Pensions Audit Sub Committee

2.00pm, Tuesday, 25 September 2018

Audited Annual Report 2018 of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund, including Annual Report by External Auditor

Item number	5.2
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 2018 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 2017/18 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 2018 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".

Report

Audited Annual Report 2018 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 2017/18 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 2018 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 2018, of both the wholly-owned companies, LPFE Limited and LPFI Limited, were approved by the respective Board of Directors in May 2018. These statements are shown in full at Appendices 3 and 4; and

1.5 Highlight any points that it would like to raise at the Pensions Committee on 26 September 2018.

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 2018 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund at its meeting on 28 June 2018.

3. Main report

Scott-Moncrieff - Lothian Pension Funds 2017/18 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 2017/18 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 Claire Gardiner, Manager, Public Sector Audit, 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 Appendix 1 ("Appendix 1: Management action plan", Pages 33 to 39 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.

3.6 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 2018 for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

3.7 With the completion of the work by Scott-Moncrieff, the Audited Annual Report 2018 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund has been finalised and is included at Appendix 2.

3.8 No numerical adjustments were required to be made to the unaudited financial statements following the Fund's audit. Some presentational changes have been incorporated.

3.9 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 2018; LPFE Limited and LPFI Limited

3.10 The consolidated financial statements (within the Annual Report 2018) combine those of the Fund (the parent entity) and its controlled entities (the investment staffing company, LPFE Limited, and the investment services company, LPFI Limited), as defined in International Accounting Standard (IAS) 27. As reported to Pensions Committee in June 2018, the financial statements of both companies have been audited by Scott-Moncrieff and were approved by the respective Boards of Directors on 28 May 2018. In the interests of governance transparency, these statements are shown in full at Appendices 3 and 4.

3.11 LPFE Limited is the employment vehicle for the Fund's 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 2018, the underlying trading profit of the company was £41,052 (2017: £30,739).

3.12 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". For the year ended 31 March 2018, the underlying trading profit of the company was £34,619 (2017: £432).

3.13 A separate report on the two companies on this agenda provides a more detailed progress update.

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 2018. 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 33 to 39 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 revised Code of Practice issued by Audit Scotland in May 2016. 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

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11. Appendices

Appendix 1 – Scott-Moncrieff - Lothian Pension Funds 2017/18 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 2018 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 2018;

Appendix 4 – LPFI Limited – Financial Statements (Audited) for the year ended 31 March 2018;

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

Appendix 1

Lothian Pension Funds

2017/18 Annual Audit Report to Members and the Controller of Audit

August 2018

Contents

Key messages

Annual report and financial statements

Lothian Pension Funds will approve the annual report and financial statements for 2017/18 on 26 September 2018. 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 (collectively referred to as the “Funds”) within our independent auditor’s report. We also intend to report that there were no matters which we were required to report by exception.

The annual report and financial statements and supporting schedules were of a high standard. Our thanks go to staff for their assistance with our work.

Wider Scope

Financial sustainability

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

The Funding Strategy Statement has been updated to ensure investment assets are sufficient to meet the full cost of past service benefits.

There is an ongoing risk that the pension scheme is not affordable for admitted bodies and as part of the triennial valuation Lothian Pension Fund required all bodies to conduct an affordability assessment.

Financial management

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

Lothian Pension Fund’s investment performance decreased in 2017/18 and was below the short term benchmark and national average. Medium and long term performance, however, remained above benchmark levels.

Governance & transparency

Governance arrangements at the Funds are deemed to be appropriate.

Our assessment has been informed by a review of the corporate governance arrangements in place, the information provided to the Board and Committees as well as the risk management arrangements in place.

Value for money

The Funds’ investment performance is subject to regular review by the Pension Committee.

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

Key facts

- The net investment assets of Lothian Pension Fund increased by 1% to £6,628 million (2016/17: £6,568 million).
- Return on investments in 2017/18 was 1.4%, which was behind the benchmark of 3.6%, however, the performance over the five and ten year period to 31 March 2018 exceeded the benchmark by an average of 1.1%.
- Lothian Pension Fund reported a net withdrawal position for the second consecutive year with the withdrawal position increasing by 86% to £17,035 million.
- Membership of Lothian Pension Fund continued to grow to 78,856 members, an increase of 3.8%.

Conclusion

This report concludes our audit for 2017/18. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK) and Ethical Standards.

Scott-Moncrieff

August 2018

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Introduction

This report is presented to those charged with governance and the Controller of Audit and concludes our audit of the Lothian Pension Funds for 2017/18.

We carry out our audit in accordance with Audit Scotland’s Code of Audit Practice (May 2016). This report also fulfils the requirements of International Standards on Auditing (UK) 260: Communication with those charged with governance.

At the Lothian Pension Funds, the Pensions Committee has been designated as “those charged with governance”.

Introduction

1. Audit Scotland appointed Scott-Moncrieff as auditor to the Funds for the five year period from 2016-17 to 2020-21.

2. The scope of the audit was set out in our External Audit Annual Plan, which was presented to the Pensions Committee on 26 March 2018. The audit was planned in accordance with the revised Code of Audit Practice issued by Audit Scotland in May 2016.

We use this report to summarise our:

- opinion on significant issues arising from our external audit for the year ended 31 March 2018; and
- consideration of the wider dimensions of public audit work, as set out in Exhibit 1, below.

Exhibit 1: Audit Dimensions within the Code of Audit Practice

Source: Code of Audit Practice, May 2016

3. The Funds are responsible for preparing annual report and accounts that show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified 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 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.

4. This report contains an action plan with specific recommendations, responsible officers and dates for implementation. We give each recommendation has been given a grading to help the Funds assess its significance and prioritise the actions required.

5. We discussed and agreed the content of this report with the Chief Executive Officer and Chief Finance Officer. We would like to thank all members of the Fund's management and staff who have been involved in our work for their co-operation and assistance during our audit work.

Confirmation of independence

6. International Standards on Auditing in the UK (ISAs (UK)) require us to communicate on a timely basis all facts and matters that may have a bearing on our independence.

7. We confirm that we have complied with Financial Reporting Council's (FRC) Revised Ethical Standard (June 2016). In our professional judgement, the audit process is independent and our objectivity has not been compromised in any way.

Adding value through the audit

8. All of our clients demand of us a positive contribution to meeting their ever-changing business needs. Our aim is to add value to the council 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 Board promote improved standards of governance, better management and decision making and more effective use of resources.

Feedback

9. Any comments you may have on the service we provide, the quality of our work and our reports would be greatly appreciated at any time. Comments can be reported directly to the audit team or through our online survey: *www.surveymonkey.co.uk/r/S2SPZBX*

10. While this report is addressed to SCTS, it will be published on Audit Scotland's website www.audit-scotland.gov.uk

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Annual report and financial statements

The Funds' annual report and financial statements are the principal means of accounting for the stewardship of its resources and its performance in the use of those resources.

In this section we summarise the findings from our audit of the 2017/18 annual report and accounts.

Annual report and financial statements

The annual report and financial statements for the year ended 31 March 2018 will be approved by the Pensions Committee on 26 September 2018. We intend to report unqualified opinions within our independent auditor's report. We did not identify any significant adjustments to the unaudited annual report and accounts.

The Funds' had good administrative processes in place to prepare the annual report and financial statements and the required supporting working papers.

The governance statement disclosures are deemed to be appropriate and highlights that in 2017/18 internal audit reported that significant enhancements were required to the Funds' control environment.

Overall conclusion

Unqualified audit opinions

11. The annual report and financial statements for the year ended 31 March 2018 will be considered by the Pensions Committee on 26 September 2018. We reported within our independent auditor's report:

- an unqualified opinion on the financial statements; and
- an unqualified opinion on other prescribed matters.

12. 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

13. 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

14. The assessed risks of material misstatement described in Exhibit 2 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. Our opinion on the annual report and financial statements is not modified with respect to any of the risks described in Exhibit 2.

Exhibit 2: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

1. Revenue Recognition
Under ISA (UK) 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 transactions in such a way as to lead to a material misstatement in the reported financial position.

Excerpt from the 2017/18 External Audit Plan

15. 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.

16. We have evaluated key revenue transactions and streams to gain assurance over the completeness and occurrence of income. We are satisfied income in fairly stated in the financial statements. We also carried out testing to confirm that the Funds' revenue recognition policies are appropriate and have been applied consistently throughout the year.

2. Risk of fraud in the recognition of expenditure

The FRC published Practice Note 10 which applies to the audit of financial statements for periods commencing after June 2016. The Practice Note recognises that most public sector bodies are net spending bodies and notes that there is an increased risk of material misstatement due to improper recognition of expenditure.

Excerpt from the 2017/18 External Audit Plan

17. At the planning stage of our audit cycle, we reported that we did not believe the risk of fraud in expenditure recognition was material to the financial statements and we therefore rebutted this risk. This position has been reviewed throughout this audit and this conclusion has remained appropriate.

3. Management Override

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 financial statements. This is treated as a presumed risk area in accordance with ISA (UK) 240 – *The auditor's responsibilities relating to fraud in an audit of financial statements*.

Excerpt from the 2017/18 External Audit Plan

18. We have not identified any indications of management override in the year. We have reviewed the Funds' accounting records and obtained evidence to ensure that transactions outside the normal course of business were valid and accounted for correctly. We have also reviewed management estimates and the journal entries processed in the period and around the year end. We did not identify any areas of bias in key judgements made by management and judgements were consistent with prior years.

4. Valuation of investments

The Funds held investments of £6.569billion as at 31 March 2017 of which 30% (£2.069 billion) were classified as level 2 or level 3 financial instruments, meaning the valuation was not based on unadjusted quoted prices in active markets. Judgements are taken by the Investment Managers to value those investments whose prices are not publically available. 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.

Excerpt from the 2017/18 External Audit Plan

19. In 2017/18, the value of level 2 and 3 investments rose by 5% to £2.184 billion increasing as a proportion of overall investments to 33%.(31% in 2016/17). Fair values of investments of this nature are provided by fund managers and custodian using various bases selected by the investment manager or custodian. The base of investment values can include reference to similar companies or bid prices.

20. We have considered the valuation basis for a sample of investments and concluded that an appropriate base has been applied in each case. The custodian and investment managers are deemed to be management experts. In line with ISA (UK) 500 we have considered the competence, capability and objectivity of the experts used to inform the valuation. In addition we have reviewed auditor reports on the internal controls at the custodian and at each key investment manager. Our testing did not raise any issues regarding the qualifications of or work provided by the management experts employed by the Funds.

21. For a sample of hard to value investments we reviewed the assumptions and bases of the fair value. We challenged the Funds on the rationale for selecting the bases and assumptions and ensured we were satisfied they were appropriate.

22. The disclosures within the annual report and financial statements are consistent with the information provided by the custodian.

5. 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 an independent firm of actuaries with specialist knowledge and experience. The latest triennial valuation was as at 31 March 2017 and sets rates for the three-year period commencing 1 April 2018. The estimates are based on the most up to date membership date 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 data provided to the actuary is not complete and that assumptions used are not appropriate.

Excerpt from the 2017/18 External Audit Plan

23. We have reviewed the controls in place for providing information to the actuary and found them to be sufficient. We obtained the information provided to the actuary and agreed to source documentation to confirm the accuracy of data provided. We did not identify any issues from the work performed.

24. The assumptions used by the actuary were compared to the benchmarks across the sector and we concluded that these were reasonable.

Our application of materiality

25. The assessment of what is material is a matter of professional judgement and involves considering both the amount and the nature of the misstatement. This means that different materiality levels will be applied to different elements of the annual accounts.

26. On receipt of the draft 2017/18 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. A key target for the Funds is to manage investments appropriately in order to generate sufficient income to meet the future pensioner needs. We consider net investment assets to be one of the principal considerations for the users of the accounts when assessing financial performance. We have therefore used this as a base for our materiality.

27. As outlined in our External Audit Plan we considered transactions when dealing with members (i.e. contributions and expenditure incurred providing payments to pensioners) to also be of key interest to the users. This is reported in the first section of the Fund Account and contains information about the day to day operation of the Funds.

28. ISA 320 states that in certain circumstances it is appropriate to set a materiality amount for particular classes of transactions for which lesser amounts than the overall materiality could influence the decision of the users of the accounts. We have therefore set a separate materiality for transactions relating to dealings with members, based on the expenditure incurred for providing payments to pensioners.

	Overall planning materiality £ million	Dealings with members overall planning materiality £ million	Overall Final materiality £ million	Dealings with members overall final materiality £ million
Lothian Pension Fund (group)[1]	98.5	10.6	100	10.7
Lothian Pension Fund (single entity)	98.5	10.6	100	10.7
Lothian Buses Pension Fund	7.3	0.6	7.6	0.6
Scottish Homes Pension Fund	2.6	0.4	2.3	0.4

Performance materiality

29. Performance materiality is the amount set by the auditor at less than overall materiality for the annual accounts as a whole to reduce to an appropriately low level the probability that the aggregate of the uncorrected and undetected misstatements exceed materiality for the annual accounts as a whole.

30. We set a performance (testing) 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. Performance testing thresholds used are set out in the following table:

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

	Area risk assessment £million		
	High (50%)	Medium (60%)	Low (75%)
Lothian Pension Fund (group and parent)	50	60	75
Lothian Buses Pension Fund	3.8	4.6	5.7
Scottish Homes Pension Fund	1.3	1.5	1.9

31. 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.

Audit differences

32. We are pleased to report that our audit identified no material adjustments. In addition we can confirm there were no unadjusted errors relating to the 2017/18 financial statements.

33. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual report and financial statements.

An overview of the scope of our audit

34. We detailed the scope of our audit in our External Audit Plan. We presented the plan to the Pensions Audit Sub-Committee on 26 March 2018. The 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 Funds. 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.

35. 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.

36. Our standard audit approach is based on performing a review of the key accounting systems in place, substantive tests and detailed analytical procedures. 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.

Other matters identified during our audit

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

The Local Authority Accounts (Scotland) Regulations 2014

38. As part of our audit we reviewed the Funds' compliance with the Local Authority Accounts (Scotland) Regulations 2014, in particular with respect to regulations 8 to 10[2] as they relate to the annual report and financial statements.

39. In 2017/18 we received an objection to the notice of the public right to inspect. Upon review there was found to be an inaccuracy with the inspection notice, which was subsequently rectified. In addition it was noted that the accounts were not available through the Lothian Pension Fund website from the beginning of the inspection period. While the financial statements were available on the City of Edinburgh Council website as part of the Pensions Committee papers, we would recommend that in future they are also placed on the Lothian Pension Fund website following Committee approval.

Action plan point 1

40. Overall we concluded that appropriate arrangements are in place to comply with these Regulations.

Management commentary

41. The management commentary is a requirement of the Local Authority Accounts (Scotland) Regulations 2014 and is intended to assist readers in understanding the financial statements and provide an overview of the organisation and its performance.

42. Guidance issued by the Scottish Government (Local Government Finance Circular 5/2015 also provides a guide as to the minimum required disclosures in the management commentary including:

- The context of the annual report and financial statements;
- 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.

43. We have concluded that the management commentary has been prepared in line with the regulations and Scottish Government guidance and is consistent with the financial statements.

Annual governance statement Governance Compliance Statement

44. We have reviewed the Funds' annual governance statement against the relevant guidance: *Delivering Good Governance in Local Government*.

45. We consider the coverage of the annual governance statement to be broadly in line with expectations.

46. The annual governance statement highlights that internal audit provided a 'red'[3] rated opinion, reflecting significant enhancements required to the Funds' control environment.

47. The internal audit reports highlighted raised highlighted the need for LPF to ensure that third party systems suppliers have established adequate and effective resilience arrangements that are aligned with LPF recovery objectives; and effective change management controls to provide assurance on the ongoing integrity of their systems.

48. The governance statement highlights the actions planned to address the internal audit issues.

49. The Chief Executive and Head of Finance of the City of Edinburgh Council have considered the internal audit findings and are satisfied that reasonable assurance can be placed upon the adequacy and effectiveness of Funds' systems of internal control.

50. We have concluded that the annual governance statement is in line with the required guidance and is consistent with the financial statements and assurances provided in year.

Governance compliance statement

[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.

[3] Significant areas of weakness and non-compliance in the control environment and governance and risk management framework that puts the achievement of organisational objectives at risk.

51. 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.

52. 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.

Legality

53. We have planned and performed our audit recognising that non-compliance with statute or regulations may materially impact on the annual report and financial statements.

54. It was highlighted during the course of our audit that the Pension Fund had not been operating its bank account in line with the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010. There is a requirement for administering authorities to hold a separate bank account for funds and this should be used to hold pension fund money.

55. Internal audit noted in November 2015, there were issues over the use of bank accounts, particularly that monies were being transferred into a City of Edinburgh bank account and payments made from this account.

56. The Funds noted that the procurement of a new payroll and ledger system would help resolve the payment issues but that there was no proposal to change current procedures.

57. The use of the Council bank account was to ensure that any unfunded payment does not come from a pension fund bank account.

58. The issue of non-compliance has been recognised in the Funds' risk register and work has commenced to deliver an updated ledger system, however, significant delays have been encountered. The issue with regarda to the use of bank accounts is therefore on going.

Action plan point 2

Group accounts

59. The Funds' annual report includes accounts for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.

60. Lothian Pension Fund accounts are prepared on a group basis following 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.

61. Group accounts were prepared for the Lothian Pension Fund 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.

62. We reviewed the consolidation process in 2017/18 and concluded the subsidiary companies had been correctly included in the group accounts of Lothian Pension Fund.

Qualitative aspects of accounting practices and financial reporting

63. 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.	We have reviewed the significant accounting policies which are disclosed in the annual report and financial statements 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. 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 £5.574 million for Lothian Pension Fund and £0.34 million for Lothian Buses (there were no indirect costs for Scottish Homes). 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.
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.	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. These estimates have been informed by advice from qualified, independent experts. We evaluated the competence, objectivity and capability of management experts in line with the requirements of ISA (UK) 500 and concluded that use of the expert is appropriate. We are satisfied with the appropriateness of the accounting estimates and judgements used in the preparation of the annual report and financial statements. We have considered the disclosures around the estimates, including sensitivity analysis and concluded that they are appropriate.
The appropriateness of the going concern assumption	We have reviewed the detailed financial forecasts for 2018/19. Our understanding of the legislative framework and activities undertaken provides us with sufficient assurance that the Funds' will continue to operate for at least 12 months from the signing date.

Qualitative aspect considered	Audit conclusion
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 financial statements contain no material misstatements or inconsistencies with the annual report and financial statements 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.	At the interim stage of our audit we conducted a review of the financial statements to identify areas where improvements to be made to reduce immaterial and surplus disclosures in the financial statements. Our recommendations were made to management and included only minor disclosure and presentational issues. No adjustments were made as a result of this work, however the impact is not considered to be significant. Additional disclosure and presentational adjustments were discussed at the year-end. Over the course of the audit there was no material disagreement 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 is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

Financial management

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

Lothian Pension Fund's investment performance decreased in 2017/18 and was below the short term benchmark and national average. Medium and long term performance, however, remained above benchmark levels.

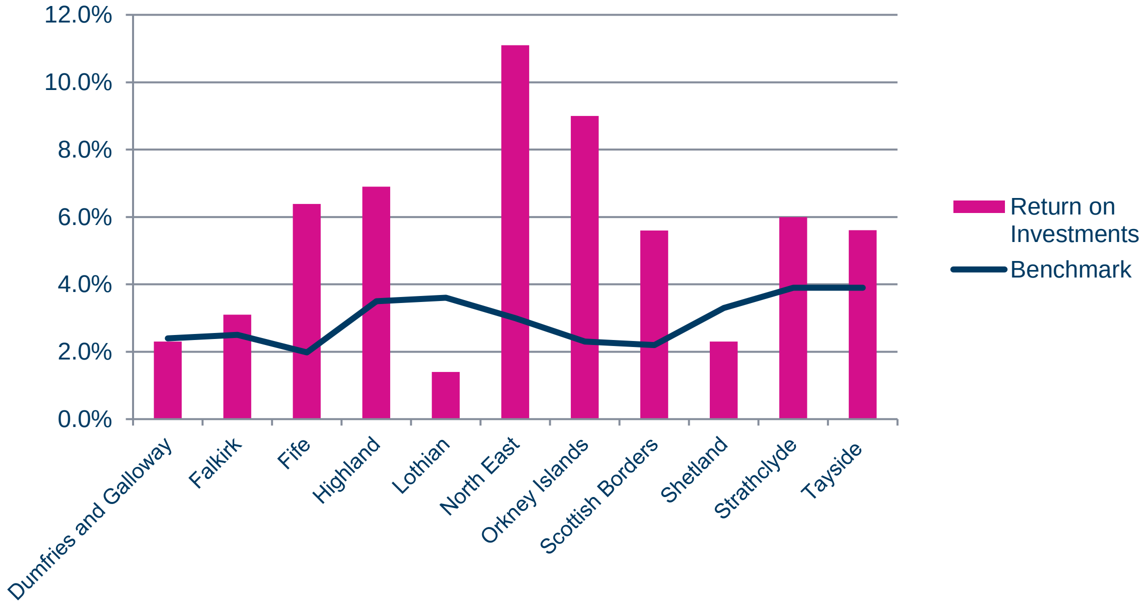
The net assets of Lothian Pension fund and Lothian Buses Pension Fund have risen at a slower rate than in 2016/17 and Scottish Homes Pension Fund assets have decreased marginally. The promised retirement benefits have decreased across all three funds.

Investment performance in 2017/18

64. The Funds report their performance with regards to returns on investments as part of the annual report and financial statements. As shown in Exhibit 4 below Lothian Pension fund has reported performance below the one year benchmark for the second year. Lothian Buses Pension Fund is reporting performance above benchmark and Scottish Homes has dropped behind the 1 year benchmark after reporting returns above benchmark in 2016/17.

