6
Statement of Financial Position	7
Statement of Changes in Equity	8
Statement of Cash Flows	9
Notes to the Financial Statements	10 - 20

LPMI LIMITED

Company information

Board of Directors:

Chairman

Hugh Dunn

Executive Directors

Struan Fairbairn

John Burns

William Miller

Clare Scott

Non-executive Director

Leslie Robb

Company Secretary:

D.W. Company Services Limited

Registered office:

4th Floor Saltire Court

20 Castle Terrace

Edinburgh

Lothian

EH1 2EN

Bankers:

The Royal Bank of Scotland plc

Auditor:

Scott-Moncrieff

Exchange Place 3

Semple Street

Edinburgh

EH3 8BL

LPFI LIMITED

Directors' report

For the year ended 31 March 2017

The directors present their report and audited financial statements for the year ended 31 March 2017.

Principal Activity

The principal activity of the company is the provision of FCA regulated investment services to Lothian Pension Fund and other Local Government Pension Scheme funds in Scotland and Northern Ireland.

Results, Dividends and Mutual Trading Surplus

The profit for the year after tax was £432. The directors do not recommend payment of a dividend.

The company's aim is to make a modest trading surplus.

Under the mutual trading agreement with the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund), the company is required to consider if any of profit arising from the mutual trade can be returned to the Council. Company Law requires that only "distributable profits" are available for distribution. None of the profit for the year is attributable to the mutual trade.

Business Review

The company is wholly owned by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) and has entered into a shareholder agreement with the Council to appropriately address certain governance matters. The company also has a loan facility provided by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) for the purpose of the provision of short term working capital.

LPFI Limited does not employ staff directly, staffing and business support services are provided to company under an intra-group resourcing agreement with the City of Edinburgh Council and LPFE Limited. LPFE Limited is also wholly owned by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund).

HMRC has agreed that any profits arising as a result from trade between the company and the City of Edinburgh Council will be covered by the "Mutual Trading" rules and so not subject to Corporation Tax.

The company was granted authorised status by the FCA on 24 June 2016. In December of 2016, LPFI Limited started work with its first client on an infrastructure investment project and a second project was in progress at the year end.

Future prospects

The company's prospects are linked to Lothian Pension Fund's requirement for FCA regulated investment services and the Fund's plans to work with other LGPS funds in the collaborative provision of such services. The company is securely funded by the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) which means that it can adapt to future trading needs.

The 2017/18 financial year should see significant expansion of the company's operations.

Directors

The directors who served during the year were:

Hugh Dunn

Struan Fairbairn

John Burns

William Miller

Clare Scott

Leslie Robb

(appointed 7 February 2017)

LPFI LIMITED

Directors' report (continued)

For the year ended 31 March 2017

Statement of directors' responsibilities

The directors are responsible for preparing the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of its results for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Disclosure of information to auditor

As far as each of the directors at the time the report is approved are aware:

- a) there is no relevant information of which the company's auditor is unaware, and
- b) the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of the information.

Auditor

The auditor, Scott-Moncrieff, is deemed to be reappointed under Section 487 (2) of the Companies Act 2006.

Small company provisions

This report has been prepared in accordance with the special provisions for small companies under Part 15 of the Companies Act 2006.

This report was approved by the board and signed on its behalf by:

Date:2017

Hugh Dunn
Chairman

LPFI LIMITED

Independent auditor's report to the members of LPFI Limited

For the year ended 31 March 2017

We have audited the financial statements of LPFI Limited for the year ended 31 March 2017 which comprise the Statement of Profit or Loss and Other Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows and related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them 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 company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective Responsibilities of the Directors and the Auditor

As explained more fully in the Statement of directors' responsibilities set out on page 3, the directors are responsible for the preparation of the financial statements and for being satisfied that they 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 (APB's) Ethical Standards for Auditors.

Scope of the Audit on the Financial Statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on Financial Statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2017 and of its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on Other Matter(s) Prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements and the Directors' Report has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the company and its environment obtained during the course of our audit, we have not identified any material misstatements in the Directors' Report.

LPFI LIMITED

Independent auditor's report to the members of LPFI Limited (continued)

For the year ended 31 March 2017

Matters on Which We Are Required to Report by Exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- the company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not entitled to prepare the financial statements in accordance with the small companies regime and take advantage of the small companies' exemption in preparing the directors' report; or
- the directors were not entitled to take advantage of the small companies exemption from the requirement to prepare a strategic report.

Nick Bennett, Senior Statutory Auditor
For and on behalf of Scott-Moncrieff, Statutory Auditor
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

Date: 2017

LPFI LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2017

	Note	2017 £	2016 £
Continuing Operations			
Revenue	1e	23,988	-
Gross profit		<u>23,988</u>	<u>-</u>
Administrative expenses		(23,348)	-
Profit from operations	2	<u>640</u>	<u>-</u>
Finance costs	3	(100)	-
Profit before income tax expense		<u>540</u>	<u>-</u>
Corporation tax charge	4	(108)	-
Profit for the year	11	<u>432</u>	<u>-</u>
Other comprehensive income		<u>-</u>	<u>-</u>
Total comprehensive income for the year		<u><u>432</u></u>	<u><u>-</u></u>

The accompanying notes on pages 10 to 20 form part of these financial statements

LPFI LIMITED

Statement of Financial Position

As at 31 March 2017

	Note	As at 31 March 2017 £	As at 31 March 2016 £
Current assets			
Trade and other receivables	6	13,246	-
Cash and cash equivalents	7	70,661	1
Total current assets		83,907	1
Total assets		83,907	1
Equity and Liabilities			
Equity attributable to equity holders of the parent			
Share capital	10	50,000	1
Retained earnings	11	432	-
		50,432	1
Liabilities			
Non-current liabilities			
Trade and other payables	9	16,000	-
Total non-current liabilities		16,000	-
Current liabilities			
Trade and other payables	8	17,475	-
Total current liabilities		17,475	-
Total liabilities		33,475	-
Total equity and liabilities		83,907	1

The financial statements were authorised for issue by the Board of Directors on 2017 and were signed on its behalf by:

.....
Director

Registered number SC497542

The accompanying notes on pages 10 to 20 form part of these financial statements

LPFI LIMITED

Statement of Changes in Equity

As at 31 March 2017

	Note	Share Capital £	Retained Earnings £	Total £
Share movements				
Share allotted upon incorporation	10	1	-	1
Comprehensive income				
Profit for the year		-	-	-
Balance at 31 March 2016		<u>1</u>	<u>-</u>	<u>1</u>

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2016		1	-	1
Comprehensive income				
Profit for the year		-	432	432
Share movements				
Shares allotted during the year	10	49,999	-	49,999
Balance at 31 March 2017		<u>50,000</u>	<u>432</u>	<u>50,432</u>

LPFI LIMITED
Statement of Cash Flows

For the year ended 31 March 2017

	2017	2016
	£	£
Cash flow from operating activities:		
Profit for the year	432	-
Changes in assets and liabilities:		
Increase in receivables and other financial assets	(13,246)	-
Increase in payables	17,475	-
Cash flows from operating activities	4,661	-
Cash flow from financing activities:		
Loans from group entities	16,000	-
Share capital issued	49,999	1
Net cash flows from financing activities	65,999	1
Net increase in cash and cash equivalents	70,660	1
Cash and cash equivalents at beginning of year	1	-
Cash and cash equivalents at end of year	70,661	1
Cash at bank and in hand	70,661	1

The accompanying notes on pages 10 to 20 form part of these financial statements

LPFI LIMITED

Notes to the Financial Statements

For the year ended 31 March 2017

1. Statement of significant accounting policies

The financial statements of LPFI Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU), IFRIC Interpretations and the Companies Act 2006 applicable to companies reporting under IFRS.

Adoption of new and revised standards

The Company has adopted the following new and amended IFRSs as of 1 April 2016.

- IAS1, Presentation of Financial Statements
- IAS19, Employee Benefits
- IFRS7, Financial Instruments: Disclosures

None of these have materially impacted the financial statements of the company.

Guidance in issue but not in force

IAS 8 requires disclosure of guidance in issue but not in force. The minimum disclosure relates to guidance issued by 31 March 2017, and with potential effect.