65. Investment performance across the local government pension funds in Scotland fell in 2017/18 from a particularly strong year in 2016/17. The average return on investments in 2017/18 was 6.12% a significant decrease compared to 21.19% in 2016/17.

Exhibit 3: LGPS Funds Returns on investments against benchmark



66. Lothian Pension fund was notably below the national average in 2017/18 and was one of only three pension funds to perform below the benchmark. However, the objective of Lothian

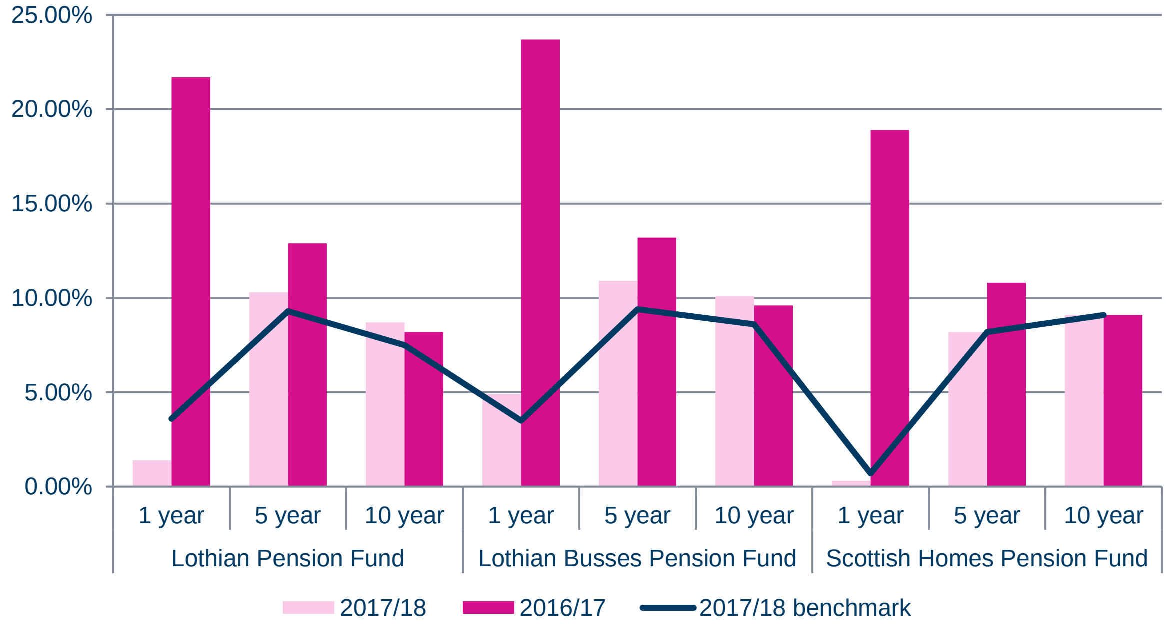
Pension Fund is that over the short term the fund should perform better than its strategic allocation if markets fall significantly.

67. Investment management outcomes are required to be considered over the longer term due to the range of factors which can influence returns including: risk appetite, asset allocation and general market performance. It is therefore important to consider the returns over a longer term.

68. The focus on the funds is stability over the long term which focuses on the medium and long term. The investment portfolio is geared to achieve this objective and therefore the short term returns are not deemed to be a key performance indicator for the Funds.

69. As shown in Exhibit 4, all three funds have met or exceeded the 5 and 10 year benchmarks which indicates the investment portfolio is being managed appropriately.

Exhibit 4: Performance against benchmark and compared to prior year



Financial position

70. The movement in net assets of the Funds varied across each fund as shown in Exhibit 5. While all three funds reported a net withdrawal position the net return on investments for Lothian Pension Fund and Lothian Buses Pension Fund exceeded the withdrawals position. The net investments for Scottish Homes was significantly below the withdrawals from dealings with members and this resulted in an overall decrease in the assets of the Fund.

Exhibit 5: LGPS Funds Returns on investments against benchmark

	Net assets			Present value of retirement benefits		
	2017/18 £m	2016/17 £m	% Movement	2017/18 £m	2016/17 £m	% Movement
Lothian Pension Fund	6,665	6,595	1.0%	7,791	8,210	-5.1%
Lothian Buses	509	488	4.3%	463	488	-5.12%
Scottish Homes	164	171	-4.1%	134	145	-7.6%

71. Hymans Robertson provided an estimate of the present value of the promised retirement benefits. Across all three funds the value of the obligation had decreased in year with the most significant decrease on the Scottish Homes Pension Fund.

72. The actuarial calculations are based on the 2017 actuarial valuation rolled forward. It was noted by the actuary in their report that asset returns under the primary investment strategy over the period have been lower than the valuation discount rate but that real bond rates were at a similar level meaning overall funding level is likely to have fallen slightly since the 2017 formal valuation.

Financial monitoring arrangements

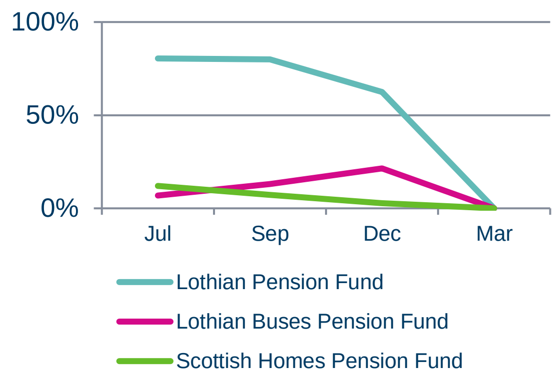
73. We have reviewed the Funds' budgetary processes and financial management arrangements in 2017/18.

74. The Pensions Committee receive annual investment updates for each fund in June 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.

75. The Pensions Committee also receive service updates at each committee which includes analysis of the financial position from dealings with members.

76. In year budgets were for a net withdrawals position across all three funds and there was some variation across the year. In all cases the projected position was a higher withdrawal than the actual year end position.

Exhibit 6: Reported movement as a percentage of year end position



77. The Lothian Pension Fund predicted position was in December 2017 was 62.5% higher than the amount reported in the financial statements in March 2018. The movement related to contributions from employers and employees rising further than predicted and lump sum payments decreasing.

Prevention and detection of fraud and irregularity

78. Our audit was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity.

79. We found the Funds' arrangements for the prevention and detection of fraud and other irregularities to be adequate.

Standards of conduct

80. In our opinion the Funds' arrangements in relation to standards of conduct and the

prevention and detection of bribery and corruption are adequate.

81. 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.

Internal Audit

82. An effective internal audit service is an important element of the Funds' governance arrangements. The City of Edinburgh Council provide the Funds' internal audit service. 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

83. In 2017/18 it was noted that the service did not fully comply with Public Sector Internal Audit Standards in two areas: follow up and quality assurance reviews. The Pensions Committee were advised that the instances of non-conformance have had no direct impact on the quality of internal audit reviews completed for the Funds in 2017/18.

84. Internal audit have taken remedial actions to put controls in place to address the weaknesses identified.

85. In 2017/18 we did not place formal reliance on the work of internal audit, however, we have considered their findings in respect of our wider scope responsibilities and we are grateful to the internal audit team for their assistance during the course of our work.

Systems of internal control

86. We have evaluated the Funds' key financial systems and internal financial controls to determine whether they are adequate to prevent material misstatements in the annual accounts. Our approach has included documenting the key internal financial controls and performing walkthroughs to confirm that they are operating as intended.

87. We identified a number of areas for improvement in 2016/17 which were followed up at interim and subsequently at year end. We have reported progress against outstanding actions in appendix 1.

88. We identified an issue relating to controls over raising journals as follows:

- In 2017/18 we noted that any member of the City of Edinburgh finance team with ledger access can post to the Funds' ledger. While any incorrect postings should be picked up through budget monitoring, there is a risk that mis-postings are not detected resulting in errors in the financial statements.

Action plan point 3

4

Financial sustainability

Financial sustainability looks forward to the medium and longer term to consider whether the Funds' are planning effectively to continue to deliver services or the way in which they should be delivered.

Financial Sustainability

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

The Funding Strategy Statement has been updated to ensure investment assets are sufficient to meet the full cost of past service benefits.

There is an ongoing risk that the pension scheme is not affordable for admitted bodies and as part of the triennial valuation Lothian Pension Fund required all bodies to conduct an affordability assessment.

Funding level

89. The Funds' undertook an actuarial valuation in 2017 in line with the requirements of the Local Government Pension Scheme Regulations 2014. The 2017 Actuarial Valuation was a triennial valuation which aims to:

- assess whether the funding strategy and assumptions are appropriate;
- assess the financial health of the Funds; and
- set future rates for contributions payable by employers.

90. At the 2017 Actuarial Valuation the funding levels increased for all three funds. Lothian Buses Pension Fund and Scottish Homes Pension Fund were achieving their target funding levels.

Exhibit 7: Funding level across the Funds

	Actual 2014 (%)	Actual 2017 (%)	Target (%)
Lothian Pension Fund	91%	98%	100%
Lothian Buses	117%	121%	100%
Scottish Homes	89%	105%	93%

91. The results of the actuarial valuation show that Lothian Pension Fund has not met its objective to hold sufficient assets to meet the full cost of the past service benefits at 31 March 2017. The increase of 7% shows that progress has been made and the deficit has decreased from £417 million to £145 million.

Contribution rates for employers

92. Contribution rates for employers are set for each scheduled and admitted employer in to Lothian Pension Fund and depend on each body's unique funding position.

93. In general, employer contribution rates across Lothian Pension Fund have increased compared to the 2014 valuation.

94. In recognition of the affordability issues facing many employers within Lothian Pension Fund, management conducted additional work on the Funding Strategy Statement, including a requirement for scheduled and admitted bodies to confirm their commitment to meeting the certified minimum contributions.

95. The Fund also prepared a funding agreement to address repayment of debt on the exit of an employer from the scheme.

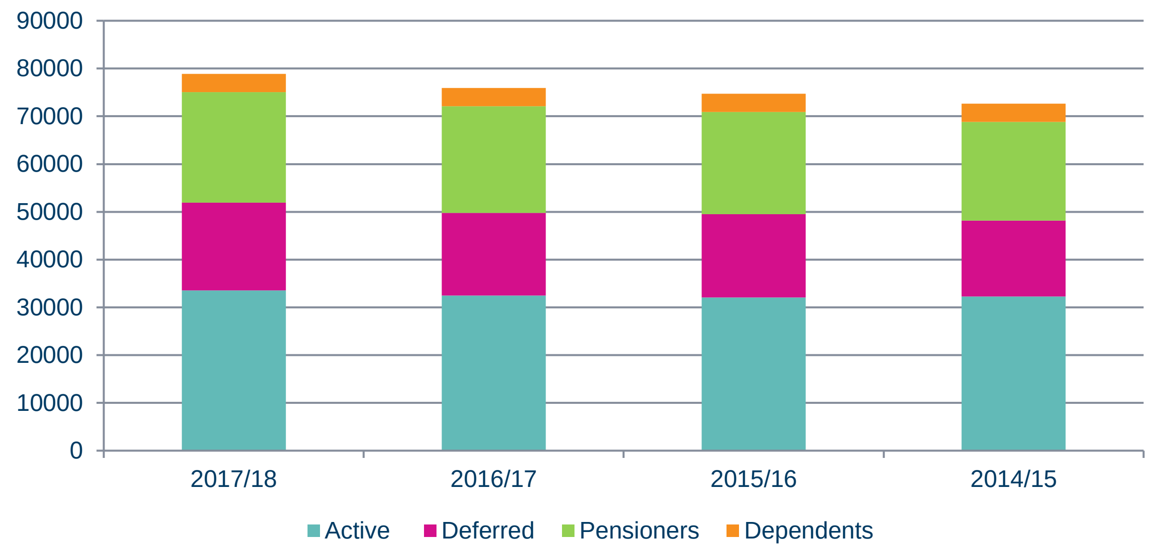
96. In 2017/18 a number of employers indicated an intention to leave the Fund. Cessation contributions increased by £1.204 million (5.78%) in year to £1.412 million and at 31 March 2018 there is a long term debtor of £1.525 million related to ceased employers.

97. In line with our recommendation in 2016/17 additional disclosures have been included around the long term debtors relating to employer cessations.

Membership

98. Lothian Pension Fund is a multi-employer fund with 14 scheduled bodies, including 4 Councils, and 72 admitted bodies. The scheme has a significant membership profile with active members being the majority. This differs from Lothian Buses and Scottish Homes Pension Funds which are single employer schemes and have a majority of inactive members (deferred, pensioners and dependents).

Exhibit 8: Membership trend analysis



99. The trend analysis shows that for Lothian Pension Fund the proportion of active members continues to grow while at Lothian Buses Pension Fund and Sottish Homes Pension Fund the level of pensioners and dependents is growing.

100. A revised Funding Strategy Statement was approved by the Pensions Committee in March 2018, following a consultation exercise in July 2017.

101. Key changes to the Funding Strategy included:

- the inclusion of a medium risk strategy which will be open to employers with more than 5 members and which are closed to new members;
- written confirmation of ability to meet contributions are required as outlined above; and
- the creation of alternative options for the payment of pension strain costs

LGPS Consultation

102. A review of the structure of the Scottish Local Government Pension Schemes was agreed with stakeholders and Scottish Government in 2015 when changes to the scheme and Scheme Advisory Board ('SAB') were introduced.

103. In February 2017, SAB produced a review report which highlighted 4 options for the future structure of the local government pension scheme in Scotland:

- Retain the current structure with 11 funds;
- Promote cooperation in investing and administration between the 11 funds;
- Pool investments between the 11 funds; and
- Merge the 11 funds into one or more new funds.

104. These options were presented to the Cabinet Secretary for Finance, Economy and Fair Work and in January 2018, it was advised that SAB should proceed to seek a consultation with

Scottish LGPS employers and employee membership bodies on the 4 options. The consultation launched in June 2018 and will close in December 2018.

105. We will continue to monitor the developments and outcomes arising from the consultation as part of our 2018/19 audit.

EU withdrawal

106. Audit Scotland has identified EU withdrawal as an emerging significant risk facing public bodies across Scotland. Three streams of potential impact were identified:

- Workforce;
- Funding; and
- Regulation.

107. The Funds have considered the impact across all three areas, and have identified that this is an area of low risk for the pension fund. The primary consideration was the impact of the EU withdrawal on movement in investments and risk mitigating measures were put in place prior to the vote.

108. From an initial assessment of the workforce stream no significant implications have been identified.

5

Governance & transparency

Governance and transparency is concerned with the adequacy of governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.

Governance & transparency

Governance arrangements at the Funds are deemed to be appropriate.

Our assessment has been informed by a review of the corporate governance arrangements in place, the information provided to the Board and Committees as well as the risk management arrangements in place.

Governance Structure

109. The Pensions Committee, supported by an Audit Sub-Committee, has been delegated responsibility for governance by the City of Edinburgh Council, the administering authority.

110. 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.

111. 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 third year of operation of the Pension Board.

112. The Pension Board meet quarterly on a concurrent basis with the Pension Committee.

113. The Funds complied with best practice and appointed an independent professional observer to the Board and Committee. The appointed independent observer resigned in February 2018 and to date the post has not been filled.

114. 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 2017/18.

Training and development

115. 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.

116. Our review found that all current Pension Committee and Board members met the requirement to have a minimum of 21 hours training, however, a member of the Committee who left in 2017/18 would not have met the full training requirement for the year.

Openness and Transparency

117. 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.

118. During the year, the Pensions Committee has evaluated whether further steps could be taken to move to best practice on the accessibility and openness of meetings held through webcasting of meetings. While the final decision was not to webcast meetings, the Committee were provided detailed information to allow a thorough evaluation and an informed decision to be made.

119. We consider the openness and transparency of the Funds to be appropriate and in line with legal requirements.

Risk Management

120. 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.

121. 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.

122. From our review of the risk management arrangements in place we have concluded that there are adequate arrangements in place at the Funds.

Information Governance

General Data Protection Regulations

123. The General Data Protection Regulations (the Regulations) came into force on 25 May 2018. The Regulations replace the Data Protection Act 1998 and as well as strengthening existing regulations, the Act has brought in new legislative requirements for the Funds. The Regulations bring significant potential penalties for non-compliance therefore increasing the importance of compliance.

124. To ensure compliance, LPF has fully reviewed its business processes to ensure they were fully compliant with the new legislation including review of LPF's data storage, information governance, ICT, office procedures and third party relationships.

125. The Pensions Committee has received regular updates on the progress of the project were primarily reported through quarterly risk management summaries.

126. Compliance with the regulations is an ongoing process, which we will monitor as part of our annual audit procedures. We have not identified any significant risks to compliance with the Regulations at this stage.

Cyber Security

127. In May 2017, a number of health boards across NHS Scotland were affected by the Wannacry global ransomware attack. In response to this the Scottish Government launched 'A Cyber Resilience Strategy for Scotland: Public Sector Action Plan, 2017/18'.

128. The action plan outlines a number of requirements that public bodies should be taking forward. This includes an action for public bodies to achieve a Cyber Essentials Plus certification by the end of October 2018.

129. The Funds currently use City of Edinburgh Council systems for the financial ledger and can place reliance on the Council's assessment. However, for Fund specific systems there is a need to complete the Cyber Essentials accreditation. We recommend that the Funds make arrangements to achieve the cyber Essentials certification by 31 October 2018.

Action plan point 4

LGPS Regulations

130. Revised Local Government Pension Scheme regulations came into effect from 1 June 2018 with an update on the implications of the new legislation being presented to the June 2018 Pensions Committee.

131. The changes to the regulations aim to consolidate all amendments since April 2015 and include a number of amendments to the scheme rules including:

- members of the LGPS 2015 will be able to elect to take early payment of their pension from age 55, with an actuarial reduction and will no longer need their employers consent;
- additional flexibility for administering authorities when employers leave the scheme and to provide extra credit to exiting employers if appropriate; and
- changes to additional voluntary contributions following the introduction of the UK governments "freedom and choice in pensions", to allow payment from age 55 as a lump sum.

132. LPF are currently seeking clarification on some aspects of the regulations and we will consider implications as part of our 2018/19 audit work.

6

Value for Money

Value for money is concerned with using resources effectively and continually improving services. In this section we report on our audit work as it relates to the Funds' reporting of their performance.

Value for money

The Funds' investment performance is subject to regular review by the Pension Committee.

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

Investment manager operations

133. Lothian Pension Fund operates two special purpose vehicles: LPFE Ltd and LPFI Ltd. Both companies were wholly owned and controlled by the Council.

134. The special purpose vehicles were established to support the investment programme of the in-house investment team by providing operational efficiencies.

135. The proportion of funds managed internally has remained steady at approximately 85% of investments since 2015/16.

Staff Transfer

136. In 2015, LPF's key investment staff transferred to LPFE Limited. In February 2018, the Funds' remaining staff also transferred to LPFE Limited following engagement with staff and trade unions.

137. It is anticipated that employing all staff in a single organisation will enable greater collaborative efforts with other local government pension funds as well as helping to ensure a consistent approach to resourcing.

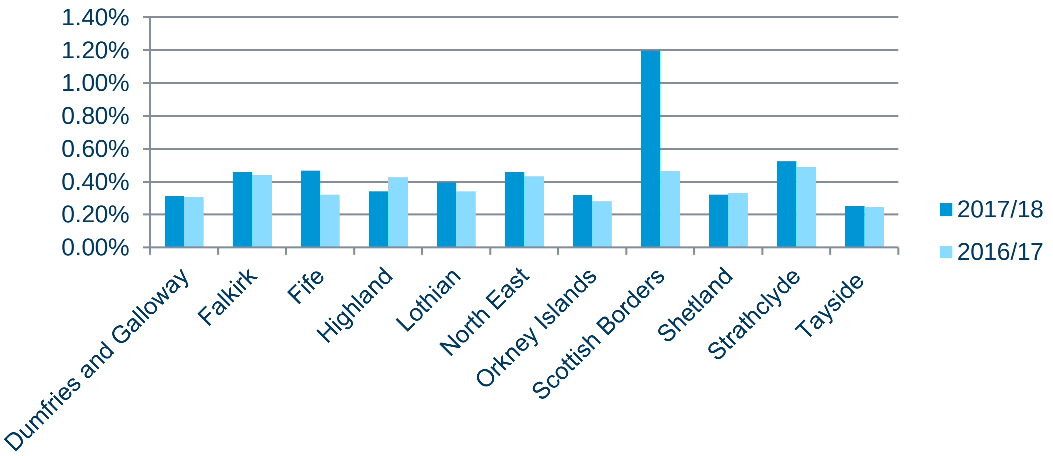
Management expenses

138. Lothian Pension Fund reported management expenses of £35.412 million in 2017/18, an increase of 19% from the prior year.

139. Management expenses are split into three main categories: administrative costs; investment manager expenses and oversight and governance costs. Investment management expenses account for 90% of total management expenses.

140. In year Lothian Pension Fund's investment manager expenses (excluding indirect expenses) rose marginally as a proportion of net assets. This is broadly in line with trends across the Local Government Pension Funds.

Exhibit 9: Investment manager expenses (excluding indirect costs) as a proportion of net assets



141. The analysis above does not include indirect investment management costs as CIPFA guidance states that only direct investment management costs i.e. those that the fund can control should be reported. Lothian Pension Fund reported £5.574 million of indirect manager expenses in 2017/18. It is not possible to benchmark the impact of indirect management costs across Scottish Local Government Pension Funds.

142. Investment manager expenses can vary due to a number of factors including actual returns on investments and the nature of the investments assets held.

143. The Funds undertake annual benchmarking exercises using externally provided data, covering 33 LGPS funds and a wider global universe of 331 funds.

144. In 2017/18 Lothian Pension Fund reported an actual investment cost of 0.41% of net assets which was below the benchmark of 0.48%

145. The pension administration cost per member was £24.37, which is higher than the average cost of local authority funds of £20.18. The cost per member is broadly deemed to be in line with other local authority funds who operate within the range of costs of £13 to £33 per member.

Monitoring investment performance

146. There is an annual review of investment performance in June for each of the Funds. The report provides a detailed analysis of each of the Fund's investment performance against its investment strategy. We concluded that Pension Committee and Board Members are engaged in monitoring the performance of investments.

147. In addition to monitoring at a Committee level the Funds' performance is calculated 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.

Investment Strategy Panel

148. The Pensions Committee has delegated responsibility for investment strategy to the Executive Director of Resource who takes advice from an Investment Strategy Panel made up of:

- Chief Executive, Lothian Pension Fund;
- Chief Investment Officer, Lothian Pension Fund; and
- two external independent investment consultants.

149. 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 Chief Financial Officers of each administering authority on the implementation of investment strategy. Over the last year, Lothian collaborated with Falkirk Council Pension Fund on 7 infrastructure investments.

150. The Investment Strategy Panel considers the appropriate investment management structure required to implement the Funds' investment strategy. In addition it is responsible for:

- setting objectives and restrictions for internally managed investments; and
- monitoring the risk and performance of all portfolios.

151. It is noted in the annual report of the Investment Strategy Panel that their focus is long term superior returns rather than short term fluctuations of the investment market.

Administrative Performance

152. The Funds' have a Service Plan in place covering the period 2016- 2018 . The Pensions Committee receive updates on the service plan at each meeting. The annual results for 2017/18 are presented in the Funds' Management Commentary.

153. The Performance Report highlights that the Fund are meeting the majority of their targets (90%) with only 1 area where performance was not in line with target levels:

- The target for the proportion of active members receiving their annual benefit statement by 31 August 2017 was 100% but the Funds' achieved a level of 99.9%. This represents an improvement on prior year performance which was 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.

Tendering for Services

154. 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.

155. The Funds follow the City of Edinburgh Council procurement procedures and maintain a contract register.

156. A paper went to the Pensions Committee in December 2017 providing an update on the contracts register and the procurement decisions which had been made in year.

157. It was noted that a review of the investment managers had been conducted, with further services being brought in house for Scottish Homes Pension Fund. One investment manager contract had been extended to allow more options appraisal work to be considered on the operation of the property management portfolio. This work is due to conclude in 2018/19.

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 in both current and previous audits.

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, Risk & Recommendation	Management Comments
1. Publication of the financial statements **Rating** **Grade 2** **Paragraph ref** **39**	**Issue** In 2017/18 Lothian Pension Fund received objections to the accounts relating to the public right to inspect the accounts. The objections related to the wording in the public inspection notice and the availability of the annual report and financial statements on the Lothian Pension Fund website. **Risk** There is a risk that Lothian Pension Fund do not meet their statutory duties in respect of the requirements of the Local Authority Accounts (Scotland) Regulations 2014. **Recommendation** We recommend that the annual report and financial statements are posted on the Lothian Pension Fund website, following approval from the Pensions Committee and in line with the public inspection notice.	Recommendation is accepted. Following consideration of the Annual Report 2019 (and Financial Statements) Unaudited by Pensions Committee, this will be posted on the Lothian Pension Fund website, supplementing the prior disclosure of all the reports to that Committee on the Council's website. **Responsible officer:** Chief Executive Officer, Lothian Pension Fund **Implementation date:** June 2019

Action plan point	Issue, Risk & Recommendation	Management Comments
Action plan point	Issue, Risk & Recommendation	Management Comments
2. Bank accounts **Rating** **Grade 3** **Paragraph ref** **57**	**Issue** The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010. require administering authorities to hold a separate bank account for funds and to be used to hold pension fund money. There is an ongoing issue that although the Funds' held their own bank accounts, monies were transferred to the City of Edinburgh Council holding account and the money was managed through this account. Actions were taken in 2017/18 to progress the issue of compliance, however, significant delays mean that during the year the Funds were not in fully compliant with the regulations. **Risk** There is a risk that monies for the Funds are not separately identifiable. **Recommendation** We recommend the Funds put arrangements in place to ensure compliance with the regulations.	Quotation for a stand-alone ledger for the Funds was sought from CGI, the Council's ICT provider, but this did not offer a cost-effective solution. Whilst LPF now fully anticipates a successful project delivery by the Council and CGI, with integration of the LPF requirement in the ledger specification, the option of complete separation, i.e. LPF to procure an alternative to the Council solution, is retained as "last resort". **Responsible officer:** Chief Finance Officer, Lothian Pension Fund **Implementation date:** As soon as possible, subject to the implementation of a revised financial ledger system by the Council to incorporate this functionality, or alternatively a separate procurement by LPF.

Action plan point	Issue, Risk & Recommendation	Management Comments
3. User access controls **Rating** **Grade 3** **Paragraph ref** **85**	**Issue** Our review of the journals environment identified that all City of Edinburgh Council staff with access to Oracle, the financial ledger system, have the ability to post to the Funds' financial ledgers. **Risk** There is a risk that incorrect or fraudulent postings could be made without detection by the Funds' officers. **Recommendation** While our audit review in respect of the 2017/18 financial year did not identify any indications of user access being manipulated, we recommend that the Funds' officers in conjunction with City of Edinburgh Council review user access controls for the financial ledger.	Recommendation is accepted. **Responsible officer:** Chief Finance Officer, Lothian Pension Fund **Implementation date:** March 2019

Action plan point	Issue, Risk & Recommendation	Management Comments
4. Cyber Essentials **Rating** **Grade 3** **Paragraph ref** **126**	**Issue** In 2017/18 In May 2017, a number of health boards across NHS Scotland were affected by the Wannacry global ransomware attack. In response to this the Scottish Government launched 'A Cyber Resilience Strategy for Scotland: Public Sector Action Plan, 2017/18'. The action plan outlines a number of requirements that public bodies should be taking forward. This includes an action for public bodies to achieve a Cyber Essentials Plus certification by the end of October 2018. The Funds are aware of the work but do not have a formal plan to achieve certification. **Risk** There is a risk that Lothian Pension Fund are not compliant with Cyber Essentials by the required Scottish Government deadline. **Recommendation** We recommend that the Funds make arrangements to ensure Cyber Essentials certification is achieved bt 31 October 2018.	Recommendation is accepted. LPF is liaising with the Council's Chief Information Officer to secure requisite certification. **Responsible officer:** Chief Executive Officer, Lothian Pension Fund **Implementation date:** October 2018

Outstanding recommendations from previous audit reports

Action plan point	Issue & Recommendation	Management Comments	Follow up
1. Authorisation of journals **Rating** **Grade 3**	**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. **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.	Agreed the fund will undertake a review of the journals processes. All parties that use the Council's financial systems are affected by this finding. The Fund awaits the Council's response to the issue. 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. **Action owner:** John Burns **Due Date:** 31 January 2018	In 2017/18 we noted that there is no authorisation process in place at the Funds. A compensating control has been put in place which requires reconciliation of journals and the ledger by a separate member of the finance team. **Action complete**

Action plan point	Issue & Recommendation	Management Comments	Follow up
2. Annual Governance Statement **Rating** **Grade 3**	**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. **Recommendation** We recommend the Funds' consider the disclosures in the Annual Governance Statement	Agreed to review for next year's accounts **Action owner:** Struan Fairbairn **Due Date:** 31 March 2018	The 2017/18 annual governance statement includes details of actions that will be taken to improve governance arrangements and the system of internal control. **Action complete.**

	to ensure they are meeting applicable guidance.		

Action plan point	Issue & Recommendation	Management Comments	Follow up
3. Employer cessation liabilities **Rating** **Grade 3**	**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. **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.	Agreed to review disclosures in management commentary for next year's accounts after the completion of the 2017 triennial actuarial valuation. 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. **Action owner:** John Burns **Due Date:** 31 March 2018	Additional commentary has been provided within the debtors section of the financial statements **Action complete**

Action plan point	Issue & Recommendation	Management Comments	Follow up
4. Annual benefits statements **Rating** **Grade 2**	**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. **Recommendation** The Pension Committee members should consider whether they deem this to be an issue which should be self-referred to the Pension Regulator.	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.	The target for the proportion of active members receiving their annual benefit statement by 31 August 2017 was 100% but the Funds' achieved a level of 99.9. 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 Funds should consider if this requires reporting to the Pension Regulator. **Responsible officer:** **Chief Finance Officer** As previously advised orally to Pensions Committee, this was not considered sufficiently material to warrant a voluntary disclosure to The Pensions Regulator.

Appendix 2: 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 2018 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 report and financial statements.

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 report and financial statements, 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 addition to our work on the Funds we are also responsible for the audit of the financial statements of LPFE Ltd and LPFI Ltd, the subsidiaries of Lothian Pension Fund. In addition to the audit of the subsidiaries, Scott-Moncrieff provides accounts preparation, corporation tax services and ad hoc VAT advice to both LPFE Ltd and LPFI Ltd.

All tax services are provided by an independent tax partner and staff who have no involvement in the audit of the financial statements.

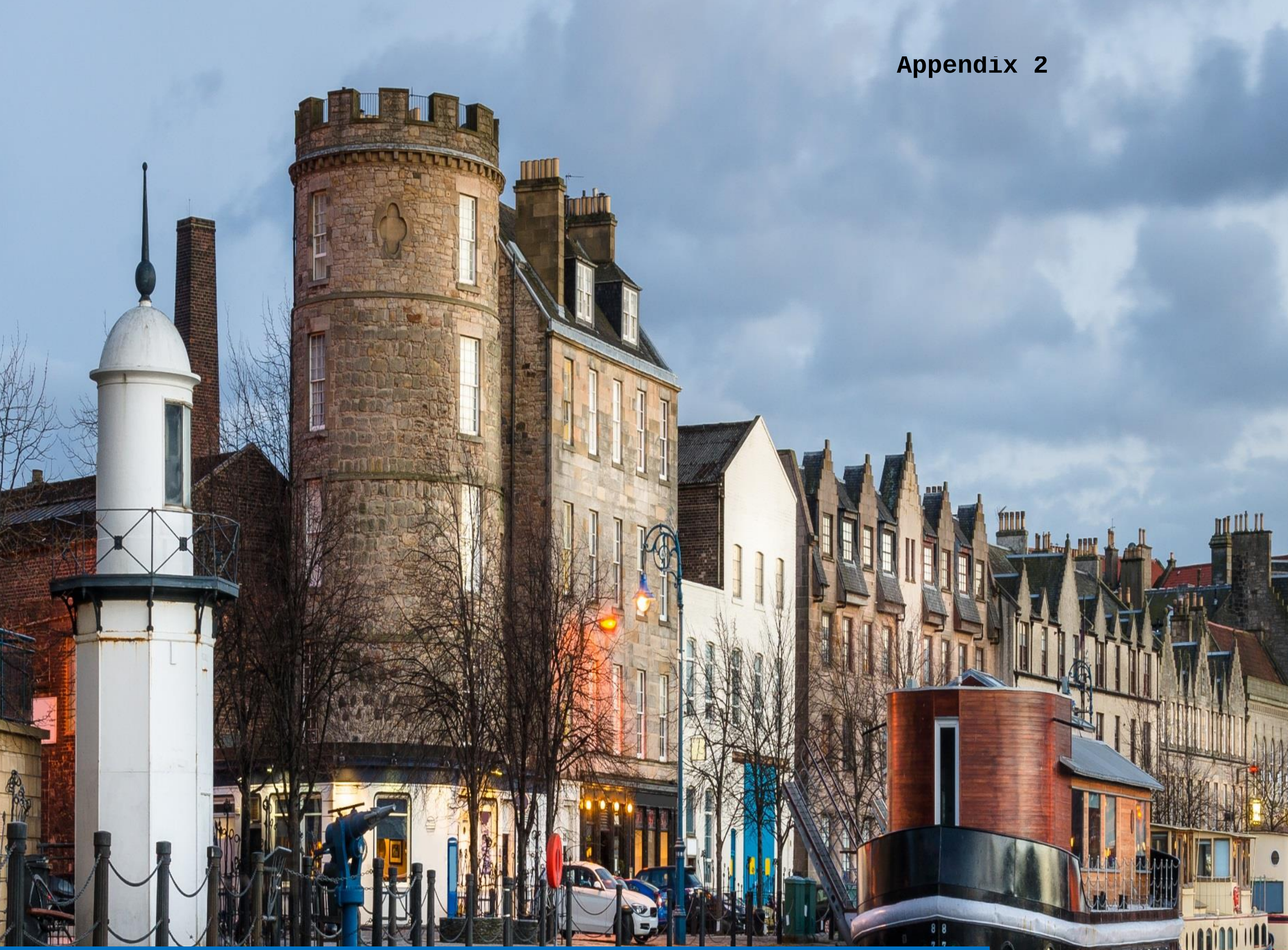
The accounts are prepared from trial balances provided by LPFE Ltd and LPFI Ltd and no significant policies, disclosures, adjustments or estimates are decided by Scott-Moncrieff.

Moore Stephens provided a Financial Conduct Authority Compliance review for LPFI Ltd. The team is independent of Scott-Moncrieff and has no involvement in the audit of Lothian Pension Fund or its subsidiaries.

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

Appendix 2



Audited Annual Report and Accounts 2017/18

Lothian Pension Fund
Lothian Buses Pension Fund
Scottish Homes Pension Fund

Contents

Foreword

Report by the Convener of the Pensions Committee

Following the Council Elections in May 2017 I was reappointed as Convener of City of Edinburgh Council's Pensions Committee for a second term. I am therefore delighted, once again to present the Annual Report and Accounts for the three Funds: Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.

This year the Funds completed their 2017 actuarial valuations which set contribution rates for employers for the three years from 1 April 2018. The funding levels of all three Funds increased from the actuarial valuation in 2014, with good asset returns offsetting increases in the value of the liabilities. Lower interest rates continue to be a challenge to the pension funds and its employers. The actuarial valuations are a significant undertaking from both staff within the Funds, our employers and our Actuary and I would like to thank them for the months of work involved.

2017 also saw the creation of the Fund's Joint Investment Strategy Panel, working alongside Falkirk Council Pension Fund. This is a new phase in our collaborative partnership which should bring further opportunities and efficiencies.

Finally, during the year Sarah Smart stepped down as the Fund's Independent Professional Observer, a position she has held since March 2013. I would like to record my thanks and those of all members of the Pensions Committee and Pension Board for the valuable contribution Sarah made during her time with the Funds.

Councillor Alasdair Rankin
Convener, Pensions Committee, City of Edinburgh Council

Report by the Convener of the Pensions Audit Sub-Committee

The Pensions Audit Sub-Committee, of which I am the Convener, assesses the controls the Funds have in place to ensure effective, efficient and value for money operations. Over 2017/18, the Sub-Committee met four times and one of the key duties is to consider the Funds accounts and the subsequent external audit of them.

Other key areas the Sub-Committee review include the findings from internal audits, considered risk assurance, fraud prevention, tax recovery on investment income and investment custodian services. I believe the Audit Sub-Committee plays a valuable role in the governance of the pension funds and adds value to members and employers.

Councillor Cameron Rose
Convener, Audit Sub Committee, City of Edinburgh Council

Report by the Chair of the Pension Board

The Pension Board forms part of the governance structure that ensures management and administration of the pension funds in accordance with the applicable law and regulation, working together with the Pensions Committee to provide oversight of the Funds operations in a transparent and collaborative manner. The Board is made up of five employer and five member representatives and I have had the pleasure of being a Pension Board member since its establishment in April 2015, serving as Chair this past year. During this year we saw a number of changes in the make-up of the Board with two new members joining, Diane Hogarth and Brian Robertson, while Catrina Warren and Eric Adair both stepped down. I would like to thank both Catrina and Eric for the work they have done with the Board.

The Board attends all meetings of the Pensions Committee and Audit Sub Committee and actively participates in the Funds' governance. Members of the Board undertook 320 hours of training within the year to ensure they are equipped with the knowledge and understanding to enable them to properly exercise the functions of a pension board member. This year the Board reviewed its approach to ensuring members have a good understanding and oversight of the Funds' compliance with The Pension Regulator's code of practice. An agenda planning document was developed to ensure regular Board review of the Funds' alignment with Pensions Regulator guidance, as well as extending the quarterly Pension Board meetings, allowing more time for this compliance activity in addition to critical review of the quarterly Committee papers. Most recently the Board received an update on the Funds' data quality from the scheme manager. Each year, the position of Chair of the Pension Board rotates and I am pleased to say that Jim Anderson was selected to take on the role of Board Chair from 1 April 2018. I look forward to continuing to support the Funds as a regular Board member in future.

Darren May
Scottish Water employer representative and Chair of the Pension Board

Report by the Independent Professional Observer

The Observer role is to assist the Pensions Committee and Pension Board undertake their governance responsibilities effectively and efficiently. Over the year, I provided support to allow them to carry out their roles ensuring the Funds comply with relevant pension legislation and requirements set by The Pensions Regulator.

As with previous years, I held surgeries before each Committee meeting to allow Pensions Committee and Pension Board members to raise questions with me, working collaboratively and efficiently together to ensure their joint oversight of the pension funds. The issues were wide ranging and included investment, actuarial valuations and collaboration and these have all been considered alongside the Funds' normal business. The quality of engagement and discussion over the year has demonstrated a high standard of governance within the Funds. This is my final report as Independent Professional Observer for the Funds. I have enjoyed working with the Pensions Committee and Pension Board and am happy to have contributed to the Funds' governance and the Committee and Board's knowledge on pension matters.

Sarah Smart
Independent Professional Observer to February 2018

Management commentary

Introduction

2017 Actuarial Valuations

During the year, the triennial assessment of the funding position of the pension funds was undertaken by the Funds' Actuary. In general, the results showed that despite better than expected asset returns since the 2014 actuarial valuation, employer costs increased due to a reduction in future expected investment returns. The Funding Strategy Statement was reviewed and amended following consultation with employers.

For Lothian Pension Fund, the funding level increased from 91% at 31 March 2014 to 98% at this valuation. The deficit decreased from £417million at 31 March 2014 to £145million at 31 March 2017. Reflecting the differences in the employers in the Fund, a third investment strategy was introduced for employers which are closed to new entrants but not close to exiting the Fund. To avoid time-consuming employer appeals of the results of the actuarial valuation, this year the Fund introduced a requirement for employers to provide written confirmation that minimum contribution rates set by the Actuary are affordable. It is not in the best interests of the individual employers or the Fund for employers to continue to accrue unaffordable pension liabilities. Four employers indicated that the minimum contribution rates are unaffordable and the Fund is working with them to manage their exit from the Fund. The Fund continues to work with employers to put in place funding agreement to address repayment of debt when an employer leaves, in order to avoid employer default or insolvency.

For Lothian Buses Pension Fund, the funding level on the ongoing basis has risen from 117% in 2014 to 121% at 31 March 2017, showing a surplus of £84million. In comparison, the funding level on a low risk (gilts) basis was 89%, with a deficit of £59million. The actuarial valuation was signed by the Actuary on the basis that the company will continue to pay deficit contributions (if necessary) after the last active member leaves the Fund and it will continue to adopt a long-term investment approach. The company's Admission Agreement is being updated accordingly to strengthen governance and affirm the employer covenant. Further, it was agreed, following consultation with stakeholders and on completion of the revised Admission Agreement, to transfer the assets and liabilities of the Lothian Buses Pension Fund into the Lothian Pension Fund. This merger is expected to deliver investment efficiencies and administrative savings, whilst the assets attributable to this employer retains a bespoke investment strategy.

The funding level for Scottish Homes Pension Fund at 31 March 2017 was 104.7%, increased from 88.8% from the 2014 actuarial valuation. Consultation was undertaken with the Scottish Government on the potential benefits offered by revising the Funding Agreement for this Fund. However, it advised that it does not wish to revisit this and as a result the investments of the Fund are now fully invested in index-linked government bonds and cash.

Cashflow & Investment

All three Funds delivered single digit positive performance over the year, with strong global equity market performance tempered by the strength of sterling. Lothian Pension Fund's assets have increased by £60million, with investments returning 1.4% over the year. 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 assets specifically designed to provide downside protection in times of market stress, together with a currency hedging programme.

The expenditure of all three pension funds continues to exceed income. The investment strategies of the Funds have targeted 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. 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.

The Pensions Committee regularly considers the legal responsibilities of administering the Funds and its fiduciary duty to members and employers. 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. There continues to be significant lobbying from external interest groups on certain investments and the Funds continue to engage with these groups as appropriate.

Customer Service

The quality of membership data continues to be a key area of focus for the Funds to ensure we meet standards set by The Pensions Regulator. All 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. It continues to be a challenge to obtain information from some employers regarding members who have left the scheme. That said, the service continues to be rated highly with 95% of customers assessing the service as ‘excellent’.

During the year, the Funds completed a tender for its pensions administration system, combining the current three systems into one contract to deliver a more integrated, efficient and cost-effective service. Contractual terms and conditions are being finalised with the preferred supplier.

Good progress continues to be made with reconciling pension records for Guaranteed Minimum Pensions ahead of the HMRC deadline in December 2018, with notably this being achieved entirely through internal staff resourcing.

Staffing

In 2015, key investment staff were transferred to LPFE Limited in order to introduce new terms and conditions to reduce retention and recruitment risks facing the Funds. In February 2018, the Funds’ remaining staff transferred to LPFE Limited following consultation with staff and trades unions.
Employing all staff in one organisation will facilitate the collaborative efforts with other local government pension funds and ensure a consistent approach to resourcing.