International Accounting Standards and Interpretations	Effective for annual periods beginning on or after
IAS 7, Statement of Cash Flows*	1 January 2017
IAS 12, Income Taxes*	1 January 2017
IAS 39, Financial Instruments: Recognition and Measurement	1 January 2018
IFRS 7, Financial Instruments: Disclosures	1 January 2018
IFRS 9, Financial Instruments	1 January 2018
IFRS 15, Revenue from Contracts With Customers	1 January 2018
IFRS 16, Leases*	1 January 2019

*Not yet adopted for use in the European Union

The directors have reviewed the requirements of the new standards and interpretations listed above and they are not expected to have a material impact on the company's financial statements in the period of initial application.

Basis of preparation

The financial statements are presented in Sterling (£) as that is the company's functional currency and the currency in which the majority of the company's accounting policies.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the company's accounting policies.

The following significant accounting policies, which are consistent with the previous period unless otherwise stated, have been adopted in the preparation of this report:

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

1. Statement of significant accounting policies (continued)

a. Going concern

The directors are of the opinion that the company has adequate resources to enable it to undertake its planned activities for a period of at least one year from the date that the financial statements are approved.

b. Current and deferred income tax

The charge for income tax expense for the year is based on the profit for the year adjusted for any non-assessable or disallowed items. It is calculated using tax rates that have been enacted or are substantively enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred income tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

c. Impairment

The carrying value of all assets are reviewed for impairment at each reporting date, with the recoverable amount being estimated when events or changes in circumstances indicate that the carrying value may be impaired.

The recoverable amount of all assets is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which it belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of the asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

LPMI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

1. Statement of significant accounting policies (continued)

d. Cash and cash equivalents

For the purposes of the statement of cash flows, cash includes cash on hand and at call deposits with banks or financial institutions, investments in money market instruments maturing within less than two months and is net of bank overdrafts.

e. Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty.

Revenue is derived wholly from the provision of FCA-regulated service in the United Kingdom. Revenue from a contract to provide services is recognised by reference to the stage of completion of the contract. The stage of completion of the contract is determined with reference to contractual rates as labour hours and direct expenses are incurred.

All revenue is stated net of the amount of value added tax (VAT).

f. Value added tax

Revenues, expenses and assets are recognised net of the amount of value added tax (VAT), except:

- i. Where the amount of VAT incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
- ii. For receivables and payables, which are recognised inclusive of VAT.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Cash flows are included in the statement of cash flows on a gross basis. The VAT component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

g. Share capital

Ordinary shares are classified as equity.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

1. Statement of significant accounting policies (continued)

h. Financial instruments

Financial assets and financial liabilities are recognised when the company has become party to the contractual provisions of the instrument.

Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is recognised in the statement of comprehensive income.

Trade payables

Trade payables are initially recognised at fair value and subsequently at amortised cost using the effective interest method.

Financial liabilities

Financial liabilities are classified according to the substance of the contractual arrangements entered into.

An instrument will be classified as a financial liability when there is a contractual obligation to deliver cash or another financial asset to another enterprise.

Loans

All interest bearing loans and other borrowings are initially recorded at fair value, which represents the fair value of the consideration received, net of any issue costs associated with other borrowings. Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs.

Finance charges, including premiums payable on settlement or redemption, are accounted for on an amortised cost basis to the statement of comprehensive income using the effective interest method, being recognised in the statement of comprehensive income over the term of such instruments at a constant rate on the carrying amount of the instrument to the extent that they are not settled in the year in which they arise.

Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

i. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

j. Critical accounting estimates and judgements

The directors evaluate estimates and judgements incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the company. The directors are satisfied that the accounting policies are appropriate and that there are no significant estimates or judgements used in the preparation of the financial statements.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

2. Profit from operations

	2017	2016
	£	£
Profit from operations has been determined after deducting:		
Auditors' remuneration:		
Audit services	3,250	-
Non-Audit services	1,600	-
	1,600	-

3. Finance costs

	2017	2016
	£	£
Loan interest payable to group entities (note 13)	100	-
	100	-

4. Corporation tax charge

	2017	2016
	£	£
Current tax:		
Corporation tax charge	108	-
	108	-
Tax on profits for the year	108	-
	108	-

Corporation tax expense is calculated at 20% of the assessable profits for the year.

The charge for the year can be reconciled to the profit per the income statement as follows:

	2017	2016
	£	£
Profit for the year before taxation	540	-
	540	-
Profit for the year at the effective rate of corporation tax of 20% (2016 – 20%)	108	-
	108	-

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 December 2017

5. Employee Benefits Expense

The aggregate payroll costs for the year consisted of fees paid to a non-executive director who was appointed during the year. These were as follows:

	2017	2016
	£	£
Wages and salaries	2,000	-
Social security costs	89	-
	2,089	-
	2,089	-

No pension benefits were accrued by the director during the year. All other staff are employed by LPFE Limited, a company under common control, and an appropriate portion of their employment costs recharged. All other directors are employed by LPFE Limited, a company also under the control of Lothian Pension Fund (administered by the City of Edinburgh Council), and the City of Edinburgh Council. In addition to the payroll costs noted above, the company was also charged £2,344 (2016: £nil) for services provided by directors employed by LPFE Limited during the year.

6. Trade and other receivables

	2017	2016
	£	£
Trade debtors	3,988	-
Prepayments	9,258	-
	13,246	-
	13,246	-

The directors consider the fair value of receivables to be in line with carrying values.

7. Cash and cash equivalents

	2017	2016
	£	£
Cash at bank and in hand	70,661	-
	70,661	-

8. Trade and other payables

	2017	2016
	£	£
Accruals	5,745	-
Social security and other taxes	4,233	-
Corporation tax	87	-
Amounts due to group entities	7,410	-
	17,475	-
	17,475	-

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 December 2017

9. Non-current liabilities

	2017	2016
	£	£
Amounts due to group entities	16,000	-
	16,000	-
	16,000	-

10. Share Capital

	2017	2016
	£	£
<i>Allotted, called up and fully paid</i> Ordinary shares of £1 each	50,000	1
	50,000	1
	50,000	1

The company issued 49,999 Ordinary shares of £1 each during the year at par value.

11. Reserves

	Retained Earnings
	£
Profit for the period	-
At 31 March 2016	-
Profit for the year	432
At 31 March 2017	432

12. Controlling interest

The City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) owns all the issued share capital of the company. The company itself has been established to support the administration of the Lothian Pension Fund. Administering authorities are required to prepare separate financial statements for the Local Government Pension Scheme funds that they administer and so it is considered appropriate to consolidate the company's individual financial statement into Lothian Pension Fund's consolidated financial statements.

Group accounts are available to the public from the following address:

Account Dept.
Lothian Pension Fund
Atria One
144 Morrison Street
Edinburgh
EH3 8EX

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 December 2017

13. Related parties

	2017	2016
	£	£
Lothian Pension Fund (pension fund administered by City of Edinburgh Council)		
Staff and other cost recharges	360	-
Payables at the period end	360	-
Loan facility balance payable at the period end	16,000	-
Interest payable during the period	100	-
Interest payable but still accruing at the period end	89	-
LPFE Limited (company under common control)		
Staff and other cost recharges	6,940	-
Payables at the period end	6,940	-
Balance payable for group tax losses utilised	21	-

The company has a loan facility agreement with Lothian Pension Fund for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the company returns any cash not immediately required and this can result in short periods when the company has returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Compensation paid in relation to key management personnel during the period was as follows:

	2017	2016
	£	£
Short-term benefits	2,000	-
	2,000	-
	2,000	-

All other key management personnel are employed by LPFE Limited, a company also under the control of Lothian Pension Fund (administered by the City of Edinburgh Council), and the City of Edinburgh Council. In addition to the compensation noted above, the company was also charged £2,344 (2016: £nil) for services provided by key management personnel employed by LPFE Limited during the year.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

14. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable.

The company did not enter into any transactions that would be classed derivative financial instruments during the period.

The totals for each category of financial instruments, measured in accordance with IAS 39 and detailed in the accounting policies, are as follows:

	Note	2017 £	2016 £
Financial Assets			
Cash and cash equivalents	7	70,661	-
Trade and other receivables	6	13,246	-
		<hr/>	<hr/>
Total Financial Assets		83,907	-
		<hr/> <hr/>	<hr/> <hr/>
Financial Liabilities			
Current liabilities - Trade and other payables	8	17,475	-
Non-current liabilities - Trade and other payables	9	16,000	-
		<hr/>	<hr/>
Total Financial Liabilities		33,475	-
		<hr/> <hr/>	<hr/> <hr/>

Financial Risk Management Policies

The company aims to manage its overall capital structure to ensure it continues to operate as a going concern. The company's capital structure represents the equity attributable to the shareholders of the company together with cash equivalents.