We also undertook a gender pay gap analysis for the first time this year. We have 57 employees split as 24 male and 33 female. The overall mean and median gender pay gap based on hourly rates of pay was 38.9% and 43.9% respectively.

The figures excluding the Investment Management Team were 16.4% and 0.0% respectively. This data shows that men employed by the Fund are paid, on average, more than women. Although this reflects the industry norm for Investment Management firms, we intend to break that mould and seek innovative ways to achieve gender balance.

Collaboration with other Pension Funds

Collaboration brings tangible benefits to both Lothian Pension Fund and its collaborative partners by investing in greater scale and for other funds to benefit from the commercial advantage of the in-house team. In addition, sharing costs between collaborating funds allows reinvestment in systems and the 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, over recent years. During the year, a Joint Investment Strategy Panel was established, advising the Finance Directors of each administrating authority (the City of Edinburgh Council and Falkirk Council) on implementation of their respective investment strategies. This collaborative structure is expected to deliver significant efficiencies. The Pensions Committee of the respective Councils continue to retain responsibility for their investment strategy and the assets of Lothian Pension Funds and Falkirk Council Pension Fund will remain separate.

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 and Falkirk, supporting Falkirk's strategy to increase its allocation to UK, European and Global infrastructure and giving both Funds greater scale and so access to opportunities that would not have otherwise been available.

Lothian Pension Fund has also continued its collaboration in private markets investment with other Local Government Pension Scheme partners, Falkirk Council Pension Fund and Northern Ireland Local Government Officers' Superannuation Committee and, over the year, Scottish Borders Pension Fund joined the collaboration.

Awards

The Fund retained the Customer Service Excellence award in 2017/18 for the tenth year. A new assessor carried out the assessment this year. The assessor's feedback included that "Lothian Pension Fund are long term holders of the Customer Service Excellence Standard and is to be congratulated in retaining its accreditation and its endorsement of CSE as a key driver for customer focused development." In March 2017, the Fund gained accreditation from Pension Administration Standards Association (PASA), following a three-day visit and our assessment for reaccreditation will take place in 2019.

The Fund received two pension industry awards this year. At the LAPF Investment Awards 2017, the Fund won LGPS Fund of the Year (over £2.5billion) for Lothian Pension Fund and at the Professional Pension's Pension Scheme of the Year Awards won the DB Scheme of the Year (under £500m) for Lothian Buses Pension Fund.

Challenges

The Funds' Service Plan for 2018-2020 shows our plans for the coming years and outlines our ambitions and values:

- to provide an excellent service to our members and employers;
- to provide funding and investment strategies for employers to manage affordability and mitigate risk; and
- to be a partner of choice for other local government pension funds to improve efficiency and sustainability.

The challenge to improve the quality of member data is ongoing. For 2018/19, we have introduced a broader set of performance measures so that we can continue to improve our service. We will continue to liaise with employers to improve the speed of transfer.

New data protection legislation comes into force in May 2018 and the Funds are reviewing and updating processes accordingly. Changes to the Scheme regulations are also expected in 2018 which will bring additional flexibility for members with early retirement and additional voluntary contributions. We will need to communicate these changes to members and employers, and change processes accordingly.

A review of the structure of the Scottish LGPS is expected to be carried out in 2018 which will consider the number of funds across Scotland. We will participate in this consultation and meanwhile we will continue to explore wider opportunities for collaboration to improve services and sustainability.

There will be further oversight and scrutiny of the Funds when the Government analyses the 2017 actuarial valuations of all funds in Scotland and the cost of the benefits in relation to the employer cost cap.

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.

Stephen Moir
Executive Director of Resources
The City of Edinburgh Council
26 September 2018

Clare Scott
Chief Executive
Lothian Pension Fund
26 September 2018

Governance

The City of Edinburgh Council is the administering authority for the Scottish Local Government Pension Scheme (LGPS) in the Lothian area. The Council administers the benefits and invests the assets of three LGPS funds, Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.

Lothian Pension Fund is the second largest LGPS fund in Scotland with assets of £6.7 billion, 90 employers with active members and over 79,000 members.

The Lothian Buses Pension Fund holds assets of £0.5 billion and 3,700 members, while Scottish Homes Pension Fund investments amount to £0.16 billion with 1,600 members.

The Funds maintains a comprehensive website for easy access to all relevant pension information and this is found at www.lpf.org.uk. This includes the Annual Report & Accounts of the three pension funds, Statement of Investment Principles, Funding Strategy Statement and Pensions Administration Strategy and Pensions Discretions Policy.

The Pensions Committee and Pensions Audit Sub-Committee

The day to day running of the Funds is delegated to a specialist team who undertake pension administration, accounting and investment functions, managing the majority of the Funds' assets internally.

All pension matters are delegated to the Pensions Committee of the Council, supported by the Audit Sub Committee, and its members act as 'quasi trustees'. Both Committees held four meetings during the year. The table below shows the Committee members before the Local Government elections held on 4 May 2017 and following the appointment of members by the Council on 29 June 2017.

1 April 2017 to 3 May 2017	From 29 June 2017 to 31 March 2018
Pensions Committee	**Pensions Committee**
Councillor Alasdair Rankin (Convener)	Councillor Alasdair Rankin (Convener)
Councillor Maureen Child	Councillor Maureen Child
Councillor Jim Orr	Councillor Adam McVey (to 14 March 2018)
Councillor Bill Cook	Councillor Claire Miller
Councillor Cameron Rose	Councillor Cameron Rose
	Councillor Neil Ross (from 15 March 2018)
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 (Convener)
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 as described above. 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 representatives appointed by trade unions for the membership of the Funds.

The Pension Board membership for the period 1 April 2017 to 31 March 2018 was as follows. There were two vacancies as of 31 March 2018.

Member representatives

Jim Anderson	Unison
Catrina Warren	Unison (to 20 March 2018)
Thomas Carr Pollock	GMB
Diane Hogarth	Unite (from 13 September 2017)
Brian Robertson	Unite (from 4 August 2017)

Employer representatives

Eric Adair	EDI Group (to 26 March 2018)
Darren May (Chair)	Scottish Water
Sharon Dalli	Police Scotland
Paul Ritchie	East Lothian Council
Alan Williamson	Edinburgh College

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 provided internally covered topics including governance and the joint investment strategy panel, climate change and company engagement, actuarial valuation and the FCA, as well as sessions on collaboration and the LGPS Governance Review.

Committee and Board representatives also attended external conferences including the Pensions and Lifetime Savings Association Local Authority Investment Conference 2017 and the 2017 Local Authority Pension Fund Forum Annual conference. Six members of the Committee and all Pension Board members achieved the required training hours during 2017/18. Pensions Committee members collectively attended 249 hours of training over the year and members of the Pension Board undertook 320 training hours.

Joint Investment Strategy Panel

Investment strategy guidance to the Committee is provided by a Joint Investment Strategy Panel (JISP), working in collaboration with the Falkirk Council Pension Fund. The JISP meets quarterly and includes senior officers and external investment advisers (currently Scott Jamieson and Gordon Bagot). The Pensions Committee of each pension fund agree their own investment strategy but delegate the implementation of strategy, including selection of investment managers, to officers. The JISP advises both pension fund administrating authorities on implementation of investment strategy. The assets of Lothian Pension Fund and Falkirk Council Pension Fund remain separate.

Lothian Pension Fund staff

The team is employed by an arms-length company, LPFE Limited (LPFE), which is wholly owned by the Council (in its capacity as administering authority for the Funds) and it is supervised by a board of directors chaired by the Council's Executive Director of Resources and includes the Convener of the Pensions Committee. The team requires to carry out certain of its activities for the Funds through its Financial Conduct Authority authorised vehicle, LPFI Limited (LPFI). LPFI is also wholly owned by the Council (in its capacity as administering authority for the Funds). LPFI is supervised by a board of directors chaired by the Council's Head of Finance. Both the boards of LPFI and LPFE comprise an independent non-executive director (Leslie Robb). All the operations, costs and liabilities in relation to the Funds, including those of LPFE and LPFI, are borne by the Funds.

The day-to-day running of the three pension Funds is carried out by the Lothian Pension Fund group, comprising the investment and pensions team within the City of Edinburgh Council (acting in its capacity as the administering authority of the Funds), LPFE and LPFI (the LPF Group). The LPF Group's functions includes investment, pension administration, employer liaison, data quality, customer support, accounting, legal, risk and compliance, communications and general business support. The investment responsibilities include carrying out in-house investment management and the monitoring and selection of external investment managers, as well as external facing collaborative initiatives with other like-minded pension funds.

In 2015, key investment staff were transferred to LPFE. As part of the transfer new terms and conditions were introduced to enable the Funds to more effectively manage the risks and controls around its staff and enable it to pursue its collaborative initiatives for the benefit of the Fund's stakeholders within an acceptable tolerance or risk. The remaining staff were transferred to LPFE in January 2018 so that all staff within the LPF Group are employed by LPFE.

Over the year, senior officers from the Council were:

Stephen Moir, Executive Director of Resources, The City of Edinburgh Council
Hugh Dunn, Head of Finance, The City of Edinburgh Council
Katy Miller, Head of Human Resources, The City of Edinburgh Council.

And senior officers from LPFE were:

Clare Scott, Chief Executive Officer 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

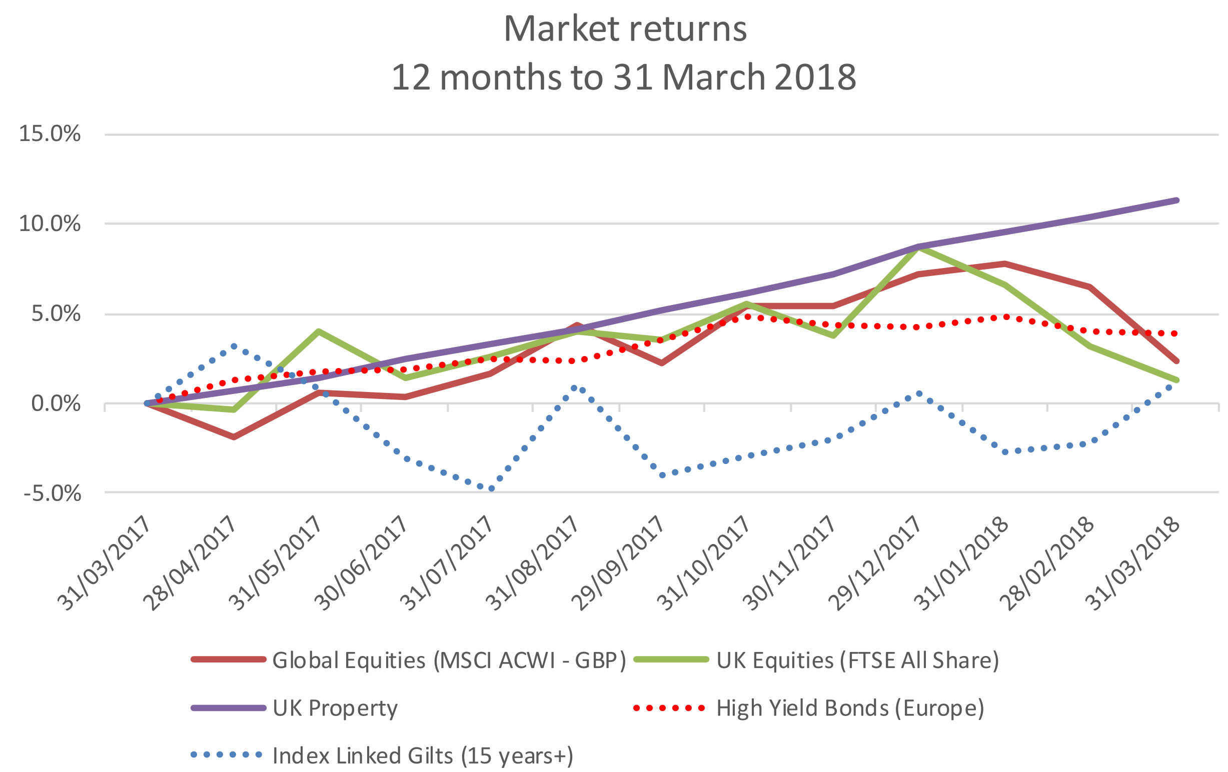
The Scheme Advisory Board for the Local Government Pension Scheme in Scotland was set up following the Public Service Pensions Act 2013. The Board's main function is to advise Scottish Ministers, when requested, on the desirability of changes to the Scheme. They can also provide advice to scheme managers 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 with a Joint Secretary to support each group. During the year, Councillor Rankin was a member and Vice-Chair of the Scheme Advisory Board and Fund officers have also advised the Board and Joint Secretaries. There is more information on the Scheme Advisory Board at www.lgpsab.scot.

Investment

Investment markets

For the 12 months to 31 March 2018, UK equities returned +1.3%, and global equities (in sterling terms) returned +2.4%. Equity market returns for sterling-based investors were dampened by the strength of the pound over the year (global equities returned +11.3% in local currency terms), which reversed much of the fall in value that followed the UK referendum in June 2016. The sharp fall in equity markets during the first quarter of 2018 was also a factor, with markets falling as much as 10% from their January 2018 highs to their lows in late March, before stabilising at the end of the quarter.



Government bond yields in most major markets were broadly unchanged, before rising in early 2018 as stronger US inflation data pushed up expectations that the US Federal Reserve would raise rates faster than previously anticipated, having already raised interest rates three times over 2017. Credit and high yield bond spreads also were broadly unchanged over the year, with high yield spreads in both the US and Europe trading close to their historic lows.

In the UK, the Bank of England increased its base rate as expected in November 2017. However, this was also accompanied by commentary at the time suggesting that further rate rises were less imminent given the Bank's cautious outlook for the economy as the path to the UK's exit from the European Union remains unclear. In Europe, 2017 saw significant positive economic momentum, though more recent data emerging in first quarter of 2018 suggested that economic activity was beginning to slow.

Over the year, the OECD raised its global economic growth forecast for 2017 and for 2018. While the latest global outlook has turned more positive, there remains significant dispersion at country level with the UK economic outlook the weakest of the major economies.

Following the passing of Trump's tax reform programme late in 2017, equities continued to march higher through January, before volatility in late January sent risk assets sharply lower before stabilising in March. Looking ahead, investors face the prospect of further tightening of monetary policy in the US, alongside concerns around increased protectionism and ongoing geo-political tensions concerning Russia, the Middle East and Korea.

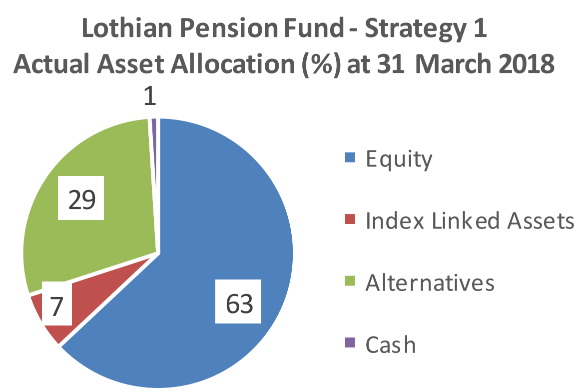
Investment strategies

The investment strategies for all three funds reflect the long-term plans to maintain an acceptable balance between contribution stability and the achievement of positive long term real returns from the assets owned. These plans were initially set during 2012, and reviewed again in 2015/2016, taking into account the results of the 2014 actuarial valuations.

At 31 March 2018, the three funds (Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund) were all invested in range of their target asset allocations, as expected. A review of the Funds' investment strategies will be undertaken again over 2018/2019, taking into account the results of the 2017 actuarial valuations.

Lothian Pension Fund

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.

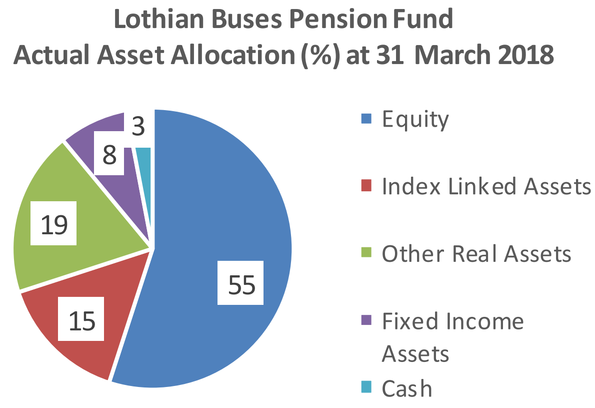


A small number of employers are funded in Strategy 2, which invests in a portfolio of UK index-linked gilts to reduce funding level and contribution rate risk to a level appropriate to their circumstances. The liabilities funded by Strategy 2 represent less than 1% of total Lothian Pension Fund liabilities.

As part of the 2017 actuarial valuation, an additional investment strategy was implemented at the end of the year. For employers who are closed to new members but do not yet qualify for Strategy 2 that aims for the middle ground between Strategy 1 and the lower risk Strategy 2.

Lothian Buses Pension Fund

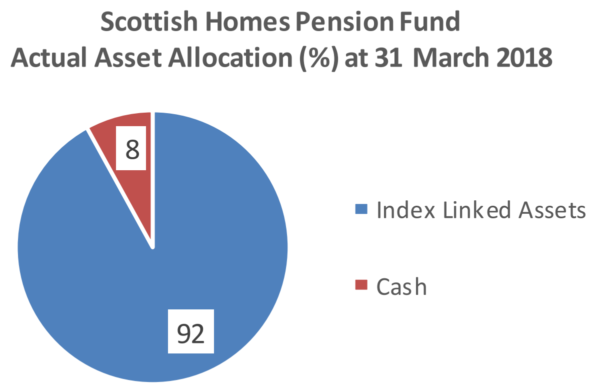
A long-term strategy allocation is in place for the Lothian Buses Pension Fund for the five-year period 2016-21. This was agreed by the Pensions Committee as part of the updated 2015/2016 strategy review. This involves making changes to the asset allocation over that timeframe reflecting the requirement for greater funding stability as the Fund grows and 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.



During the year to 31 March 2018, Lothian Pension Fund and Lothian Buses Pension Fund continued to reduce their equity allocations. This was achieved by redirecting, rather than re-investing, dividend income from equities and distributions from the Funds' private equity holdings. There were increased allocations to alternative assets, including infrastructure investments in the UK and overseas, and further investments in private debt. Over the past 10+ years, the Funds have 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.

Scottish Homes Pension Fund

For Scottish Homes Pension Fund, the year to 31 March 2018 has seen further change. This follows on from the changes at the end of the prior year in March 2017, when the bond and equity portfolios were brought in-house, with the bonds restructured to improve cash-flow matching of the assets with future liability payments.



In September 2017, the fund's target equity allocation was reduced from 15% to 10% as the estimated funding level improved. Over the year, the results of the 2017 actuarial valuation showed a funding level of 104%+, significantly ahead of expectations and achieved primarily through better than anticipated investment returns. Discussions with the Scottish Government, as guarantor to the Fund confirmed that it preferred that the Fund disinvest its remaining equity and property allocation. At 31 March 2018, the Scottish Homes Pension Fund was invested in index-linked gilts and cash, structured to broadly match the expected liability payments as they fall due.

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 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 Lothian Pension Fund, performance has been ahead of benchmark by 1.0% per year over the last five years and this has been achieved with lower risk than the benchmark. 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 governments and politicians encourage public pension funds to increase their investment in this area. Infrastructure investments have the potential to generate attractive risk-adjusted returns, with cash flows often linked to inflation. The long-term and defensive nature of these assets also can provide an element of diversification to the Funds' investment 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, 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 closely with investment managers to ensure execution certainty and to diligence the commercial and legal terms.

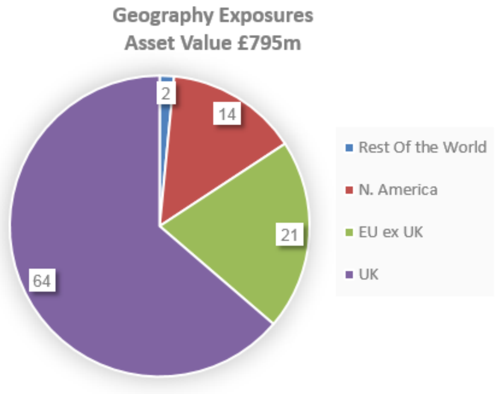
Infrastructure investments represented 11.4% of the value of Lothian Pension Fund assets at 31 March 2018, comprising one of the largest and most diversified allocations among UK LGPS funds. Lothian Buses Pension Fund investments in infrastructure accounted for 9.6% at 31 March 2018. Of the combined £795 million (31 March 2017: £730m) invested in infrastructure across both funds, the majority (64%) is invested in the UK.

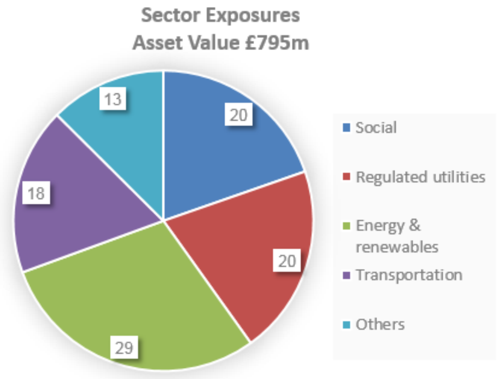
During 2017/18, Lothian Pension Fund and Lothian Buses Pension Fund completed one primary fund investment, acquired two secondary fund interests at discounts to net asset value and invested in five co-investment and/or specified asset investment vehicles. Approximately £105 million has been invested over the year in UK, European and Global infrastructure assets. During the same period, £138 million has been distributed to the Funds.

Investments are across a diverse range of projects, in the areas of:

- social infrastructure (including hospitals, schools and roads);
- regulated utilities (including water and electricity);
- energy & renewables (including solar, wind and hydro, as well as oil and gas storage and distribution);
- transportation (including airports, ports and rail); and
- others (including waste management, car parks and smart meters).