The Board is charged with the overall responsibility of establishing and monitoring the company's risk management policies and processes in order to identify, analyse and monitor the risks that are faced by the company. The company does not enter into or trade financial instruments for speculative purposes.

The main risks that the company is exposed to through its financial instruments are credit risk, liquidity risk and market risk. These are managed as follows:

a. Credit risk

Exposure to credit risk relating to financial assets arises from the potential non-performance by counterparties of contractual obligations that could lead to a financial loss to the company.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance sheet date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the Statement of Financial Position and notes to the financial statements. As at 31 March 2017 none of the company's financial assets were past due or impaired.

Credit risk is managed and reviewed regularly by senior management. It mainly arises from amounts owed by customers. Given the financial stature of its customers the credit risk faced by the company is considered to be very small.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2017

14. Financial Risk Management (continued)

b. Liquidity Risk

Liquidity risk arises from the possibility that the company might encounter difficulty in settling its debts or otherwise meeting its financial obligations as they fall due. The company manages this risk through the following mechanisms:

- preparing forward-looking cash flow analysis in relation to its operational, investing and financing activities; and
- ensuring that adequate unutilised borrowing facilities are maintained.

The tables below reflect an undiscounted contractual maturity analysis for financial liabilities.

Financial liability and financial asset maturity analysis

	Note	Within 1 Year 2017 £	1 to 5 Years 2017 £	Total 2017 £
Financial liabilities due for payment				
Trade and other payables	8	(17,475)	(16,000)	(33,475)
		<u>(17,475)</u>	<u>(16,000)</u>	<u>(33,475)</u>
Financial assets — cash flows realisable				
Cash and cash equivalents	7	70,661	-	70,661
Trade and other receivables	6	13,246	-	13,246
		<u>83,907</u>	<u>-</u>	<u>83,907</u>
Total anticipated inflows		<u>83,907</u>	<u>-</u>	<u>83,907</u>
		<u>66,432</u>	<u>(16,000)</u>	<u>50,432</u>
Net inflow of financial instruments		<u>66,432</u>	<u>(16,000)</u>	<u>50,432</u>

Cash flows realised from financial assets reflect management's expectation as to the timing of realisation. Actual timing may therefore differ from that disclosed. The timing of cash flows as presented in the table (to settle financial liabilities) reflects the earliest contractual settlement dates.

The company has been granted a £75,000 unsecured revolving loan facility by its parent, The City of Edinburgh Council. The ceiling of the facility has been set at a level to ensure sufficient cash is available to meet the company's short-term cash flow needs, should there be a delay in customers settling invoices for services provided.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the period ended 31 March 2017

14. Financial Risk Management (continued)

c. Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the company's financial position. The company has no direct exposure to movements in foreign exchange or equity prices, and has very little exposure to interest rate movements, due to the low level of borrowing. The company monitors this risk but the directors are of the opinion that it is very unlikely to have a significant effect on the company's financial position.



Scott-Moncrieff
Exchange Place,
3 Semple Street
Edinburgh
EH3 8BL

Dear Sirs

Lothian Pension Funds

This representation letter is provided in connection with your audit of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund Annual Report and Financial statements for the period ended 31 March 2017 for the purpose of expressing an opinion as to whether the financial statements show a true and fair view of the financial transactions of the Funds during the period from 1 April 2017 to 31 March 2017 and of the amount and disposition at that date of its assets and liabilities (other than liabilities to pay pensions and benefits after the end of the period) in accordance with Part VII of the Local Government (Scotland) Act 1973 and International Financial Reporting Standards as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 and making a statement about contributions.

By a resolution of the board, passed today, I am directed to confirm to you, in respect of the financial statements of the Funds for the period ended 31 March 2017 the following:-

1. We have fulfilled our responsibilities for preparing financial statements which give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 and for making accurate representations to you.
2. We have provided you with:
 - access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - additional information that you have requested from us for the purpose of the audit; and
 - unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
3. All transactions have been recorded in the accounting records and are reflected in the financial statements.
4. We acknowledge as trustees our responsibilities for the design and implementation of internal control in order to prevent and detect fraud and to prevent and detect error.
5. We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity and involves:
 - management
 - employees who have significant roles in internal control
 - others where the fraud could have a material effect on the financial statements.
6. We are not aware of any allegations of fraud or suspected fraud with a potential effect on the financial statements which have been communicated to us by employees, former employees, regulators or other third parties.

7. We have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations, whose effects should be considered when preparing the financial statements.
8. We confirm that, in our opinion, the assumptions that have been used in determining fair values, whether such values are disclosed or applied in the financial statements, are reasonable and reflect our ability and intent to carry out specific courses of action, where this is relevant to the determination of those values.
9. In our opinion the significant assumptions used by us in making accounting estimates are reasonable.
10. Where required, the value at which assets and liabilities are recorded in the net assets statement is, in the opinion of the trustees, the market value. We are responsible for the reasonableness of any significant assumptions underlying the valuation, including consideration of whether they appropriately reflect our intent and ability to carry out specific courses of action on behalf of the Funds. Any significant changes in those values since the accounting reference date have been disclosed to you.
11. We have disclosed to you the identity of the company's related parties and all related party relationships and transactions of which we are aware.
12. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of International Financial Reporting Standards as adopted by the European Union.
13. In particular, no trustee, shadow trustee, their connected persons or other officers had any indebtedness, agreement concerning indebtedness or disclosable interest in a transaction with the Funds at any time during the year.
14. The following have been properly recorded and, when appropriate, adequately disclosed in the financial statements:
 - losses arising from sale and purchase commitments;
 - agreements and options to buy back assets previously sold;
 - assets pledged as collateral.
15. We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.
16. We have no plans to abandon activities or other plans or intentions that will result in any excess or obsolete stocks, and no stock is stated at an amount in excess of net realisable value.
17. The Funds have satisfactory title to all assets and there are no liens or encumbrances on the Funds' assets, other than as disclosed in the financial statements.
18. We have recorded or disclosed, as appropriate, all liabilities, both actual and contingent, and all guarantees that we have given to third parties.
19. All events subsequent to the date of the financial statements and for which International Financial Reporting Standards as adopted by the European Union require adjustment or disclosure have been adjusted or disclosed. Should any material events occur which may necessitate revision of the figures included in the financial statements or inclusion in the notes thereto, we will advise you accordingly.
20. The Funds have complied with all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance.
21. To the best of our knowledge and belief, the information disclosed in the financial statements in respect of parties which control the Funds is complete and accurate.
22. Except as disclosed in the financial statements, the results for the year were not materially affected by:
 - any change in accounting policies;
 - transactions of a type not usually undertaken by the Funds I group;
 - circumstances of an exceptional or non-recurrent nature; or
 - charges or credits relating to prior periods.
23. There is no pending or potential litigation against the Funds and there are no contingencies of a material amount for which provision has not been made in the financial statements.

24. We confirm that we have reviewed going concern considerations and are satisfied that it is appropriate for the financial statements to have been drawn up on the going concern basis. In reaching this opinion we have taken into account all relevant matters of which we are aware and have considered a future period of at least one year from the date on which the financial statements were approved.
25. We confirm that the effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial statements. A list of uncorrected misstatements is attached to the representation letter.

Yours faithfully

.....

John Burns

Chief Finance Officer (Section 95 Officer for the Pension Funds)

Pensions Audit Sub Committee

2.00pm, Tuesday, 26 September 2017

Fraud Prevention

Item number	5.4
Report number	
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for all

Executive Summary

The purpose of this report is to enable the Pensions Audit Sub-Committee to review and scrutinise the work undertaken by Lothian Pension Fund to prevent fraud. The report provides details of participation in fraud prevention initiatives as an integral part of the control environment and the overall management of risk.

Pensioner existence is one of the biggest fraud risks. Participating in the National Fraud Initiative (NFI) and matching of records with the General Registrar's Office ensures unnotified deaths are dealt with quickly. The Fund also uses Western Union to verify that overseas pensioners are alive. The Local Government Association (LGA) developed a service that enables all Local Government Pension Funds access to "Tell us Once", a national application of registering a birth or death. The LGA database has two purposes, (i) to prevent the payment of duplicate death grants and (ii) to enable LGPS to join the Tell Us Once Service. Lothian Pension Fund has been informed of deaths through the Tell Us Once Service since April 2017.

Fraud Prevention

1. Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider;
- 1.2 Note the report and highlight any points it would like to raise at the Pensions Committee on 27 September 2017.