The geographic and sector exposures for the combined Lothian Pension Fund and Lothian Buses Pension Fund infrastructure allocations (at 31 March 2018) are shown in the charts below.





The market value of infrastructure investments in the UK at 31 March 2018 was £507 million. The map and table below shows the location of the Funds' 20 largest major UK infrastructure investments, representing c74% of the UK total (c£375m).

Location	Sector-Subsector	%
Various	Renewables-Solar	5.6
Worthing	Utility-Water	5.6
Livingston	Energy meters	5.4
Redhill	Roads	5.3
Liverpool	Ports	5.3
Isle of Man	Utility-Gas	5.3
Perth	Renewables-Hydro	4.9
Walsall	Utility-Water	4.8
Manchester	Energy meters	4.6
London	Sewage system	4.5
Warwick	Utility-Gas	3.8
North Sea	Pipeline	3.3
Barnsley	Utility-Water	2.5
Newport Pagnell	Motorway services	2.3
West Lothian	Renewables-Wind	2.3
Hertfordshire	Utility-Water	2.0
Edinburgh	Ports	2.0
Folkestone	Rail	1.8
Dudley	Healthcare	1.6
Southern North Sea	Electricity	1.4

Responsible Investment

The Funds have been a strong proponent of responsible investment for many years. It became a signatory to the Principles for Responsible Investment (PRI) in 2008. The PRI, which is supported by the United Nations, encourages investors to use responsible investment to enhance returns and better manage risks. By implementing the six principles (https://www.unpri.org/pri/about-the-pri), the goal of signatories is to develop a more sustainable global financial system.

The PRI undertakes a detailed annual assessment of each signatory and its responsible investment activities. It publishes its findings in two reports (Transparency and Assessment) and, for Lothian Pension Fund, these 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 2017 is very favourable. The Funds are a signatory to the Financial Reporting Council (FRC) UK Stewardship Code. The UK Stewardship Code provides seven principles that institutional investors should adhere to. Lothian Pension Fund is classed as a Tier 1 signatory, due to its close adherence to the code. The Funds also participates in the CDP (Carbon Disclosure Project), an international disclosure system that enables companies, cities, states and regions to measure and manage their environmental impacts.

The Funds receives queries about its approach to responsible investment on a regular basis. In particular, there are groups that lobby for the divestment of certain company shares, or those that operate in certain industries or in certain geographies on ethical grounds. Examples include companies operating in the defense arena, the extraction of fossil fuels and the sale of tobacco or alcohol, and companies operating in controversial areas of the world, such as the occupied territories of Palestine. The issues raised by lobby groups often involve complex social, legal and moral issues.

Whilst the Funds are sympathetic to some of the issues raised, it has its own obligations to fulfil within the constraints of the legal setting. 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).

Its approach is widely followed across the industry and reflects the fact that its primary objective is to pay pensions to its members when they fall due and it strives to do this by investing in a responsible manner, which includes engagement with companies. It does not have a policy of exclusion. Its policy is to engage with the companies in which it owns shares with a view to improving corporate behaviour to the benefit of shareholders. By doing this, the Funds aim to satisfy its most important social responsibility, which is to its members and employers by providing pensions, and it believes that this approach will also provide wider societal benefits.

It is important to note that the Funds invest only in legal businesses and that it 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 its fiduciary duty to provide the highest standard of stewardship on behalf of the members and employers.

Investment Process

The Funds' (and the industry's) investment processes have evolved over the years to include a greater focus on ESG issues, risks and opportunities. ESG issues can clearly affect the financial performance of the companies in which the Funds invests. As a signatory to the Principles for Responsible Investment, the Funds are obliged to incorporate ESG issues into investment analysis and decision-making processes (Principle 1).

Investment opportunities are assessed with a view to meeting a required level of financial return in the context of achieving an appropriate level of risk, and ESG issues are part of that assessment. ESG factors are an important element of investment risk and opportunity, and there is evidence that the shares of companies with improving ESG ratings are better investments than those that are simply highly rated. As such, engaging with companies to improve their positions on ESG issues can lead to better long-term outcomes for the Funds. However, it is also important to note that the Funds do disinvest from shares where it considers financial risk to be unrewarded.

The Funds' internal portfolios are actively managed using both fundamental and quantitative investment processes. For the portfolios managed on a fundamental basis, ESG factors are formally assessed as part of the due diligence process before shares are purchased, supported by the research of a specialist third party service (currently MSCI ESG Research), which provides ESG specific data, analysis and research to help identify the risks and opportunities that companies face. This ensures that consideration of ESG factors can be applied to the investment process using data that has been collated in a consistent manner.

The Funds' external managers are also selected and appointed after due consideration of their approach to integrating ESG considerations into their investment processes. Their activities, including scrutiny of how ESG considerations affected investment decisions, are monitored by the Funds quarterly.

Climate Change

Climate change concerns have prompted governments around the world to implement policies to limit global temperature increases. The Funds' recognise that such policies will affect 'fossil fuel' companies in a significant way. However not all 'fossil fuels' are equal. Gas is much cleaner than coal - gas and renewables are expected to grow their share of the energy mix at the expense of coal. Many 'fossil fuel' companies are investing heavily in cleaner fuels and renewables – while they are part of the problem, they are also part of the solution.

Lothian Pension Fund has carried out a carbon footprint exercise to aid research, engagement and monitoring activities. The results show a footprint almost identical to its benchmark although it should be noted that there are limitations on the data used in these exercises. The Funds believes that divestment of 'fossil fuels' as a policy will have little or no impact on company operations.

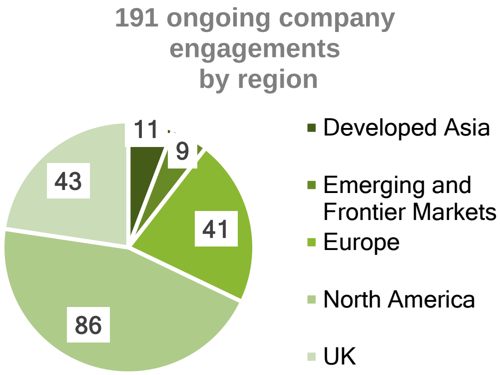
As highlighted above, the Funds have been researching opportunities and invests in the renewable sector within the private market for several years with renewables, including wind, solar and hydro assets, valued at £113m at 31 March 2018.

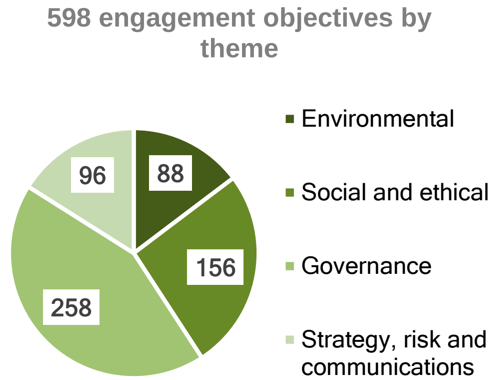
Voting and Engagement

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.

During 2017/18, voting and engagement activities related to the Funds' shareholdings were largely undertaken by Hermes Equity Ownership Services (EOS), with Baillie Gifford taking responsibility for the investments they manage on behalf of the Funds. A summary of these activities is provided in the charts below. The Funds' influence with investee companies is enhanced through Hermes EOS' aggregate representation for over £330bn in assets at 31 March 2018.

Hermes EOS collates voting and engagement data for the Funds and reports this for calendar year periods. During calendar year 2017, the Funds voted at the annual meetings of the 517 companies in which it was invested. There were votes on 7,446 resolutions, and the Funds opposed 614 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. More details can be found on the Funds' website www.lpf.org.uk.





Engagement activities are also undertaken on behalf of the Funds and approximately 70 other UK Local Government Pension Scheme in the UK by the Local Authority Pension Fund Forum (LAPFF). Councillor Alasdair Rankin, Convener of the Pensions Committee, is a member of the Executive Committee of the LAPFF. Membership of the LAPFF Executive entails meeting with the boards of companies and attending company Annual General Meetings to represent shareholders' interests.

Funding Strategy Statement

The Funding Strategy Statement covers the funding strategies of each of the three Funds and can be viewed on our website at www.lpf.org.uk.

The purpose of the Funding Strategy Statement is:

- to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward;
- to support the regulatory framework to maintain as nearly constant employer contribution rates as possible; and
- to take a prudent longer-term view of funding those liabilities.

These objectives are desirable individually but may be mutually conflicting.

The Funding Strategy Statement also ensures that the regulatory requirements to set contributions to ensure the solvency and long-term cost efficiency of the Funds, (as defined by the Public Service Pensions Act 2013) are met.

The Funding Strategy Statement was revised at the 2017 Actuarial Valuation. In addition to updates required as a result of changes to the Scheme Regulations and other guidance, changes included:

- the introduction of a new medium risk investment strategy, and;
- the requirement for employers to confirm commitment to contribution rates.

As required by Scheme regulations, the Funds consulted with employers as part of the review process.

The Funds must be able to meet all benefit payments as and when they fall due. These payments will be met by contributions (resulting from the funding strategy), or asset returns (resulting from the investment strategy). A formal review of the Funds' investment strategies is undertaken at least every three years to ensure appropriate alignment with liabilities. Further information on the investment strategies can be found in the Funds' Statement of Investment Principles also available at www.lpf.org.uk.

Financial Performance

Administration expenses

A summary of the Funds' administrative expenditure for 2017/18, against the budget approved by Pensions Committee, is shown in the table below. This budget includes adjustment agreed by Pensions Committee as part of the collaboration business case.

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 £27,127k against budgeted of £27,808k represented an underspending of £681k (2.4%) for the Funds. The key budget variances serving to generate this underspending were:-

- Investment management fees - £867k overspend. This budget also includes investment management fees deducted from capital, but excludes the performance related element of these charges due to their unpredictable nature. During the year there was higher than expected deal flow for infrastructure and private debt assets which contributed to the overspend. Broker commission for the first three quarters of the period included research costs which had been budgeted separately in third party payments.
- Other third-party payments - £549k underspend. The rollout of direct investment broker research invoicing was delayed until the final quarter of the year. From April to December 2017 these charges continued to be paid via commission, with approximately £325k of this underspend offsetting the investment management fees for the year. The Funds did not suffer any broken deal costs in relation to its co-investment infrastructure investments during the period which contributed to the underspend.
- Supplies and Services - £606k underspend. Delays in the implementation of the investment front office system and further collaboration work resulted in the underspend for the period.
- 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	3,210	2,747	(463)
Property	201	195	(6)
Plant and Transport	41	33	(8)
Supplies and Services	1,594	988	(606)
Investment Managers Fees*	22,300	23,167	867
Other Third-Party Payments	1,404	855	(549)
Capital funding - Depreciation	82	80	(2)
Direct Expenditure	28,832	28,065	(767)
Support Costs	286	250	(36)
Income	(1,310)	(1,188)	(122)
Total net controllable cost to the Funds	**27,808**	**27,127**	**(681)**

**Does not include performance elements*

Reconciliation to total costs

	Actual outturn
	£000
Actual outturn on budgeted items above	27,127
Add back securities lending revenue included in income above	865
Investment management fees deducted from capital – performance related element	9,322
IAS19 LPFE retirement benefits	1,030
LPFE deferred tax on retirement benefits	(175)
Total cost to the Funds (inclusive of full investment management fees)	38,169
Per Fund Accounts	
Lothian Pension Fund group	35,412
Lothian Buses Pension Fund	2,523
Scottish Homes Pension Fund	234
Total	**38,169**

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.

Lothian Pension Fund continued to experience 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 by demographic and economic factors. Outlays exceeded receipts by £17.0million representing a £7.9million change in position from 31 March 2017 (net withdrawals of £9.1million).

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 2018, outlays from dealing with members remained in excess of receipts, by £2.8million for 2017/18. This represents a change of £0.1million on the position as at 31 March 2017, where net outlays totaled £2.7million. 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 which is consistent with the previous year.

It is anticipated that for the next few years these cash flow trends will remain broadly consistent.

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.

In May 2018, CIPFA published "Proposals for LGPS Fund Reporting in a 'Pooled World'". "This …. sets out proposals for revised reporting for LGPS pension funds to meet a number of objectives", including "to further enhance reporting of costs reflecting the introduction of the LGPS SAB Code of Transparency for asset managers, and initiatives underway by the Financial Conduct Authority (FCA) and Department for Work and Pensions (DWP) which aim to create more transparent and granular reporting standards for both providers and trustees …. This paper has been issued by CIPFA as good practice which is to be incorporated into 2018/19 Annual Report guidance for local government pension funds. It would be helpful however if funds could also apply the guidance when preparing their 2017/18 annual reports and feedback any practical issues encountered. Proposals can then be refined as necessary before the Annual Report guidance is finalised." Although this contains explicit reference to the SAB in England and Wales and to the applicable pooling arrangements, it is anticipated that CIPFA Guidance will be revised on a UK wide basis.

The financial statements of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund continue to include full transparency of all investment management fees.

	Investment management expenses in compliance with CIPFA guidance	Investment management expenses per 2017/18 financial statements	Disclosure in excess of CIPFA guidance
	£000	**£000**	**£000**
Lothian Pension Fund	27,687	33,261	5,574
Lothian Buses Pension Fund	2,086	2,424	338
Scottish Homes Pension Fund	165	165	0
TOTAL	**29,938**	**35,850**	**5,912**

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 331 global pension funds representing £6.2 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 0.41% of Fund assets are significantly lower than CEM's benchmark cost of 0.48%, an equivalent annual saving of approximately £4.3m. This saving largely reflects the fact that the Funds manage 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

An extensive risk register is maintained covering a wide range of issues across investments and benefit operations. The register is subject to internal review each quarter and a summary is reported to the Pensions Committee and Pensions Audit Sub-Committee. On an annual basis the Pensions Audit Sub-Committee reviews the register.

Risk Management

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

As at 31 March 2018, the most significant risks (after taking account of risk reduction controls), as assessed using a score out of 100 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
Recruitment and retention of appropriate key staff	6	6	36
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	8	8	64
Human Resource within the Division not sufficient to carry out core task in conjunction with active or anticipated projects.	6	6	36

Risk Assurance

The Funds operate a bespoke assurance framework designed to ensure they meets their objectives, are adequately resourced, managed to high professional standards, meet legislative requirements and have high customer satisfaction.

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. We set challenging performance standards and measure these through key indicators reported to our Pensions Committee and Pension Board and internal indicators reported to internal management.

Key Performance indicators 2017/18

We achieved all but one key indicator in 2017/18 except for the issuing of benefits statements. The table shows our performance against these indicators with a narrative on the performance highlights.

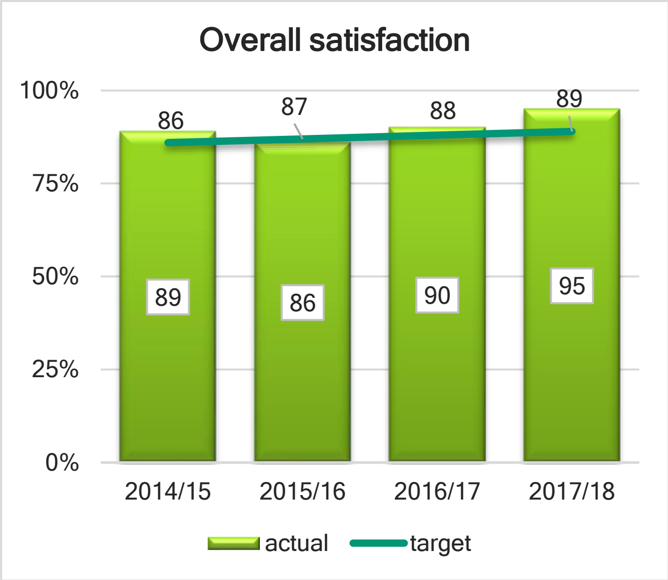
	Target	Actual
Maintain Customer Service Excellence Standard	Retain	**Yes**
Overall satisfaction of employers, active members and pensioners with our services as measured by surveys	89%	**95.2%**
Proportion of active members receiving a benefit statement by 31 August 2017	100%	**99.9%**
Proportion of critical pensions administration work completed within standards	Greater than 90%	**94.8%**
All staff complete at least two days training a year	Yes	**Yes**
Level of sickness absence	Less than 4%	**1.55%**
Staff survey satisfaction	75%	**82%**
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	**met**
Contributions received within 19 days of the end of the month to which they relate	99.0%	**99.7%**

Key achievements in 2017/18

- Set up Joint Collaborative working with Falkirk Council Pension Fund
- Maintained Customer Service Excellence and Pensions Administration Standards Association accreditation
- Transferred remaining staff to LPFE
- Successfully completed the Actuarial Valuation 2017
- Completed 90% Guaranteed Minimum Pension (GMP) reconciliation with HMRC carried out inhouse.
- Provide other Scottish LGPS funds access to alternative investment through club deals
- Retained Customer Service Excellence for 10th year
- Winner – Professional Pension Scheme of the Year Awards 2017 (to £500m).

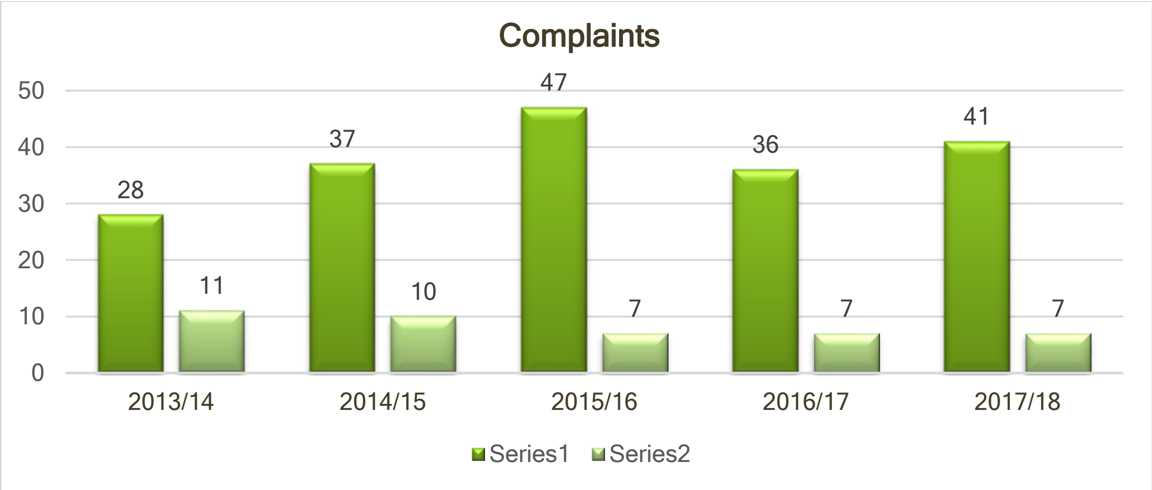
Customer feedback

Listening to feedback is key to our services, with the Funds carrying out surveys to monitor individual and overall satisfaction. Our overall satisfaction question is included in all our surveys and continues to improve rising to 95% this year from 90% in 2016/17. This exceeds the target of 89%.



We also monitor complaints and ensure we respond and resolve where possible, within 20 working days. We investigate and learn from both formal and informal complaints to ensure we are continuously improving our services. Complaints are split by those about the service we provide and those about how scheme regulations are applied.

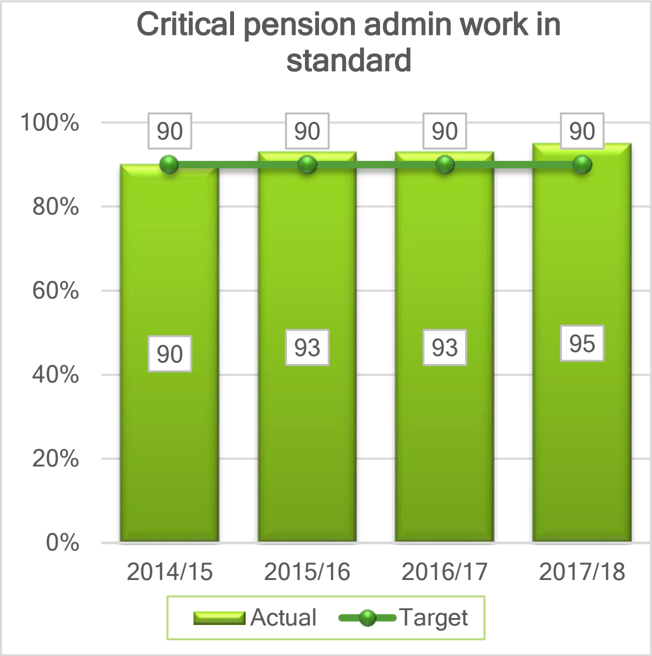
We carried out 23,500 processes in 2017/18 and there were very few complaints made, less than 0.1%. Complaints covered a broader range of issues including taking small pensions as a cash lump sum and the time it took to pay a CETV to new pension providers.



Our data

We issued 99.9% of benefit statements by the statutory deadline of 31 August 2017 with the remaining 26 statements being issued after. All employers are submitting contribution data monthly and the majority had cleaner membership data and fewer queries at the end of the year. The data of some employers continues to require significant attention.

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.



We measure our pension record keeping standards against The Pension Regulator's best practice guidance. Poor record-keeping can lead to significant additional costs in areas such as administration, error correction, claims from members as well as fines from The Pensions Regulator. Over the year, we have continued data cleansing with our employers and carried out significant additional work as part of the Actuarial Valuation. We are also carrying out external tracing of members where we do not hold a current address.

	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%

For 2018/19, we are planning to use new tools that will provide more comprehensive analysis of membership data. This should allow us to identify and improve data quality and the service to our members.

Pension Administration

The introduction of the career average pension scheme in April 2015 has meant that pension administration has become more complex for both the Funds and employers.

We continue to review our processes to improve our performance so that the Funds can meet new challenges and deliver an excellent service to members.

Despite the challenging environment, 95% of key procedures in 2017/18 were completed in target.

Employer performance

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 referring 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; and
- Failure to provide details of member contributions monthly.

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

Overall employer performance for 2017/18 is shown below, with 2016/17 shown for comparison purposes.

		2016/17			2017/18		
Case type	**Target (working days)**	**Number received**	**Number within target**	**% within target**	**Number received**	**Number within target**	**% within target**
New members	20	4,764	4,074	86%	6,204	5,439	88%
Leavers	20	3,425	1,421	42%	2,460	1,058	43%
Retirements	20	1,244	440	35%	1,050	427	41%
Deaths in Service	10	29	21	72%	26	13	50%

The majority of new starter information continues to be received within target in most cases and the increase in number received is due to auto-enrolment regulations. For leavers, whilst the provision of leaver information in target has increased slightly, the majority continue to be received out of target. We continue to target historical cases with employers and provide missing leaver queries to employers monthly.

Unfortunately, most retirement information continues to be provided out of target. This year we saw a large increase in the number of 'early' retirements where members are over age 60 but are taking their pension benefits with a permanent actuarial reduction.

Payment of employer contributions

We monitor the payment of employer contributions as employers are required under the Pensions Act 1995 to pay contributions by the 19th of the month after the deduction was made. This is a key performance indicator with a target of was 99% contributions paid in time.

99.77% of contributions by value were paid on time. Of the 1,152 payments made, 21 were paid later than the 19th and these are shown in the table below.

Employer	Number of late payments	Employer	Number of late payments
Dean Orphanage & Cauvins Trust	2	Cyrenians	1
Enjoy East Lothian	2	Four Square	1
Homeless Action Scotland	2	Into Work	1
ISS UK Ltd	2	Open Door Accommodation Project	1
Skanska	2	Scotland's Learning Partnership	1
Barony Housing Association Ltd	1	Scottish Police Services Authority	1
Centre for the Moving Image	1	Visit Scotland	1
Children's Hearing Scotland	1	Young Scot Enterprise	1
		TOTAL	21

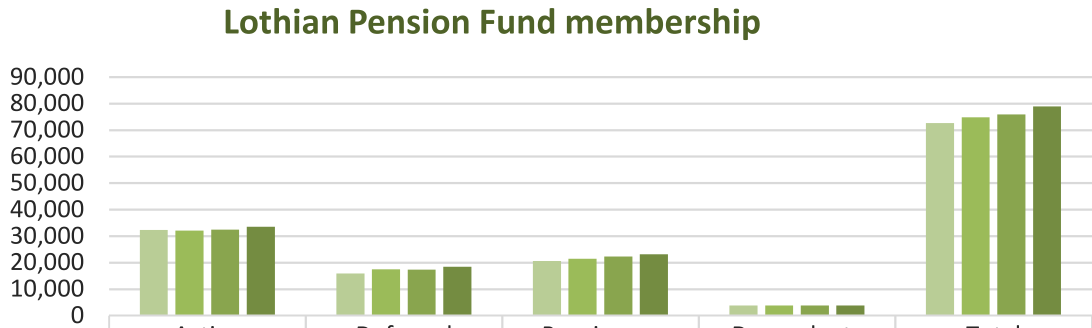
Management commentary approved by:

ANDREW KERR
Chief Executive
The City of Edinburgh Council
26 September 2018

CLARE SCOTT
Chief Executive
Lothian Pension Fund
26 September 2018

JOHN BURNS
Chief Financial Officer
Lothian Pension Fund
26 September 2018

Lothian Pension Fund



	Active	Deferred	Pensioners	Dependants	Total
31 March 2015	32,273	15,916	20,636	3,810	72,635
31 March 2016	32,079	17,444	21,371	3,849	74,743
31 March 2017	32,457	17,299	22,315	3,842	75,913
31 March 2018	33,528	18,384	23,119	3,825	78,856

Investment Strategy

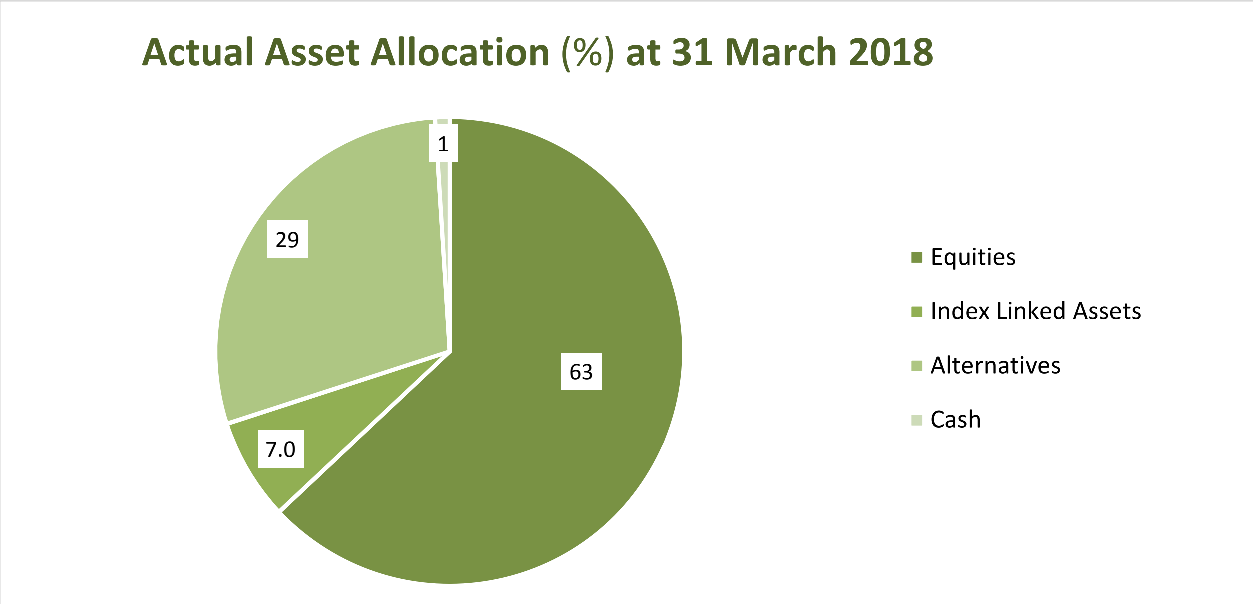
In order to provide suitable investment strategies for the differing requirements of employers, the Fund currently operates two investment strategies. Most employer liabilities are funded under Strategy 1, which adopts a long-term investment strategy, aiming to maximise the investment return within reasonable 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 Assets and Alternatives, which are the key determinants of investment risk and return.

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 as these employers approach exit from the Fund. The liabilities funded by Strategy 2 represent less than 1% of total liabilities.

The plan for the Fund's investment strategy was initially set during 2012, and reviewed again in 2015/2016, taking into account the results of the 2014 actuarial valuation. A review of investment strategy will be undertaken again over the coming months, taking into account the results of the latest 2017 actuarial valuation.

The Fund's strategy incorporates a gradually changing risk profile for the Fund, but retains significant exposure to real 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. Prior to the 2012-17 investment strategy, the targeted allocation was 71.5% Equities, 5% Index-Linked gilts, 22.5% Alternatives and 1% Cash. The 2012-17 strategy is shown in the table below.

Strategy 1	**Long term Strategy 2012 - 2017 %**	**Permitted ranges %**
Equities	65	50 - 75
Index Linked Assets	7	0 - 20
Alternatives	28	20 - 35
Cash	0	0 - 10
Total	**100**	**n/a**



A key objective of the Fund's investment strategy is to reduce risk and this is largely achieved by reducing risk within the equity pool of assets. Implementation of the strategy has involved a shift from a regional to a global manager structure. Significant steps have been taken in this regard in prior years with the introduction of the internally managed global equity portfolios. As such, 2017/18 represented much more of a "steady state" in terms of the structure within the equity exposure.

The activity in recent years has been to increase the proportion of internally managed global equity strategies to reduce investment risk. The resultant equity pool of assets is expected to perform relatively well when equity markets are weak and produce good positive absolute returns in rising equity markets.

Almost 85% of the Fund's listed equities are 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 also hedges exposures to the currencies of overseas listed equities with the explicit aim of reducing volatility rather than seeking to generate improved returns. The Fund therefore maintains exposure to currencies that are expected to reduce volatility, such as the US Dollar and Japanese Yen which tend to fall as equities rise, and hedges exposure to currencies that are expected to increase volatility, such as the Australian Dollar which tends to rise as equities rise.

Investment performance

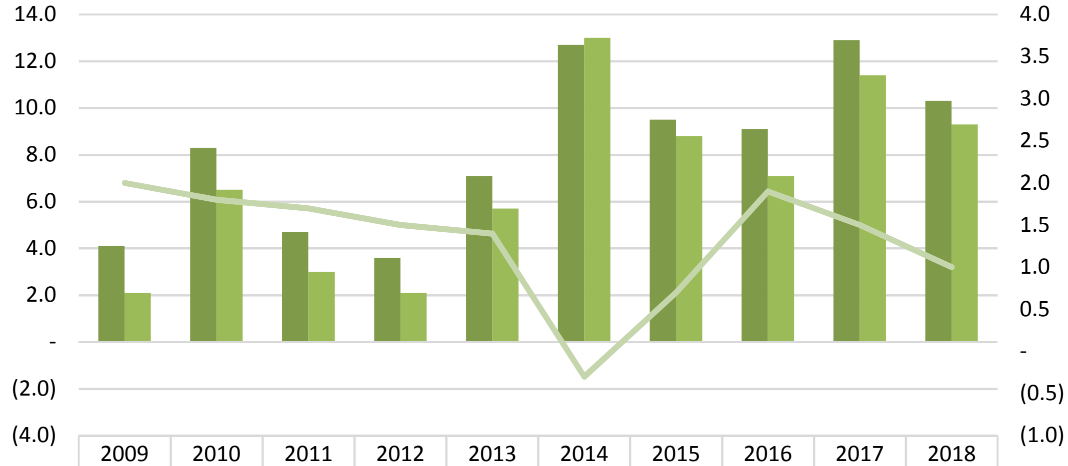
The Fund's performance over the last year and over longer-term timeframes is shown in the table below.

Annualised returns to 31 March 2018 (% per year)	1 year	5 year	10 years
Lothian Pension Fund - Strategy 1	1.4	10.3	8.7
Benchmark*	3.6	9.3	7.5
Lothian Pension Fund - Strategy 2 (from 2015)	0.5	-	-
Benchmark	0.5	-	-
Actuarial Valuation Assumptions - Strategy 1 **	3.2	4.8	5.4
Actuarial Valuation Assumptions - Strategy 2 **	1.7		
Retail Price Index (RPI)	3.3	2.3	2.8
Consumer Price Index (CPI)	2.5	1.4	2.3
National Average Earnings	2.4	2.6	1.6

*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)



	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fund	4.1	8.3	4.7	3.6	7.1	12.7	9.5	9.1	12.9	10.3
Benchmark	2.1	6.5	3.0	2.1	5.7	13.0	8.8	7.1	11.4	9.3
Relative (RHS)	2.0	1.8	1.7	1.5	1.4	(0.3)	0.7	1.9	1.5	1.0

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 performance of Strategy 2 was in line with benchmark over the year, returning +0.5%. Performance of this strategy has also been in line with benchmark since inception (29 March 2016), with a return of +10.1% per annum.

The Fund's return has exceeded its objective of meeting the benchmark return over the economic cycle, with both the 5 and 10 year return ahead of benchmark. The direction of the Fund's performance when markets are increasing and decreasing is one way of measuring volatility. The lower volatility objective and strategy for Strategy 1 was put in place in December 2013 and over this period market volatility has been relatively benign, for the most part. Nevertheless, performance since the change in structure (with the launch of the global low volatility equity portfolio and the shift from regional passive to active) indicates that the Fund is delivering returns with lower volatility than its benchmark.

For Strategy 1, fund performance since January 2014 to March 2018 has been:

- better than the strategic allocation when markets fell (17 out of 51 months) with average performance of 0.32% better than the strategic benchmark and,
- very marginally worse than the strategic allocation when markets were rising (34 out of 51 months) with average performance 0.03% behind the strategic benchmark.

Risk analysis also shows that the portfolio is positioned well if markets fall significantly.

Lothian Pension Fund

Fund Account for year ended 31 March 2018

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 2016/17 £000	Lothian Pension Fund Group 2016/17 £000		Note	Lothian Pension Fund Parent 2017/18 £000	Lothian Pension Fund Group 2017/18 £000
		Income			
153,735	153,735	Contributions from employers	**4**	148,821	148,821
42,578	42,578	Contributions from members	**5**	43,421	43,421
5,536	5,536	Transfers from other schemes	**6**	4,191	4,191
201,849	**201,849**			**196,433**	**196,433**
		Less: expenditure			
141,778	141,778	Pension payments including increases	**7**	149,384	149,384
48,895	48,895	Lump sum retirement payments	**8**	42,533	42,533
6,384	6,384	Lump sum death benefits	**9**	6,359	6,359
615	615	Refunds to members leaving service		596	596
361	361	Premiums to State Scheme		129	129
11,098	11,098	Transfers to other schemes	**10**	12,517	12,517
1,895	1,954	Administrative expenses	**11b**	1,950	2,151
211,026	**211,085**			**213,468**	**213,669**
(9,177)	**(9,236)**	**Net (withdrawals)/additions from dealing with members**		**(17,035)**	**(17,236)**
		Returns on investments			
153,016	153,016	Investment income	**12**	163,869	163,869
1,044,952	1,044,952	Change in market value of investments	**14, 19b**	(43,288)	(43,288)
(27,375)	(27,712)	Investment management expenses	**11c**	(32,643)	(33,261)
1,170,593	**1,170,256**	**Net returns on investments**		**87,938**	**87,320**
1,161,416	**1,161,020**	**Net increase in the Fund during the year**		**70,903**	**70,084**
5,434,014	5,433,871	**Net assets of the Fund at 1 April 2017**		6,595,430	6,594,891
6,595,430	**6,594,891**	**Net assets of the Fund at 31 March 2018**		**6,666,333**	**6,664,975**

Lothian Pension Fund

Net Assets Statement as at 31 March 2018

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

Lothian Pension Fund Parent 31 March 2017 £000	Lothian Pension Fund Group 31 March 2017 £000		Note	Lothian Pension Fund Parent 31 March 2018 £000	Lothian Pension Fund Group 31 March 2018 £000
		Investments			
6,570,547	6,570,547	Assets		6,633,467	6,633,467
(1,798)	(1,798)	Liabilities		(5,112)	(5,112)
6,568,749	**6,568,749**	**Net investment assets**	**13**	**6,628,355**	**6,628,355**
		Non current assets			
259	259	Debtors	**23**	1,525	1,525
248	248	Computer systems		168	168
50	-	Share Capital		60	-
-	117	Deferred tax	**28a**	-	292
557	**624**			**1,753**	**1,985**
		Current assets			
4,467	4,467	The City of Edinburgh Council	**27**	2,784	2,784
27,278	27,362	Cash balances	**20, 27**	47,024	47,117
14,938	14,965	Debtors	**24**	15,564	15,634
46,683	**46,794**			**65,372**	**65,535**
		Non current liabilities			
-	(685)	Retirement benefit obligation	**29**	-	(1,715)
-	**(685)**			**-**	**(1,715)**
		Current liabilities			
(20,559)	(20,591)	Creditors	**25**	(29,147)	(29,185)
(20,559)	**(20,591)**			**(29,147)**	**(29,185)**
6,595,430	**6,594,891**	**Net assets of the Fund at 31 March**		**6,666,333**	**6,664,975**

The unaudited accounts were issued on 27 June 2018 and the audited accounts were authorised for issue on 26 September 2018.

JOHN BURNS FCMA CGMA
Chief Finance Officer, Lothian Pension Fund
26 September 2018

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 114.

2 Lothian Pension Fund Group

Basis of consolidation, presentation of financial statements and notes

Commencing with the year ended 31 March 2017, 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
27	Related party transactions and balances Describes transactions during the year and balances at year end which relate to the parent and the companies.
28a	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.
28b	Consolidated Lothian Pension Fund group - LPFE Limited and LPFI Limited - share capital Describes the share capital of the Company.
29	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.

Prior to the consolidation of the group accounts the LPFE and LPFI boards met on the 28th May 2018 and approved their respective audited financial statements for 2017/18. The figures used in the consolidation are from these audited financial statements.

3 Events after the Reporting Date

There have been no events since 31 March 2018, and up to the date when these accounts were authorised, that require any adjustments to these accounts.

At its meeting on 26 March 2018, the Pensions Committee approved the merger of the assets and liabilities of the Lothian Buses Pension Fund into the Lothian Pension Fund at the earliest suitable date (to be determined by the Executive Director of Resources), subject to the satisfactory completion of a revised admission agreement and shareholder guarantee.

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	2016/17 £000	2017/18 £000
Future service rate	133,301	136,968
Past service deficit	7,668	7,694
Strain costs	12,558	2,747
Cessation contributions	208	1,412
	153,735	148,821

By employer type	2016/17 £000	2017/18 £000
Administering Authority	63,542	55,041
Other Scheduled Bodies	71,426	73,692
Community Admission Bodies	18,312	19,629
Transferee Admission Bodies	455	459
	153,735	148,821

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	2016/17 £000	2017/18 £000
Administering Authority	15,345	15,633
Other Scheduled Bodies	20,993	21,475
Community Admission Bodies	6,099	6,161
Transferee Admission Bodies	141	152
	42,578	43,421

Notes to the Accounts

6 Transfers in from other pension schemes

	2016/17 £000	2017/18 £000
Group transfers	-	-
Individual transfers	5,536	4,191
	5,536	4,191

7 Pensions payable

By employer type	2016/17 £000	2017/18 £000
Administering Authority	70,547	73,922
Other Scheduled Bodies	58,364	61,729
Community Admission Bodies	12,687	13,537
Transferee Admission Bodies	180	196
	141,778	149,384

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	2016/17 £000	2017/18 £000
Administering Authority	26,340	16,623
Other Scheduled Bodies	18,503	20,650
Community Admission Bodies	3,900	5,131
Transferee Admission Bodies	152	129
	48,895	42,533

9 Lump sum death benefits payable

By employer type	2016/17 £000	2017/18 £000
Administering Authority	2,578	3,375
Other Scheduled Bodies	3,312	2,571
Community Admission Bodies	488	413
Transferee Admission Bodies	6	-
	6,384	6,359

Notes to the Accounts

10 Transfers out to other pension schemes

	2016/17 £000	2017/18 £000
Group transfers	173	-
Individual transfers	10,925	12,517
	11,098	12,517

11a Total management expenses

In accordance with CIPFA, the below analysis looks at the combined administration and investment management expenses in notes 11b and c and splits out the costs to include a third category covering oversight and governance expenditure. Administration costs such as Actuarial fees and Investment Management expenses such as investment consultancy would instead be shown in the Oversight and governance costs category.

	LPF Parent 2016/17 £000	LPF Group 2016/17 £000	LPF Parent 2017/18 £000	LPF Group 2017/18 £000
Administrative costs	1,686	1,719	1,615	1,801
Investment management expenses	26,345	26,592	31,620	31,918
Oversight and governance costs	1,239	1,355	1,359	1,693
	29,270	29,666	34,594	35,412

11b Administrative expenses

	LPF Parent 2016/17 £000	LPF Group 2016/17 £000	LPF Parent 2017/18 £000	LPF Group 2017/18 £000
Employee Costs	1,093	1,098	1,143	1,167
The City of Edinburgh Council - other support costs	132	132	-	-
System costs	231	231	292	293
Actuarial fees	64	64	116	116
External/Internal audit fees	41	49	65	71
Legal fees	60	60	2	2
Printing and postage	79	79	115	115
Depreciation	57	57	57	57
Office costs	110	110	102	102
Sundry costs less sundry income	28	18	58	57
IAS19 retirement benefit adjustments - see note 29		66	-	206
Deferred tax on retirement benefit obligation - see note 28a		(10)	-	(35)
Corporation tax losses utilised by CEC group - see note 27	-	-	-	-
	1,895	1,954	1,950	2,151

LPFE Ltd, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer 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.

Notes to the Accounts

11c Investment management expenses

	LPF Parent 2016/17 £000	LPF Group 2016/17 £000	LPF Parent 2017/18 £000	LPF Group 2017/18 £000
External management fees -				
invoiced	3,970	3,970	4,270	4,270
deducted from capital (direct investment)	15,245	15,245	18,642	18,642
deducted from capital (indirect investment)	4,157	4,157	5,574	5,574
Securities lending fees	155	155	173	173
Transaction costs - Equities	956	956	1,148	1,148
Property operational costs	558	558	337	337
Employee costs	1,116	1,149	1,272	1,375
Custody fees	300	300	368	368
Engagement and voting fees	82	82	86	86
Performance measurement fees	50	50	62	62
Consultancy fees	64	64	49	49
Research fees	-	-	65	65
System costs	245	245	299	300
Legal fees	210	210	61	89
The City of Edinburgh Council - other support costs	111	111	-	-
Depreciation	7	7	7	7
Office costs	85	85	78	78
Sundry costs less sundry income	64	(1)	152	(54)
IAS19 retirement benefit adjustments - see note 29	-	439	-	824
Deferred tax on retirement benefit obligation - see note 28	-	(70)	-	(140)
Corporation tax losses utilised by CEC group - see note 27	-	-	-	8
	27,375	27,712	32,643	33,261

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 £8.9m (£6.6m direct, £2.3m indirect) in respect of performance-related fees compared to £4.0m in 2016/17 (£3.9m direct, £0.1m indirect).