2. Background

- 2.1 An annual update on fraud prevention is reported to Pensions Audit Sub Committee.
- 2.2 The pensions administration team deliver services to members using a browser based pension software system. The software stores and controls all aspects of the membership database, document management and benefit calculations. Access is restricted to authorised individuals by user identification and password protection. In addition, the Fund's compliance policy includes the restriction that members of staff should not be involved in the computation or checking benefits payable to a member who is a connected person.
- 2.3 The operation of internal controls also gives comfort that the risk of fraud is mitigated or minimised. Procedural controls include:
 - obtaining original relevant certificates;
 - if any beneficiary of a lump sum death grant is a Minor (under age 16), and their share is over £5000, the payment must be referred to the Accountant of Court. If their share is under £5,000 their parent or guardian must set up a Trust Fund. The parent or guardian must also evidence that they are capable and have the appropriate capacity to act in the best interests of the minor;
 - authorisation of payments in line with the Council's Scheme of Delegation.
- 2.4 The Fund processes one-off payments to members and nominated third parties, such as solicitors and dependents. Controls ensure that payments are made to authorised recipients only and that all payments are authorised in line with the Scheme of Delegation. All member movements (for example active member to pensioner member status) are reconciled against financial transactions on a monthly basis.

3. Main report

- 3.1 **The National Fraud Initiative (NFI)** is a well-established data matching exercise, led by Audit Scotland, which is carried out every two years. It is designed to help organisations identify causes of fraud and detect and correct any consequential overpayments from the public purse. The matching exercises undertaken include a comparison of public sector records to death records and other pension related outcomes, for example, when retirees have returned to work but not reported circumstances that require their pension to be reduced. For the first time in 2016/17, the data match exercise included a match against deferred pensioners (not currently in payment). Costs are met through the annual audit fee. The 2016/17 data match against current pensioners and deferred pensioner identified 15 and 26 deaths respectively, that had not been reported. The matches are currently being investigated.
- 3.2 **The “Tell Us Once” service** has been available to public service pension schemes since March 2016. The Local Government Association (LGA) on behalf of all Local Government Pension Schemes (LGPS) across the UK holds a central database, known as the “National Insurance (NI) database”. Should a match between an NI Number on the LGPS NI database occur the relevant LGPS Fund is notified that data relating to a death of one of their members is available for it to access. Lothian Pension Fund has participated in the Tell Us Once service from April 2017. Up until 31 August 2017, 101 death notifications have been received through the service.
- 3.3 On a quarterly basis, Lothian Pension Fund continues to match its records to the **General Registrar’s Office for Scotland (GRO)**. Undertaking this exercise highlights cases promptly. As Lothian Pension Fund is now participating in the Tell Us Once service, the Fund will undertake a review at the end of the year to consider if the GRO matching exercise is still required.
- 3.4 Since last year, the Fund has undertaken an overseas pensioner **existence check in partnership with Western Union** and its network of agents. There are 159 overseas pensioners with an overseas bank account who must verify that they are alive by means of a face-to-face meeting at which they must produce a valid form of identification, such as a passport or driving licence. In this year’s exercise, overseas pensioners had until 31 August 2017 to complete the procedure. Three pensioners have not yet completed the existence check and consequently payment of their pensions has been suspended. A second existence check designed to cover pensioners living overseas who have their pension paid to a UK bank account was carried out in November 2016. There are 208 overseas pensioners with an UK bank account. The pensioner was required to follow the same Western Union process. Following the exercise 9 members initially had their pension suspended. Of those 4 remain suspended and under investigation at present. The exercise will be carried out again in November 2017.
- 3.5 The Fund continues to exercise its discretion as to whether to approve transfers to prevent “**pension liberation**” scams. While the Pension Regulator has issued

guidance in terms of identifying potential cases of liberation fraud, it places the onus on the pension funds themselves to have sufficient procedures in place to identify any suspicious practices and properly exercise their discretion as to whether to approve a transfer. Therefore, the Fund has a procedure which involves additional levels of diligence/enquiry of the member and the proposed transferee scheme. This is to ensure that any decisions to approve these types of transfer can be as informed as possible, are clearly documented and to assert that we are sending a clear external message that these transfers are not being approved as a matter of course. Over the period 1 September 2016 – 31 August 2017, Lothian Pension Fund received 57 transfer requests to a Defined Contribution (DC) Scheme. No transfer payments were rejected.

- 3.6 At Spring Budget 2017, the UK Government announced a new 25% overseas transfer charge to some overseas pension transfers that were previously tax free. This will reduce the attractiveness of an overseas transfer.
- 3.7 During 2015/16, the Fund undertook a trial period with of the” **CallValidate**” product. CallValidate checks member’s names and addressed against their bank account. The trial highlighted a fundamental weakness in that CallValidate could only accurately match bank accounts opened after 1990. However, during 2016/17 CallValidate enhanced their product to include “Bank Account Premium”. Bank Account Premium allows a check against older bank accounts. Since January 2017, Lothian Pension Fund carries out a bank validation check on all new pensioners and when a change to a pensioner’s bank account is received.

4. Measures of success

- 4.1 Lothian Pension Fund is committed to deter and ultimately prevent fraud. Suitable controls are in place and subject to regular scrutiny. Should any fraud be detected, however, immediate action is taken to prevent further losses and recover any overpayment.

5. Financial impact

- 5.1 The Lothian Pension Fund budget includes expenditure for fraud prevention. Staff resource is met within the existing budget for pension administration employee costs.

6. Risk, policy, compliance and governance impact

- 6.1 There are no adverse risk, policy, compliance or governance impacts arising from this report.

7. Equalities impact

7.1 There are no adverse equalities impacts rising from this report.

8. Sustainability impact

8.1 There are no adverse sustainability impacts arising from this report.

9. Consultation and engagement

9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

10. Background reading/external references

10.1 None

Stephen S. Moir

Executive Director of Resources

Contact: John Burns, Chief Finance Officer, Lothian Pension Fund

E-mail: john.burns@edinburgh.gov.uk | Tel: 0131 469 3711

11. Appendices

None.

Pensions Audit Sub Committee

2.00pm, Tuesday, 26 September 2017

Irrecoverable overpayment of pensions – decisions made under delegated authority

Item number	5.5
Report number	
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for all

Executive Summary

This report advises Pensions Audit Sub Committee of pension overpayments, during the period 1 September 2016 to 31 August 2017, which have been deemed irrecoverable by the Executive Director of Resources, in accordance with the Council's "Scheme of Delegation to Officers".

Irrecoverable overpayment of pensions – decisions made under delegated authority

1. Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider;
- 1.2 Note that the total value of pension overpayments written off between 1 September 2016 and 31 August 2017 is £8,128.39; and
- 1.3 Highlight any points it would like to raise at the Pensions Committee on 27 September 2017.

2. Background

- 2.1 Delegated authority has been granted to the Executive Director of Resources, in certain circumstances, to write-off pension overpayments up to £3,000. Any overpayments above this limit require approval of the Pensions Committee.

3. Main report

- 3.1 Pension regulations determine the calculation and payment of pension benefits to scheme members. During the process of administration, overpayments of pension may occur upon the death of a pensioner, where pensioners return to work when receiving a pension (this only affects people who retired on the grounds of efficiency and received compensatory added years when they retired) or where a mistake occurs.
- 3.2 Attempts are made to recover overpayments over £250. Occasionally, however, it may not be in the best interest of the Fund to seek recovery of an overpaid pension. Depending on the circumstances of the particular case, in line with delegated functions, certain officers in the Investment & Pensions division may write off the whole or part of an overpayment up to £3,000. The most likely circumstances would be if recovery would cause undue hardship to the member's family, if there are insufficient funds to repay the overpayment or it is uneconomical to pursue. Any overpayments over £3,000 are referred to the Pensions Committee.
- 3.3 The value of pension overpayment write offs between 1 September 2016 and 31 August 2017 is shown below. The total value is £8,128.39.

	Date of Death	Amount	Reason for write-off	Date of write-off
Member A	N/A	£22.50	The Fund did not amend the short-term pension amount to the long-term pension amount. The payment was written off due to the small amount.	12/09/2016
Member B	20/05/2011	£1,084.22	The Fund was unable to ascertain the address of a relative or the next-of kin.	21/09/2016
Member C	25/08/2014	£888.02	The overpayment was not recovered despite contacting the next of kin several times. An assisted funeral was arranged. The overpayment was written off as uneconomical to pursue.	25/10/2016
Member D	26/01/2015	£390.97	The overpayment was written off despite attempts to recover through debt recovery.	18/01/2017
Member E	24/06/2015	£265.38	The acting solicitor advised that the Estate had been wound up.	19/01/2017
Member F	20/10/2015	£2,254.11	The death was identified through General Registrar's Office (GRO) screening. The member was homeless and the death was reported by the Police. Despite several attempts to find a next of kin we were unable to collect the overpayment.	03/02/2017
Member G	01/04/2016	£329.54	The death was identified through GRO. In the context of a complaint regarding poor service being upheld, a decision was made to write off the overpayment.	10/02/2017
Member H	18/11/2014	£2,510.11	The overpayment was written off following unsuccessful attempts to pursue debt recovery.	20/02/2017
Member I	21/07/2016	£31.60	The Fund made a mistake in the calculation of the balance of pension	27/03/2017

	Date of Death	Amount	Reason for write-off	Date of write-off
			payable to the Estate. The payment was written off due to the small amount	
Member J	06/09/2016	£351.94	The death was identified through the National Fraud Initiative (NFI) 2016/17. The next of kin died shortly after.	09/08/2017

- 3.4 Any overpayment of pension is charged to the respective fund, namely the Lothian Pension Fund, the Lothian Buses Pension Fund or the Scottish Homes Pension Fund.
- 3.5 The NFI 2016/17 data match against current pensioners identified 15 deaths. The matches are currently being investigated. Lothian Pension Fund is also reviewing repayment terms previously agreed, for example when abatement applied when a pensioner took up further employment. It is likely that the amounts due will not be fully recovered under current repayment terms.

4. Measures of success

- 4.1 Not applicable

5. Financial impact

- 5.1 As the expenditure has already been reflected in the relevant financial statements of the Lothian Pension Funds, there is no additional financial impact arising from the overpayment of pensions.

6. Risk, policy, compliance and governance impact

- 6.1 There are no adverse risk, policy, compliance or governance impacts arising from this report.

7. Equalities impact

- 7.1 There are no adverse equalities impacts arising from this report.

8. Sustainability impact

8.1 There are no adverse sustainability impacts arising from this report.

9. Consultation and engagement

9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

10. Background reading/external references

10.1 None.

Stephen S. Moir

Executive Director of Resources

Contact: John Burns, Chief Finance Officer, Lothian Pension Fund

E-mail: john.burns@edinburgh.gov.uk | Tel: 0131 469 3711

11. Appendices

None

Pensions Audit Sub Committee

2.00pm, Tuesday, 26 September 2017

Overpayment of Pension

Item number	5.6
Report number	
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for all

Executive Summary

This report highlights that Pensions Committee will be asked not to pursue recovery of overpayment of pensions totalling £34,563.21.

Overpayment of Pension

1. Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider; and
- 1.2 Note the report and highlight any points it would like to raise at the Pensions Committee on 27 September 2017.

2. Background

- 2.1 Delegated authority has been granted to the Executive Director of Resources, in certain circumstances, to write-off pension overpayments up to £3,000. Any overpayments above this limit require approval of the Pensions Committee.

3. Main report

- 3.1 This report details two instances where overpayment of pension has arisen following the death of a member.
- 3.2 The first case refers to a suspected fraud, details of which were reported to Pensions Audit Sub-Committee at its meeting on 27 September 2016.
- 3.3 The relevant extract from that report is as follows:
- 3.4 “Despite the Fund undertaking regular mortality screening checks, the National Fraud Initiative (NFI) 2014/15 did identify a member as being deceased since 23 July 2003. In this particular case, a match had also been made in NFI 2004/05 and 2008/09. In previous years, a “Life Certificate” was sent to ascertain whether or not the pensioner was alive and these were completed and returned, validated by another person. When a match was again made in 2014/15, the case was scrutinised in further detail and an incident raised with Police Scotland for investigation. An overpayment of £31,519.52 has occurred and Police Scotland has submitted a report to the Procurator Fiscal (in July 2016). (Although the Fund also matches its records to the General Registrar’s Office for Scotland, volumes restrict the Fund to looking at “good” matches. In this particular case, there was an anomaly in the initials of the individual member. It has since been ascertained that this case appeared in the “possible” matches).”

- 3.5 In July 2017, the Fund was advised that the Procurator Fiscal had determined that there was insufficient evidence to proceed with criminal charges.
- 3.6 In the second case, a member died on 12 January 2012. Lothian Pension Fund, however, was not informed and continued to pay the member's pension until May 2013. An overpayment of pension arose over the period amounting to £3,043.69.
- 3.7 The Fund contacted the member's daughter as she had registered the death. The daughter advised that she had been estranged from her mother and other family members were dealing with the estate. In February 2014, the Fund instructed the City of Edinburgh Council's Debt Recovery Division to pursue settlement on its behalf. In July 2017, the Fund was advised that Scott and Company, Sheriff Officers, acting for the Council, had deemed the case "uneconomical to proceed with further recovery".
- 3.8 In respect of both these two cases, Pensions Committee, at its meeting on 27 September 2017, will be requested to approve that further debt recovery attempts should not be pursued.

4. Measures of success

- 4.1 Not applicable.

5. Financial impact

- 5.1 As the expenditure has already been reflected in the relevant financial statements of Lothian Pension Fund, there is no additional financial impact arising from the overpayment of pension.

6. Risk, policy, compliance and governance impact

- 6.1 There are no adverse risk, policy, compliance or governance impacts arising directly from this report.
- 6.2 The most common cause of overpayment of pensions is unreported pensioner deaths and re-marriage. Participation in the "Tell Us Once" project should reduce such risk in future. This would not prevent fraud cases, however, where the intention is not to report the death of a member at all. Utilisation of the "CallValidate" product to verify bank account details should also serve to mitigate risk.

7. Equalities impact

- 7.1 There are no adverse equalities impacts arising from this report.

8. Sustainability impact

8.1 There are no adverse sustainability impacts arising from this report.

9. Consultation and engagement

9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

10. Background reading/external references

10.1 None.

Stephen S. Moir

Executive Director of Resources

Contact: John Burns, Chief Finance Officer, Lothian Pension Fund

E-mail: john.burns@edinburgh.gov.uk | Tel: 0131 469 3711

11. Appendices

None.

Pensions Audit Sub Committee

2.00 p.m., Tuesday, 26 September 2017

Risk Management Summary

Item number	5.7
Report number	
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for all

Executive Summary

In line with the pension funds' ongoing risk management procedures, this paper provides an overview of the Fund's risk analysis for consideration by the Committee.

Risk Management Summary

1. Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider; and
- 1.2 Note the Quarterly Risk Overview and highlight any points that it would like raised at the Pensions Committee on 27 September 2017.

2. Background

- 2.1 The pension funds' risk management procedures require the Fund to:
 - 2.1.1 maintain a detailed operational risk register which sets out all the risks identified and assessed by the officers on an ongoing basis, the degree of risk associated in each case and our action to mitigate these risks (the "Operational Risk Register"); and
 - 2.1.2 produce a summary report of the risk register for the Pensions Committee and the Pensions Audit Sub-Committee which highlights the material risks facing the pension funds and identifies any new risks/concerns and the progress being made over time by the officers in mitigating the relevant risks (the "Quarterly Risk Overview").

3. Main report

- 3.1 The Operational Risk Register is issued to the conveners of the Pensions Committee and the Pensions Audit-Sub Committee and the Independent Professional Observer on a quarterly basis.
- 3.2 The Quarterly Risk Overview, as at 16 August 2017, is set out in the appendix to this report for consideration.

4. Measures of success

- 4.1 Improved visibility of the risks facing the pension funds and progress in analysing/mitigating these risks. Regular, focused and relevant risk updates to the Committee should increase general awareness and allow productive analysis/feedback by the Committee members on these fundamental issues.

- 4.2 Ultimately, risk management should lead to less third party exposure, an improved financial position and have a positive impact on the reputation of the pension funds.

5. Financial impact

- 5.1 There are no direct financial implications as a result of this report.

6. Risk, policy, compliance and governance impact

- 6.1 Please see the Quarterly Risk Overview appended to this report.

7. Equalities impact

- 7.1 None.

8. Sustainability impact

- 8.1 None.