It should be noted that Lothian 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 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 25. This further disclosure highlights an extra £5.6m in costs (2017 £4.2m).

Notes to the Accounts

12 Investment income

	2016/17 £000	2017/18 £000
Income from fixed interest securities	3,589	4,006
Dividends from equities	120,326	131,588
Unquoted private equity and infrastructure	5,646	7,601
Income from pooled investment vehicles	1,111	5,130
Gross rents from properties	23,085	23,079
Interest on cash deposits	597	675
Stock lending and sundries	775	865
	155,129	172,944
Irrecoverable withholding tax	(2,113)	(9,075)
	153,016	163,869

Included within the dividend from equities income for the year is cross border withholding tax yet to be received. These reclaims have a high certainty of success and are completed and managed by the Fund's custodian Northern Trust. For the period of 2017/18 £4,014k of the stated income relates to tax yet to be received. At the 31st March 2018 £7,135k (including prior periods) of investment income receivable related to cross border withholding tax. The Fund monitors these claims to ensure its optimum tax efficiency and provides an annual progress report to the Pensions Audit Sub-Committee.

Notes to the Accounts

13 Net investment assets

Investment Assets	Region	31 March 2017 £000	31 March 2018 £000
Bonds			
Public sector fixed interest	UK	156,876	153,585
Public sector index linked gilts quoted	UK	502,439	508,572
		659,315	662,157
Equities			
Quoted	UK	655,522	528,882
Quoted	Overseas	3,564,953	3,481,292
		4,220,475	4,010,174
Pooled investment vehicles			
Private equity, infrastructure, private debt & timber	UK	457,647	495,441
Private equity, infrastructure, private debt & timber	Overseas	556,623	567,141
Property	UK	67,969	66,638
Other	UK	19,191	867
		1,101,430	1,130,087
Properties			
Direct property	UK	356,741	392,743
		356,741	392,743
Derivatives			
Derivatives - forward foreign exchange		1,081	12,121
		1,081	12,121
Cash deposits			
Deposits		216,036	407,689
		216,036	407,689
Other investment assets			
Due from broker		1,320	2,677
Dividends and other income due		14,521	15,819
		15,841	18,496
Total investment assets		6,570,919	6,633,467
Investment liabilities			
Derivatives			
Derivatives - forward foreign exchange		(424)	(204)
		(424)	(204)
Other financial liabilities			
Due to broker		(1,746)	(4,908)
		(1,746)	(4,908)
Total investment liabilities		(2,170)	(5,112)
Net investment assets		6,568,749	6,628,355

Notes to the Accounts

14a Reconciliation of movement in investments and derivatives

	Market value at 31 March 2017 £000	Purchases at cost & derivative payments £000	Sale & derivative receipts £000	Change in market value £000	Market value at 31 March 2018 £000
Bonds	659,315	38,157	(35,692)	377	662,157
Equities	4,220,475	878,940	(929,194)	(160,047)	4,010,174
Pooled investment vehicles	1,101,430	64,330	(145,328)	109,655	1,130,087
Property	356,741	40,758	(17,329)	12,573	392,743
Derivatives - futures	-	11	163	(174)	-
Derivatives - forward foreign exchange	657	2,968	(3,711)	12,003	11,917
	6,338,618	1,025,164	(1,131,091)	(25,613)	6,207,078
Other financial assets / liabilities					
Cash deposits*	216,036			(17,667)	407,689
Broker balances*	(426)			(8)	(2,231)
Investment income due*	14,521			-	15,819
	230,131			(17,675)	421,277
Net financial assets	6,568,749			(43,288)	6,628,355

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 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					
Cash deposits*	227,409			21,837	216,036
Broker balances*	17,205			(383)	(426)
Investment income due*	12,380			-	14,521
	256,994			21,454	230,131
Net financial assets	5,398,963			1,044,952	6,568,749

** As per CIPFA disclosures the change in market value intentionally does not balance opening/closing market values*

Notes to the Accounts

14d Reconciliation of fair value measurements within level 3

Pooled investments	Market value at 31 March 2017	Level 3 transfers in	Level 3 transfers out	Purchases at cost & derivative payments	Sales & derivative receipts	Unrealised gains / (losses)	Realised gains / (losses)	Market value at 31 March 2018
Infrastructure	663,194	-	-	107,269	(111,609)	31,841	36,874	727,569
Property	67,969	-	-	-	(3,204)	6,801	(4,928)	66,638
Private Equity	129,311	-	-	297	(50,137)	(24,246)	35,178	90,403
Timber	132,532	-	-	-	(15,114)	(9,241)	3,220	111,397
Private debt	89,233	-	-	53,368	(15,317)	5,704	230	133,218
Freehold Property	356,741	-	-	40,758	(17,329)	5,842	6,731	392,743
	1,438,980	-	-	201,692	(212,710)	16,701	77,305	1,521,968

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 2018

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	48,179	82,284	3,213	-
Up to one month	AUD	GBP	6,793	3,915	-	(202)
Up to one month	GBP	CAD	108,389	180,036	8,875	-
Up to one month	JPY	USD	33,328	314	-	(1)
Up to one month	ZAR	USD	4,359	369	-	(1)
One to six months	USD	CHF	9,264	8,695	33	-

Open forward currency contracts at 31 March 2018	12,121	(204)
Net forward currency contracts at 31 March 2018		11,917
Prior year comparative		
Open forward currency contracts at 31 March 2017	1,081	(424)
Net forward currency contracts at 31 March 2017		657

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 2017 £000	% of total 31 March 2017 %	Market value at 31 March 2018 £000	% of total 31 March 2018 %
In-house	UK all cap equities	130,362	2.0	139,655	2.1
In-house	UK mid cap equities	121,061	1.8	131,607	2.0
Total UK equities		251,423	3.8	271,262	4.1
In-house	European ex UK equities	120,393	1.8	130,696	2.0
In-house	US equities	150,941	2.3	146,279	2.2
Total regional overseas equities		271,334	4.1	276,975	4.2
In-house	Global high dividend	928,720	14.1	856,911	12.9
In-house	Global low volatility	1,162,921	17.7	1,097,057	16.6
In-house	Global multi factor value	985,286	15.0	934,708	14.1
Harris	Global equities	263,263	4.0	273,298	4.1
Nordea	Global equities	280,815	4.3	268,444	4.0
Total global equities		3,621,005	55.1	3,430,418	51.7
In-house	Currency hedge	708	0.0	11,885	0.2
Total currency overlay		708	0.0	11,885	0.2
Total listed equities		4,144,470	63.1	3,990,540	60.2
In-house	Private equity unquoted	129,311	2.0	90,403	1.4
In-house	Private equity quoted	75,902	1.2	61,885	0.9
Total private equity		205,213	3.2	152,288	2.3
Total equity		4,349,683	66.3	4,142,828	62.5
In-house	Index linked gilts	450,833	6.9	455,930	6.9
In-house	Gold	19,652	0.3	-	-
Total inflation linked assets		470,485	7.2	455,930	6.9
In-house	Property	38,038	0.6	37,447	0.6
Standard Life	Property	414,574	6.3	454,430	6.8
Total property		452,612	6.9	491,877	7.4
In-house	Infrastructure unquoted	663,194	10.1	727,569	11.0
In-house	Infrastructure quoted	23,548	0.4	18,981	0.3
In-house	Timber	132,532	2.0	111,397	1.7
Total other real assets		819,274	12.5	857,947	13.0
In-house	Secured loans	14,142	0.2	-	0.0
In-house	Private debt	89,233	1.4	133,218	2.0
In-house	Sovereign bonds	159,307	2.4	158,280	2.4
Total debt assets		262,682	4.0	291,498	4.4

Notes to the Accounts

16 Investment managers and mandates (cont)

Manager	Mandate	Market value at 31 March 2017 £000	% of total 31 March 2017 %	Market value at 31 March 2018 £000	% of total 31 March 2018 %
In-house	Cash	159,645	2.4	332,090	5.0
In-house	Transitions	92	0.0	1,614	0.0
Total cash and sundries		159,737	2.4	333,704	5.0
Strategy 1 financial assets		6,514,473	99.2	6,573,784	99.2
In-house	Mature employer gilts	54,276	0.8	54,571	0.8
Strategy 2 financial assets		54,276	0.8	54,571	0.8
Net financial assets		6,568,749	100.0	6,628,355	100.0

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

17 Securities lending

During the year Lothian Pension Fund participated in a securities lending arrangement with the Northern Trust Company. As at 31 March 2018, £254.9m (2017 £220.3m) of securities were released to third parties. Collateral valued at 105.5% (2017 104.6%) of the market value of the securities on loan was held at that date.

18 Property holdings

	2016/17 £000	2017/18 £000
Opening balance	356,280	356,741
Additions	4,675	40,875
Disposals	(2,358)	(17,329)
Net change in market value	(1,856)	12,456
Closing balance	356,741	392,743

As at 31 March 2018, 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 of £850,000 for the planning, design and contractor procurement to potentially re-develop 100 St John Street, London

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

	2016/17 £000	2017/18 £000
Within one year	22,526	23,327
Between one and five years	67,195	66,574
Later than five years	99,741	101,160
	189,462	191,061

Notes to the Accounts

19 Financial Instruments

19a 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.

Classification of financial instruments - parent	31 March 2017			31 March 2018		
	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
Investment assets						
Bonds	659,316	-	-	662,156	-	-
Equities	4,220,475	-	-	4,010,174	-	-
Pooled investments	1,101,430	-	-	1,130,087	-	-
Property Leases	6,243	-	-	4,376	-	-
Derivative contracts	1,081	-	-	12,121	-	-
Margin balances	-	-	-	-	-	-
Cash	-	216,036	-	-	407,689	-
Other balances	-	15,841	-	-	18,496	-
	5,988,545	231,877	-	5,818,914	426,185	-
Other assets						
City of Edinburgh Council	-	4,467	-	-	2,784	-
Cash	-	27,278	-	-	47,024	-
Share Capital	-	50	-	-	60	-
Debtors - current	-	14,937	-	-	15,564	-
Debtors - non-current	-	259	-	-	1,525	-
	-	46,991	-	-	66,957	-
Assets total	5,988,545	278,868	-	5,818,914	493,142	-
Financial liabilities						
Investment liabilities						
Derivative contracts	(424)	-	-	(204)	-	-
Other investment balances	(1,746)	-	-	(4,908)	-	-
	(2,170)	-	-	(5,112)	-	-
Other liabilities						
Creditors	-	-	(20,559)	-	-	(29,147)
Liabilities total	(2,170)	-	(20,559)	(5,112)	-	(29,147)
Total net assets	5,986,375	278,868	(20,559)	5,813,802	493,142	(29,147)

	31 March 2017	31 March 2018
Total net financial instruments	6,244,684	6,277,797
Amounts not classified as financial instruments	348,707	388,536
Total net assets - parent	6,593,391	6,666,333

Notes to the Accounts

19a Classification of financial instruments (cont)

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

	31 March 2017			31 March 2018		
	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
Other assets						
Cash	-	84	-	-	93	-
Share Capital	-	(50)	-	-	(60)	-
Debtors - current	-	27	-	-	70	-
Debtors - non-current	-	117	-	-	292	-
	-	178	-	-	395	-
Assets total	-	178	-	-	395	-
Other liabilities						
Retire. benefit obligation	-	-	(685)	-	-	(1,715)
Creditors	-	-	(32)	-	-	(38)
Liabilities total	-	-	(717)	-	-	(1,753)
Total net assets	-	178	(717)	-	395	(1,753)

	31 March 2017	31 March 2018
Total adjustments to net financial instruments	(539)	(1,358)
Total net assets - group	6,592,852	6,664,975

19b Net gains and losses on financial instruments

	2016/17 £000	2017/18 £000
Designated as fair value through fund account	1,025,354	(38,186)
Loans and receivables	21,454	(17,675)
Financial liabilities at amortised cost	-	-
Total	1,046,808	(55,861)
Gains and losses on directly held freehold property	(1,856)	12,573
Change in market value of investments per fund account	1,044,952	(43,288)

Notes to the Accounts

19c 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.

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 2018			
	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
Investment assets				
Designated as fair value through fund account	4,023,162	662,156	1,135,464	5,820,782
Non-financial assets at fair value through profit and loss	-	-	386,500	386,500
Loans and receivables	426,185	-	-	426,185
Total investment assets	4,449,347	662,156	1,521,964	6,633,467
Investment liabilities				
Designated as fair value through fund account	(5,112)	-	-	(5,112)
Total investment liabilities	(5,112)	-	-	(5,112)
Net investment assets	4,444,235	662,156	1,521,964	6,628,355

Notes to the Accounts

19c Fair Value Hierarchy

	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

20 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.

Notes to the Accounts

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

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:

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	10.0%
Fixed Interest Gilts	6.5%
Index-Linked Gilts	11.0%
Infrastructure	12.0%
Property	13.0%
Cash	1.0%

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.

Notes to the Accounts

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

	Value at 31 March 2018 £m	% of fund %	Potential Change +/- %	Value on increase £m	Value on decrease £m
Equities - Developed Markets	3,770	56.9	20.5	4,542.9	2,997.2
Equities - Emerging Markets	208	3.1	30.0	270.4	145.6
Private Equity	152	2.3	30.0	197.6	106.4
Timber and Gold	111	1.7	18.0	131.0	91.0
Secured Loan	133	2.0	10.0	146.3	119.7
Fixed Interest Gilts	158	2.4	6.5	168.3	147.7
Index-Linked Gilts	511	7.7	11.0	567.2	454.8
Infrastructure	747	11.3	12.0	836.6	657.4
Property	492	7.4	13.0	556.0	428.0
Cash and forward foreign exchange	346	5.2	1.0	349.5	342.5
Total [1]	6,628	100.0	17.2	7,765.8	5,490.3
Total [2]			13.8	7,545.6	5,710.4
Total [3]			13.9	7,551.4	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.

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.

Notes to the Accounts

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

Cash deposits

At 31 March 2018, cash deposits represented £454.7m, 6.82% of total net assets. This was held with the following institutions:

	Moody's Credit Rating at 31 March 2018	Balances at 31 March 2017 £000	Balances at 31 March 2018 £000
Held for investment purposes			
Northern Trust Global Investment Limited - liquidity funds	Aaa-mf	83,249	8,075
Northern Trust Company - cash deposits	Aa2	40,697	308,831
The City of Edinburgh Council - treasury management	See below	92,090	90,783
Total investment cash		216,036	407,689
Held for other purposes			
The City of Edinburgh Council - treasury management	See below	27,278	47,024
Total cash - parent		243,314	454,713
Cash held by LPFE/LPFI Limited			
Royal Bank of Scotland	A3	84	93
Total cash - group		243,398	454,806

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.

	Moody's Credit Rating at 31 March 2018	Balances at 31 March 2017 £000	Balances at 31 March 2018 £000
Money market funds			
Deutsche Bank AG, London	Aaa-mf	652	596
Goldman Sachs	Aaa-mf	14	1
Standard Life Investments Sterling Liquidity Fund	Aaa-mf	-	20,424
Bank call accounts			
Bank of Scotland	Aa3	11,911	13,606
Royal Bank of Scotland	A3	169	501
Santander UK	Aa3	30	361
Barclays Bank	A1	2	11
Svenska Handelsbanken	Aa2	23	676
HSBC Bank PLC	Aa3	4	51
UK Pseudo-Sovereign risk instruments			
Other Local Authorities [1]	Aa1	106,563	101,580
		119,368	137,807

[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 2018 was 'Aa1').

20 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

(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.

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 2018, the Fund was owed £11.9m 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.

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 77% (2017 78%)) of the Fund's investments could be converted to cash within three months in a normal trading environment.

21 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.

Notes to the Accounts

22 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 £7,791m (2017 £8,210m). 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 2017 % p.a.	31 March 2018 % p.a.
Inflation / pensions increase rate	2.4	2.4
Salary increase rate	4.4	4.1
Discount rate	2.6	2.7

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2016 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 2017		31 March 2018	
	Males	Females	Males	Females
Current pensioners	22.1 years	23.7 years	21.7 years	24.3 years
Future pensioners (assumed to be currently 45)	24.2 years	26.3 years	24.7 years	27.5 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.

23 Non-current Debtors

	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000	LPF Parent 31 March 2018 £000	LPF Group 31 March 2018 £000
Contributions due - employers' cessation	259	259	1,525	1,525
	259	259	1,525	1,525

In accordance with the Funding Strategy Statement and in recognition of severe affordability constraints facing the charitable sector, “Funding Agreements” have been put in place to allow certain former employers to repay cessation valuation debt over longer terms (up to twenty years), to avoid potential default or insolvency.

The above debtors all relate to community admission bodies.

Notes to the Accounts

24 Debtors

	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000	LPF Parent 31 March 2018 £000	LPF Group 31 March 2018 £000
Contributions due - employers	11,434	11,434	11,586	11,586
Contributions due - members	3,304	3,304	3,517	3,517
Benefits paid in advance or recoverable	-	-	33	33
Sundry debtors	160	193	92	163
Corporation tax losses utilised by CEC group	-	1	-	-
Prepayments	283	292	325	335
LPFE & LPFI Limited Loan facility - see note 28	16	-	11	-
	15,197	15,224	15,564	15,634

Analysis of debtors	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000	LPF Parent 31 March 2018 £000	LPF Group 31 March 2018 £000
Administering Authority	6,081	6,081	6,122	6,122
Other Scheduled Bodies	6,477	6,477	7,061	7,061
Community Admission Bodies	2,158	2,158	1,926	1,926
Transferee Admission Bodies	35	35	33	33
Other Local Authorities	22	56	7	43
Central Government Bodies	-	-	-	-
Other entities and individuals	424	417	415	449
	15,197	15,224	15,564	15,634

25 Creditors

	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000	LPF Parent 31 March 2018 £000	LPF Group 31 March 2018 £000
Benefits payable	5,745	5,745	6,914	6,914
VAT, PAYE and State Scheme premiums	2,940	3,052	1,432	1,571
Contributions in advance	8,719	8,719	18,290	18,290
Miscellaneous creditors and accrued expenses	2,760	2,809	1,982	2,167
Office - operating lease	266	266	243	243
LPFE Loan facility - see note 28	24	-	-	-
Intra group creditor - see note 28	105	-	287	-
	20,559	20,591	29,148	29,185

Notes to the Accounts

25 Creditors (cont)

Analysis of Creditors

	LPF Parent 31 March 2017 £000	LPF Group 31 March 2017 £000	LPF Parent 31 March 2018 £000	LPF Group 31 March 2018 £000
Administering Authority	51	51	295	295
Other Scheduled Bodies	11,715	11,715	18,251	18,251
Community Admission Bodies	19	19	28	28
Transferee Admission Bodies	-	-	-	
Central Government Bodies	2,889	3,001	1,432	1,571
Other entities and individuals	5,885	5,805	9,142	9,040
	20,559	20,591	29,148	29,185

26 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.

Total contributions during year for Lothian Pension fund	2016/17 £000	2017/18 £000
Standard Life	339	305
Prudential	1,816	1,983
	2,155	2,288

Total value at year end for Lothian Pension Fund	31 March 2017 £000	31 March 2018 £000
Standard Life	5,041	4,705
Prudential	5,097	6,259
	10,138	10,964

27 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.

LPFE Ltd which is a wholly owned subsidiary 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.

Notes to the Accounts

27 Related parties (cont)

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 2017 £000	31 March 2018 £000
Year end balance of holding account	4,467	2,784
	4,467	2,784

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 2018, the fund had an average investment balance of £117.1m (2016/17 £105.7m). Interest earned was £482k (2016/17 £427.4k).

Year end balance on treasury management account	31 March 2017 £000	31 March 2018 £000
Held for investment purposes	92,090	90,783
Held for other purposes	27,278	47,024
	119,368	137,807

Scheme employers

All scheme employers to the fund are (by definition) related parties, a full list of employers can be found on page 69. The employer contributions for the ten largest scheme employers are as follows -

	31 March 2017 £000	31 March 2018 £000
City of Edinburgh Council	63,542	50,041
West Lothian Council	22,214	22,895
East Lothian Council	13,267	13,812
Midlothian Council	11,849	13,148
Scottish Water	9,191	9,526
Edinburgh Napier University	5,001	4,938
Heriot-Watt University	3,077	3,324
Scottish Police Authority	3,519	2,945
Edinburgh College	2,924	2,289
Audit Scotland	2,020	1,944

Governance

As at 31 March 2018, all members of the Pensions Committee, with the exception of Richard Lamont, and all members of the Pension Board, were members of the Lothian Pension Fund or Lothian Buses Pension Fund, with one member of the Pension Board in reciept 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 Accounts

27 Related parties (cont)

During the period from 1 April 2017 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 City of Edinburgh Council members of staff, 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 2017 £000	Accrued CETV as at 31 March 2018 £000
Stephen Moir*	Executive Director of Resources, City of Edinburgh Council	-	22
Hugh Dunn*	Head of Finance, City of Edinburgh Council	1,251	949
Katy Miller*	Head of Human Resources, City of Edinburgh Council **	29	51
Clare Scott*	Chief Executive Officer, Lothian Pension Fund	221	270
Bruce Miller	Chief Investment Officer, Lothian Pension Fund	267	334
Struan Fairbairn	Chief Risk Officer, Lothian Pension Fund	46	64
John Burns	Chief Finance Officer, Lothian Pension Fund	538	624
Esmond Hamilton	Financial Controller, Lothian Pension Fund	200	238

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

** Appears due to being a Director in LPFE Ltd

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

	31 March 2017 £000	31 March 2018 £000
Short-term employee benefits	380	415
Post-employment benefits - employer pension contributions	78	85

Key management personnel employed by LPFE, had accrued pensions totalling £97,456 (1 April 2017: £81,825) and lump sums totalling £110,889 (1 April 2017: £100,185) 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 £1,380 of which £198 was due at the year end and for LPFI Limited interest payable was £168 of which there was none due at year end. At 31 March 2018, the balance on the loan facility was £10k due to LPFE Limited and a zero balance from LPFI Limited.