9. Consultation and engagement

- 9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

10. Background reading/external references

- 10.1 None

Stephen S. Moir

Executive Director of Resources

Contact: Struan Fairbairn, Chief Risk Officer, Lothian Pension Fund

E-mail: struan.fairbairn@edinburgh.gov.uk | Tel: 0131 529 4689

11. Appendices




Appendix 1 – Quarterly Risk Summary, as at 16 August 2017












QUARTERLY RISK OVERVIEW

16 August 2017

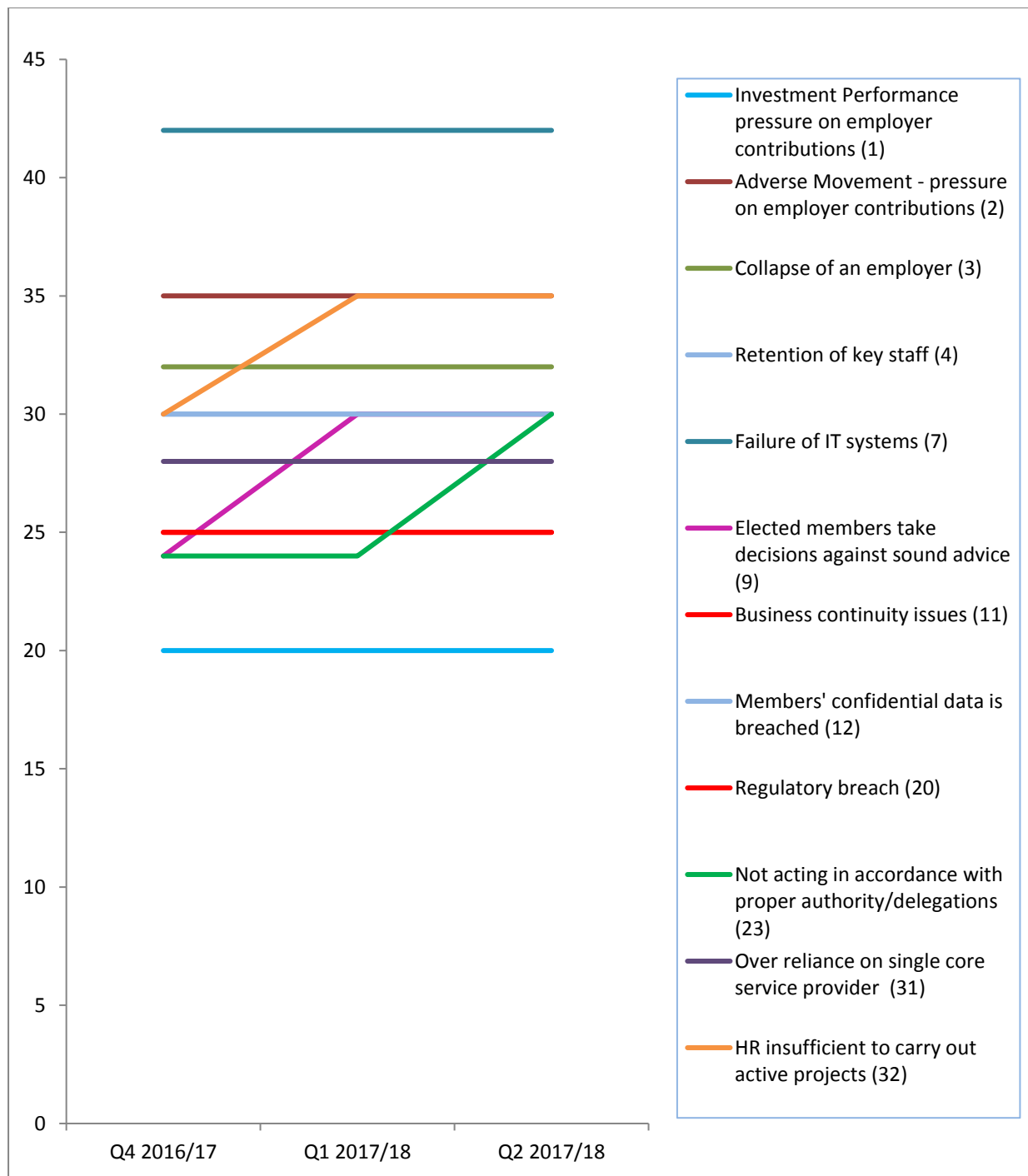
UPDATE ON MOST NOTABLE RISKS

Risk & Reference Number	Update	Trend / RAG
Adverse Investment performance leading to pressure on employer contribution (1)	Implementation of the Lothian Buses Pension Fund strategy is being planned with the Investment Strategy Panel, together with the review of the merger of the Fund with Lothian Buses Pension Fund. Consultation with Employers on the Funding Strategy Statement and implementation of the third Investment Strategy is underway.	Static 
Adverse movement against non-investment funding assumptions leading to pressure on employer contributions (2)	Preparations are underway for the 2017 actuarial valuation. The Contribution stability mechanism will be reviewed again in advance of the 2020 valuation.	Static 
Collapse/restructuring of an employer body leading to pressure on other employers (3)	The funding approach introduced in the 2014 actuarial valuation for employers close to exiting the Fund reduces the overall risk to the Fund and the other employers. The Fund continues to engage with a number of smaller employers regarding the potentially adverse financial impact of the revised funding strategy and to implement the outcomes from the appeals process and the Pensions Committee decision in this regard. Funding Agreements for payment of cessation debt are now in place with a number of the appellants, and others are in process of being finalised. Where appropriate, the Fund will be pursuing guarantees and securities from the employers and updated admission agreements in order to further mitigate this risk.	Static 

Risk & Reference Number	Update	Trend / RAG
Recruitment and retention of key staff (4)	<p>The Fund continues to assess resourcing in light of future collaborative initiatives and the increasingly complex nature of the Fund's business. The Fund is also continuing to closely monitor, in the shorter term, the impact on senior management resource during the negotiation and implementation of these wider collaborative initiatives in addition to increasing levels of business as usual.</p> <p>The Bond Portfolio Manager post is to be re-advertised after the preferred candidate withdrew. The position has been vacant since March 2017 which highlights a recruitment/resourcing risk and the management is engaging with the LPFE Limited (LPFE) board on as part of the wider review. Temporary investment administration support has been secured to help alleviate the continued pressure on resources elsewhere within the investment team.</p> <p>The Fund's management team continue to engage with the LPFE board as part of the wider HR relaunch to coincide with all LPF's staff being employed within LPFE following the phase 2 transfer. This is now scheduled to take place at the end of October 2017.</p>	<p>Static</p> 
Failure of IT leading to poor ICT responsiveness, legal exposure and cost/risk implications (7)	<p>The Fund continues to closely monitor the outcome and process for CEC to embed the new IT provider, CGI, to ensure existing systems and IT will continue to be supported. The Fund is liaising directly with CGI to ascertain options around it having a separate service arrangement to allow for it to have an IT service provision tailored to the its requirements. Addressing this service risk is now an important priority for the Fund as its requirement to implement systems improvements in several key areas will shortly impact on the deliverability of other key business initiatives.</p> <p>The Fund continues to seek a response from CGI on a solution to the Redbox call recording systems issues. This continues to be a priority.</p> <p>The CEC accounts system is still scheduled to be transferred to a new system, which may cause transitional difficulties for the Fund's finance team but with no major impact on the Fund's systems. As reported last quarter, this project has currently been delayed; the date of transfer to the new system is to be confirmed.</p> <p>An internal audit is in progress on 'Payescape', LPFE's new HR & Payroll System.</p>	<p>Static</p> 
Elected member take decisions against sound advice (9)	<p>Induction training for newly appointed members to the Pensions Committee is expected to take place on 13 September 2017, before their first formal meeting.</p> <p>The Fund continues to receive an increasing number of queries or approaches regarding both its investments and on other socio-economic and environmental matters, most recently including a petition to the wider Council. The petition is being referred to Pensions Committee in September. The risk therefore remains on warning given the extent of these approaches and their converging with the introduction of several new members to the Pensions Committee and Pension Board.</p>	<p>Static</p> 
Business continuity issues (11)	<p>The Fund's business continuity plan has been updated and arrangements to test the plan are being prepared with the help of the City of Edinburgh Councils resilience team. The Fund is also ensuring that home-working and relevant health and safety procedures are adhered to across the board and, where necessary, continue to be enhanced in line with current practice.</p>	<p>Static</p> 

Risk & Reference Number	Update	Trend / RAG
	<p>Internal Audit are currently preparing a report on the business continuity measures in place with the suppliers of key services, for example, the pension administration system and investment custody. The results of this will be reported to committee in due course.</p> <p>As above, the position around LPF's IT systems and services is being progressed as a priority.</p>	
Members' confidential data is lost or made public. Breach of Data Protection Act (12)	<p>The Fund is preparing for the onerous Data Protection legislation (the General Data Protection Regulations – GDPR) coming into force in May 2018. In August, the legal and risk team delivered an overview of key changes and training for staff on GDPR.</p>	<p>Static</p> 
Regulatory breach (20)	<p>The implementation of MiFID II within the UK will result in LGPS funds stepping down to Retail Investor status. Although the Fund should be in a strong position to "opt-up" to Professional Investor status, close scrutiny of this continues. The Fund is also monitoring impact of this on other LGPS funds, with whom it may be looking to collaborate.</p> <p>The Fund is also closely monitoring the ongoing collaboration initiatives to ensure regulatory compliance and appropriate systems and governance are in place prior to any subsequent material change in business scope. Moore Stephens are carrying out a regulatory compliance review of the activities of LPFI Limited review of its first collaborative deal. This is also being done in conjunction with a project to enhance the LPF Group's compliance policies and procedures. The report from the initial review has been received and the team are looking to address the points raised prior to the next quarterly audit at the end of September. Feedback on the compliance audits will be included in more extensive reporting on LPFI and LPFE to the Pensions Committee in December.</p>	<p>Static</p> 
Acting out-with proper authority/delegations (23)	<p>Regular updates of the Fund's delegations are required to take into account the staffing changes occurring within the Fund's governance. The most recent of which is the arrival of Stephen Moir as the Executive Director of Resources. This update remains outstanding and so is being put in place as a priority.</p> <p>Further, the Fund is liaising with CEC's governance team in relation to an update to the scheme of delegation to ensure that the reserved powers relating to CEC subsidiaries does not cut across the otherwise overarching delegation of authority for pension fund matters (including those in relation to LPFE and LPFI Limited) to the Pensions Committee.</p>	<p>Increase</p> 
Human Resource within the Division not sufficient to carry out core tasks in conjunction with active or anticipated projects (32)	<p>In light of the significant collaborative, employer and other national initiatives that the Fund is currently involved in, we are closely monitoring the risk that senior management time and other resource is stretched to the point where this adversely impacts on the 'business as usual' processes within the Fund.</p> <p>In addition, the Fund is also reviewing its other corporate services resource (HR, IT etc.) to ensure it is fit for purpose currently and in light of the Fund's development strategy.</p>	<p>Static</p> 

NOTABLE RISKS: PROGRESSION OF CURRENT RISK (ACCOUNTING FOR CONTROLS) IN LAST THREE QUARTERS

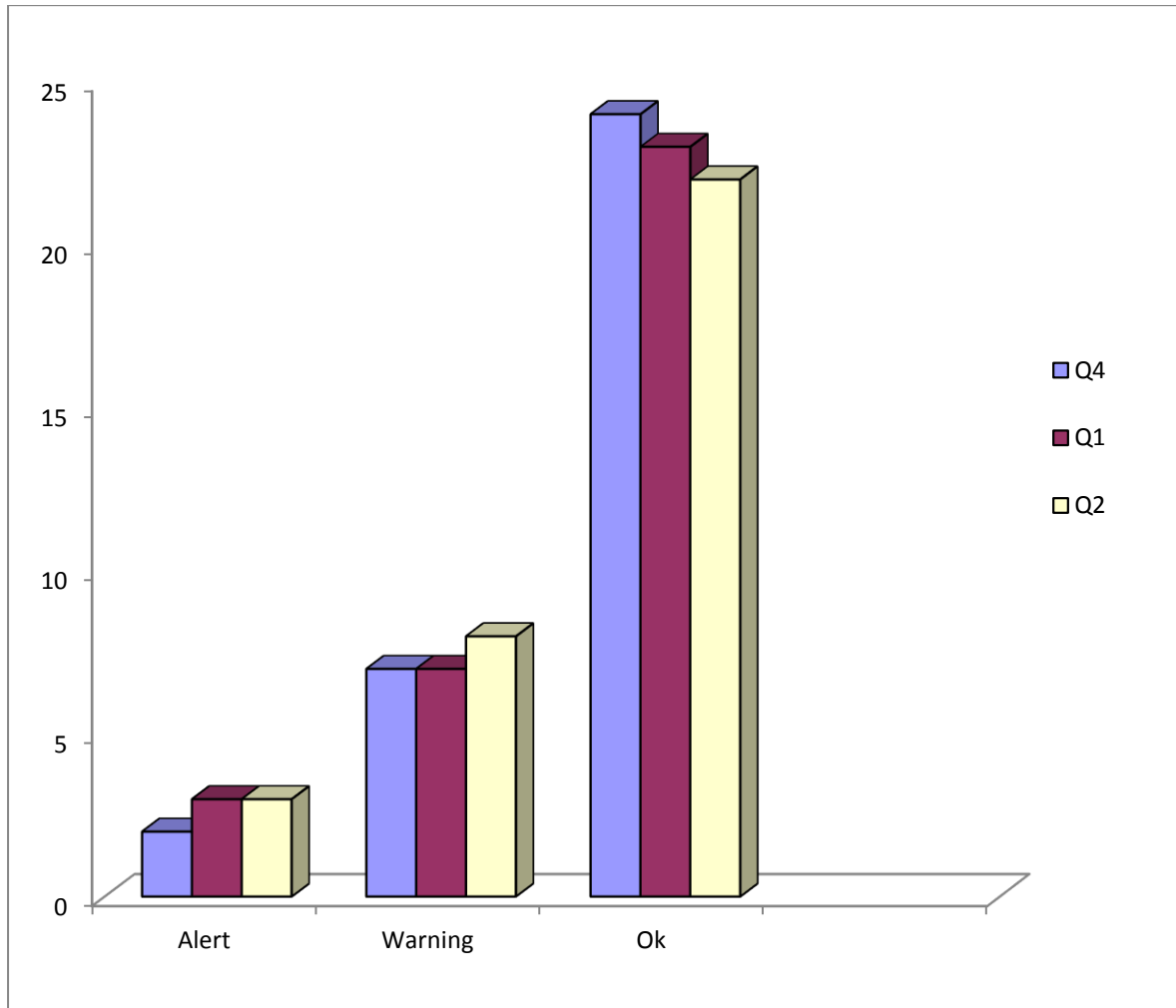


PLEASE NOTE, OVER THE LAST THREE QUARTERS RISK '11 – BUSINESS CONTINUITY' AND RISK '20 – REGULATORY BREACH' HAVE SHARED THE SAME RISK SCORE. IN ADDITION, RISK '12 MEMBERS' CONFIDENTIAL DATA IS LOST OR MADE PUBLIC' AND RISK '4 – RECRUITMENT AND RETENTION OF KEY STAFF' HAVE ALSO SHARED THE SAME RISK SCORE.

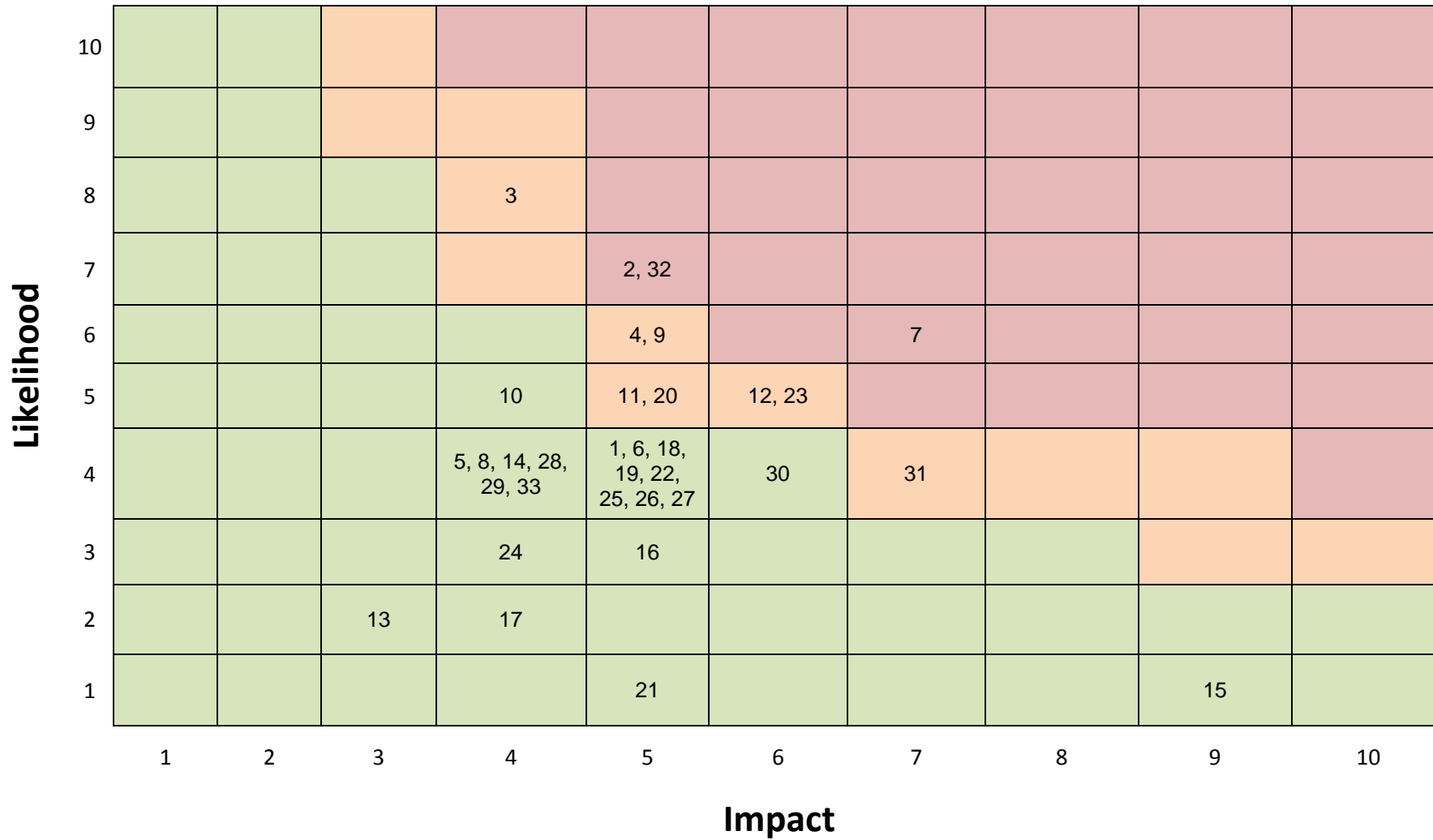
OTHER KEY POINTS

	Comments
New significant risks	None.
Other new risks	None.
New controls	Funding Agreements in place for some employers for payment of cessation debt (3)
Eliminated risks	None.
Notable initiatives / actions	<p>Moore Stephens is engaged on a regulatory compliance audit and the Fund is working to enhance certain of its compliance processes and procedures. (20)</p> <p>The Fund is engaged with CGI to ascertain options around a bespoke IT service provision for the pension fund (7).</p> <p>The Fund continues to monitor the position in relation to the following new regulation: GDPR, MiFID II, new anti-money laundering regulations and changes in the margin requirements for certain derivative transactions. (12, 20)</p> <p>The recently appointed Executive Director of Resources is to be appointed to the board of LPFE Limited. (26)</p> <p>The Fund is looking to train more first aiders and fire wardens to ensure appropriate cover. Also, the Fund is looking to ensure holiday and flexi process is updated to ensure there is always a member of staff with such an official role in the office and co-ordinate this across the teams. (11)</p> <p>The Fund is looking to ensure continuity around access to HR files and other critical business systems and to ensure that each member of staff has two emergency contacts on the system and that there are processes to ensure this remains up to date and accessible to key persons. A test for the business continuity plan is being prepared to check whether the plans are robust. (33)</p>
Material Litigation	None.

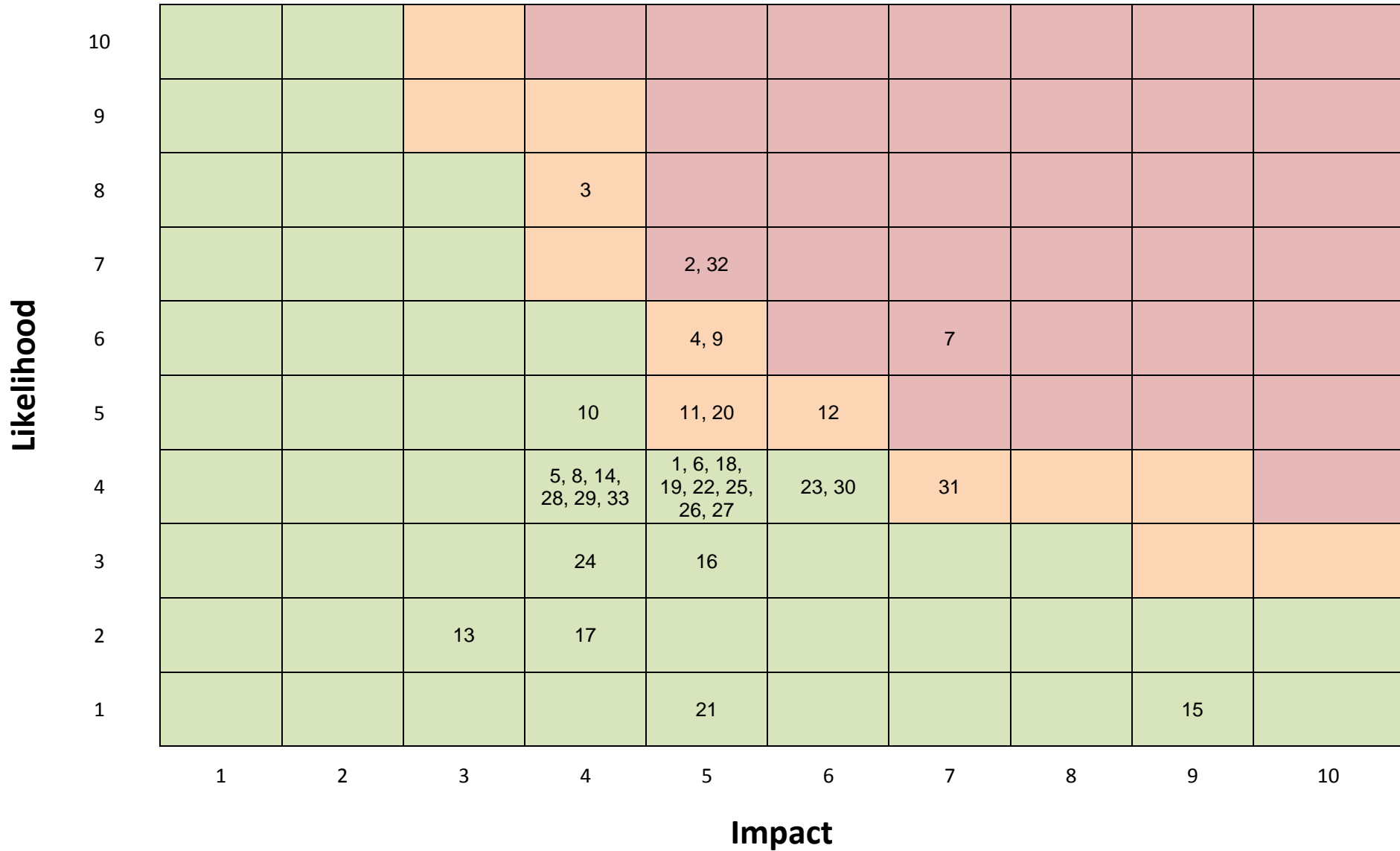
All Risks: Status Overview



Q2 2017/18 All Risks: Impact and Likelihood Overview



Q1 2017/18 - All Risks: Impact and Likelihood Overview



Key: Risks by Number

- 1 Adverse Investment Performance - pressure on employer contributions
- 2 Adverse Movement of non-investment funding assumptions- pressure on employer contributions
- 3 Collapse of an employer
- 4 Recruitment and retention of key staff
- 5 Fraud or theft of Council/Pension Fund assets
- 6 Staff negligence
- 7 Failure of IT systems
- 8 Employers HR decisions without consideration of fund
- 9 Committee members take decisions against sound advice

- 10 Pension Board not operating effectively
- 11 Business continuity issues
- 12 Members' confidential data is breached
- 13 Loss due to stock lending default
- 14 Risk of incorrect pension payments
- 15 Late payment of pension
- 16 Market abuse by investment team or others
- 17 Portfolio transition issues

- 18 Disclosure of confidential information
- 19 Material breach of contract
- 20 Regulatory breach
- 21 FOI process not in accordance with law
- 22 Incorrect communication with members
- 23 Not acting in accordance with proper authority/delegations
- 24 Inappropriate use of pension fund monies
- 25 Procurement/framework breach
- 26 Group Structure and Governance not fully compliant and up to date (including integration of subsidiaries)
- 27 Claim or liability arising from shared services
- 28 Unauthorised access to PensionsWEB
- 29 Incorrect data from Employers leading to fines etc.
- 30 Inadequate contractual protection for services
- 31 Over reliance on single core service provider
- 32 HR insufficient to carry out active projects
- 33 Breach of Health and safety regulations