Notes to the Accounts

27 Related parties (cont)

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 2018, the Fund was invoiced £1,450k (2017 £1,073k) for the services of LPFE Limited staff, £288k (2017 £105k) of this remained payable at year end.

28a Consolidated Lothian Pension Fund Group - LPFE Limited & LPFI Limited - deferred tax

Movement in deferred tax asset (Non-current asset)	LPF Group 2016/17 £000	LPF Group 2017/18 £000
At 1 April 2017	36	117
Credit for year to Fund Account	81	175
At 31 March 2018	117	292

Elements of closing deferred tax asset	LPF Group 31 March 2017 £000	LPF Group 31 March 2018 £000
Pension liability	117	292
	117	292

28b Shares in group companies - LPFE Limited & LPFI Limited

	31 March 2017 £	31 March 2018 £
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	60,000
	50,001	60,001

**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.*

29 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

29 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 2017 £000	% of total 31 March 2017 %	Fair value at 31 March 2018 £000	% of total 31 March 2018 %
Equity securities:	Consumer	425	15.0	1,185	14.0
	Manufacturing	429	15.2	1,288	15.0
	Energy and utilities	210	7.4	541	6.0
	Financial institutions	197	7.0	769	9.0
	Health and care	166	5.9	424	5.0
	Information technology	140	4.9	528	6.0
	Other	195	6.9	543	6.0
Debt securities:	Corporate Bonds	-	0.0	169	2.0
	UK Government	284	10.0	839	10.0
	Other	6	0.2	-	0.0
Private equity:	All	91	3.2	158	2.0
Real property	UK property	191	6.7	556	6.0
	Overseas property	-	0.0	9	0.0
Investment funds and unit trusts:	Equities	-	0.0	83	1.0
	Commodities	8	0.3	-	0.0
	Bonds	42	1.5	-	0.0
	Infrastructure	253	8.9	1,025	12.0
	Other	60	2.1	20	0.0
Derivatives:	Foreign Exchange	-	0.0	4	0.0
Cash and cash equivalents:	All	131	4.8	511	6.0
		2,828	100.0	8,652	100.0

Amounts recognised in the Net Assets Statement	LPF Group 31 March 2017 £000	LPF Group 31 March 2018 £000
Fair value of Fund assets	2,828	8,652
Present value of Fund liabilities	(3,513)	(10,367)
	(685)	(1,715)

Notes to the Accounts

29 Retirement benefits obligation - group (cont)

Movement in the defined benefit obligation during the period

	LPF Group 2016/17 £000	LPF Group 2017/18 £000
Brought forward	2,277	3,513
Current service cost	172	336
Interest cost on obligation	86	131
Fund participants contributions	76	7,175
Benefits paid	-	
Actuarial losses arising from changes in financial assumptions	902	(788)
Actuarial losses arising from changes in demographic assumptions	-	
Other actuarial losses	-	
Balance at year end	3,513	10,367

Movement in the fair value of Fund assets during the period

	LPF Group 2016/17 £000	LPF Group 2017/18 £000
Brought forward	2,097	2,828
Benefits paid	-	
Interest income on Fund assets	80	104
Contributions by employer	156	204
Contributions by member	76	91
Contributions in respect of unfunded benefits	-	-
Unfunded benefits paid	-	(4)
Effect of business combinations and disposals	-	5,711
Return on assets excluding amounts included in net interest	419	(282)
Balance at year end	2,828	8,652

Amounts recognised in the Fund Account

	LPF Group 2016/17 £000	LPF Group 2017/18 £000
Interest received on Fund assets	(80)	(104)
Interest cost on Fund liabilities	86	131
Current service costs	172	336
Transfer of opening retirement benefit obligation on 1 May 2015	-	-
Actuarial gains due to re-measurement of the defined benefit obligation	902	(788)
Return on Fund assets (excluding interest above)	(419)	282
Net cost recognised in Fund account	661	(143)
Less - cash flows	(156)	(204)
Increase in retirement benefit obligations	505	(347)

Notes to the Accounts

29 Retirement benefits obligation - group (cont)

Principal actuarial assumptions used in this valuation	31 March 2017 % p.a.	31 March 2018 % p.a.
Inflation / pensions increase rate	2.4	2.3
Salary increase rate	4.4	4.0
Discount rate	2.7	2.7

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 2017		31 March 2018	
	Males	Females	Males	Females
Current pensioners	22.1 years	23.7 years	21.7 years	24.3 years
Future pensioners	24.2 years	26.3 years	24.7 years	27.5 years

Expected employer contributions to the defined benefit plan for the year ended 31 March 2019 are £415,000, based on a pensionable payroll cost of £1,742,000.

30 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 2017 £000	31 March 2018 £000
Outstanding investment commitments	235,565	202,723
	235,565	202,723

Notes to the Accounts

30 Contractual commitments (cont)

Office accommodation - 144 Morrison Street, Edinburgh

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

	31 March 2017 £000	31 March 2018 £000
Within one year	115	115
Between one and five years	345	345
After five years	877	762
	1,337	1,222

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 £85.1k.

31 Contingent assets and liabilities

Contribution refunds

At 31st March 2018, Lothian Pension Fund had £894k in unclaimed refunds due to members.

Employer Cessations

As stated in note 23, "In accordance with the Funding Strategy Statement and in recognition of severe affordability constraints facing the charitable sector, "Funding Agreements" have been put in place with certain former employers to repay cessation valuation debt"…. In exceptional circumstances, this includes "repayment of less than the cessation debt in order to avoid employer insolvency, with an appropriate agreement which allows the Fund to revisit the repayment of the remaining debt at a future date (i.e. the debt would be a contingent liability and hence not recognised on an employer's balance sheet); and seeking, where appropriate, suitable "anti-embarrassment" provisions in legal agreement covering future increase in employer asset values". At 31 March 2018, such contingent assets of the Fund totalled £1,635k.

EU Tax claims & income recovery

The Fund participates in various claims to recover withheld investment income. EU tax claims relate to the recovery of tax deducted from dividend payments prior to receipt or payable tax credits thereon. The claims can be divided into three main types – "Manninen" / Foreign Income Dividends (Fids), "Fokus Bank" and Manufactured Dividends. Given the high level of uncertainty as to the eventual success of such claims from EU tax authorities, no accrual of income is made in the financial statements. The value of these outstanding claims is approximately £9.8m. To date, the amount of tax recovered exceeds the cost of pursuing claims. Legal costs are shared across a pool of claimants and the Fund has the right to cease participation without incurring further costs. An annual progress report is provided to Pensions Audit Sub-Committee.

32 Impairment losses

During the year the Fund recognised an increase in impairment losses in respect of specific benefit over payments for which reimbursement has been requested of £4.9k. This increased the impairment to £27.7k at the year end.

Lothian Pension Fund

Actuarial Statement for 2017/18

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 (FSS), dated March 2018. In summary, the key funding principles are as follows:

- to ensure the long-term solvency of the overall 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 achieve these objectives.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2014 was as at 31 March 2017. This valuation revealed that the Fund's assets, which at 31 March 2017 were valued at £6,598 million, were sufficient to meet 98% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2017 valuation was £145 million. For the avoidance of doubt, these results are based on the assumptions that apply to the Fund's Primary investment strategy.

Each employer had contribution requirements set at the valuation with the aim of achieving full funding within a given time horizon. Contribution rates were set using one of two approaches depending on each employer's circumstances:

- Certain low risk and open employers participate in a contribution stability mechanism which limits annual changes in contribution rates. The mechanism is tested at each valuation to make sure it achieves the desired funding objectives.
- Other employers pay the contributions required to cover the cost of future service benefits and to recover the deficit/surplus identified as at 31 March 2017 over a given time period.

Individual employers' contributions for the period 1 April 2018 to 31 March 2021 were set in accordance with the Fund's funding policy as set out in its FSS, which includes further detail on the approaches mentioned above.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the 2017 valuation report.

Lothian Pension Fund

Actuarial Statement for 2017/18

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 and inflation 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.

The key financial assumptions adopted under the Primary investment strategy for the 2017 valuation were as follows:

Financial assumptions	31 March 2017 % p.a.
Discount rate	5.0%
Pay increases*	5.0%
Price inflation/Pension increases	2.7%

The key demographic assumption was the allowance made for longevity. The life expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2016 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.25% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	21.7 years	24.3 years
Future Pensioners *	24.7 years	27.5 years

*Aged 45 as at 31 March 2017

Copies of the 2017 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2017

Asset returns under the Primary investment strategy over the period have been lower than the valuation discount rate but real bond yields at 31 March 2018 are at a similar level to 31 March 2017. Combining the impact of these may mean that the overall funding level at 31 March 2018 has fallen slightly since the last formal valuation.

The next actuarial valuation will be carried out as at 31 March 2020. 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 2018

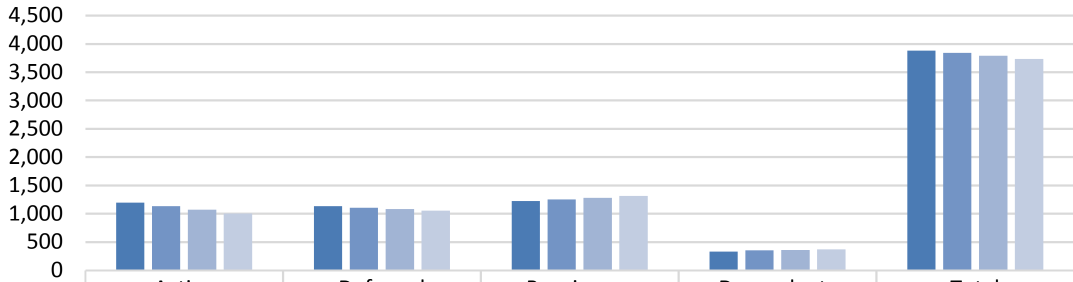
List of active employers at 31 March 2018

Scheduled Bodies	
City of Edinburgh Council (The)	Scottish Fire and Rescue Service
East Lothian Council	Scottish Police Authority
Edinburgh College	Scottish Water
Heriot-Watt University	SESTRAN
Lothian Valuation Joint Board	Visit Scotland
Midlothian Council	West Lothian College
Scotland’s Rural College (SRUC)	West Lothian Council

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

Lothian Buses Pension Fund

Lothian Buses Pension Fund membership



	Active	Deferred	Pensioners	Dependants	Total
31 March 2015	1,196	1,131	1,222	332	3,881
31 March 2016	1,130	1,104	1,253	350	3,837
31 March 2017	1,069	1,082	1,280	360	3,791
31 March 2018	1,000	1,053	1,311	370	3,734

Investment Strategy

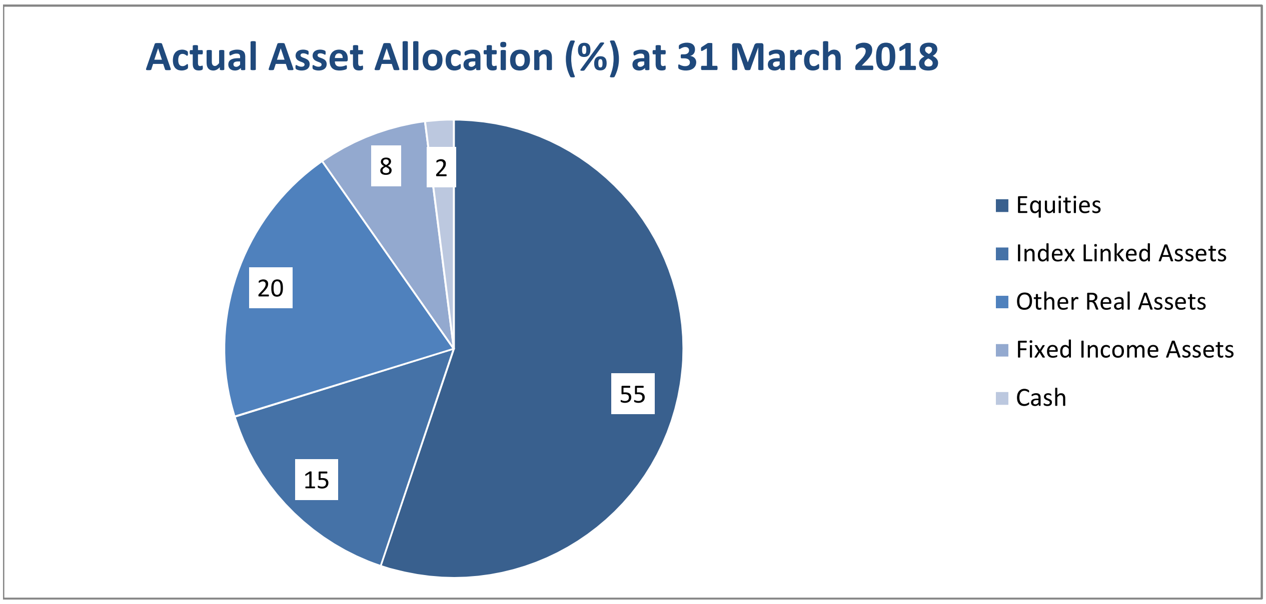
The Fund adopts a long-term investment strategy, aiming to maximise the investment return within reasonable and considered risk parameters and hence minimise the cost to the employer. A new Investment Strategy 2016-21 was agreed by Committee in March 2016. This aims to better align the risk assets held by the Fund with its maturing liability profile by reducing equity exposure to 40%, increasing the index-linked asset allocation to 20%, and increasing investments in real (18%) and fixed income (22%) assets to 40% in a phased manner over the 5-year time horizon.

A decision to merge Lothian Buses Pension Fund with the Lothian Pension Fund was made by the Pensions Committee in March 2018 subject to the satisfactory completion of a revised admission agreement and shareholders' guarantees. Progress is being made on putting in place the agreement and guarantees. The merger is expected to be enacted in the coming months, facilitated by the new employer unitisation accounting system and with the creation of a bespoke strategy for Lothian Buses in the main Lothian Pension Fund.

The implementation of the strategy progressed over the financial year 2017/18 as investment opportunities in real assets (largely infrastructure) and fixed income assets became available and as research on opportunities was completed. Implementation progress must also consider the fact that the actual asset allocation changes as markets fluctuate

The changes to the interim strategy allocations and actual allocations over the financial year 2017/18 are shown in the table below:

	Strategic Allocation 31/03/2018 %	Long term Strategy 2016 - 2021 %
Equities	55.5	40.0
Index Linked Assets	16.0	20.0
Other Real Assets	18.0	18.0
Fixed Income Assets	10.5	22.0
Cash	-	-
Total	**100.0**	**100.0**



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.

Overall, the Fund produced a return of 4.9% over the year, ahead of the benchmark return of 3.5%. Over five years, the Fund returned 10.9% per annum, ahead of benchmark by 1.4% per annum.

The Fund investment return of 4.9% was dragged down by the impact of Sterling strength on overseas investments (global equities returned 15% in US$ terms but only 2% when converted to Sterling). The return exceeded that of the strategy allocation benchmark over the last year, due mainly to the strong performance of the Baillie Gifford Global Equity portfolio. The Fund continues to meet its main objective of achieving a return consistent with that of its strategic allocation over long-term economic cycles.

The Fund continues to meet its main objective of achieving a return consistent with that of its strategic allocation over long-term economic cycles. The five-year return was 10.9% per annum and the 10-year return was 10.1% per annum (compared to benchmark returns of 9.5% and 8.6% respectively).

Annualised returns to 31 March 2018 (% per year)	1 year	5 year	10 years
Lothian Buses Pension Fund	4.9	10.9	10.1
Benchmark	3.5	9.4	8.6
Actuarial Valuation Assumptions *	3.2	4.8	5.4
Retail Price Index (RPI)	3.3	2.3	2.8
Consumer Price Index (CPI)	2.5	1.4	2.3
National Average Earnings	2.4	2.6	1.6

*estimate

The Fund continues to meet its main objective of achieving a return consistent with that of its strategic allocation over long-term economic cycles. The five-year return was 10.9% per annum and the 10-year return was 10.1% per annum (compared to benchmark returns of 9.5% and 8.6% respectively).

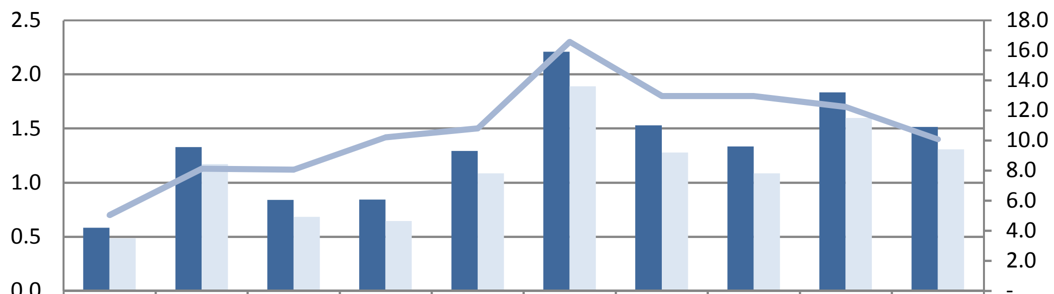
The Fund's shorter-term objective, to perform better than the strategic allocation if markets fall significantly, is yet to be tested. The Fund's return (+4.9%) over the year was ahead of the benchmark return (+3.6%) due to the strong performance of the Baillie Gifford Global Equity portfolio.

The Fund's equity investments delivered more muted, though still positive, returns (+5.1%) in comparison to last year's exceptionally strong levels. However, the return was very strong compared to the benchmark return (+2.4%). Baillie Gifford's Global Alpha portfolio in particular contributed strongly, returning 13.2% (much better than benchmark), while the much smaller Private Equity portfolio rose 5.6% (also better than benchmark). The performance of the internally-managed Global High Yield Equity portfolio tempered this somewhat, returning -2.1% over the year as high yielding, "safe haven" stocks lagged the wider market. As these stocks are lower risk than the benchmark, this is consistent with expectations.

The Fund's internally-managed index-linked assets produced a modest 1.1% gain over the year, in line with the benchmark return as expected as the portfolio is passively managed.

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, with the average excess return over the last 10 years being 1.5% pa.

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



	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fund	4.2	9.6	6.0	6.1	9.3	15.9	11.0	9.6	13.2	10.9
Benchmark	3.50	8.4	4.9	4.6	7.8	13.6	9.2	7.8	11.5	9.4
Relative (LHS)	0.7	1.1	1.1	1.4	1.5	2.3	1.8	1.8	1.7	1.4

Lothian Buses Pension Fund

Fund Account for year ended 31 March 2018

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.

2016/17 £000		Note	2017/18 £000
	Income		
7,731	Contributions from employer	**3**	7,581
2,060	Contributions from members		1,988
10	Transfers from other schemes		13
9,801			**9,582**
	Less: expenditure		
8,425	Pension payments including increases		8,755
3,277	Lump sum retirement payments		2,584
295	Lump sum death benefits		283
9	Refunds to members leaving service		4
418	Transfers to other schemes		657
98	Administrative expenses	**4b**	99
12,522			**12,382**
(2,721)	**Net withdrawals from dealing with members**		**(2,800)**
	Returns on investments		
7,641	Investment income	**5**	8,079
90,672	Change in market value of investments	**7, 11b**	17,749
(1,880)	Investment management expenses	**4c**	(2,424)
96,433	**Net returns on investments**		**23,404**
93,712	**Net increase in the Fund during the year**		**20,604**
394,431	**Net assets of the Fund at 1 April 2017**		488,143
488,143	**Net assets of the Fund at 31 March 2018**		**508,747**

Lothian Buses Pension Fund

Net Assets Statement as at 31 March 2018

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

31 March 2017 £000		Note	31 March 2018 £000
	Investment Assets		
73,313	Bonds	**6**	74,321
273,603	Equities	**6**	277,290
122,566	Pooled investment vehicles	**6, 19**	134,466
14,074	Cash Deposits	**12**	18,691
1,398	Other investment assets		1,614
484,954			**506,382**
	Investment Liabilities		
(18)	Other investment assets		(250)
(18)			**(250)**
484,936	**Net investment assets**	**6, 7, 8, 9, 11**	**506,132**
	Current assets		
385	The City of Edinburgh Council	**18**	299
2,440	Cash balances	**12, 18**	1,809
744	Debtors	**15**	842
3,569			**2,950**
	Current liabilities		
(362)	Creditors	**16**	(335)
(362)			**(335)**
3,207	**Net current assets**		**2,615**
488,143	**Net assets of the Fund at 31 March 2018**	**11**	**508,747**

The unaudited accounts were issued on 27 June 2018 and the audited accounts were authorised for issue on 26 September 2018.

JOHN BURNS FCMA CGMA
Chief Finance Officer, Lothian Pension Fund
26 September 2018

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 114.

2 Events after the Reporting Date

There have been no events since 31 March 2018, and up to the date when these accounts were authorised, that require any adjustments to these accounts.

At its meeting on 26 March 2018, the Pensions Committee approved the merger of the assets and liabilities of the Lothian Buses Pension Fund into the Lothian Pension Fund at the earliest suitable date (to be determined by the Executive Director of Resources), subject to the satisfactory completion of a revised admission agreement and shareholder guarantee.

3 Contributions from employer

By category	2016/17 £000	2017/18 £000
Normal (ongoing contributions)	7,516	7,581
Deficit contribution	-	-
Strain costs and augmentation contributions	215	-
	7,731	7,581

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

The employer contribution rate was 24.1% for 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.

4a Total management expenses

In accordance with CIPFA, the analysis below looks at the combined administration and investment management expenses in notes 4a and b and splits out the costs to include a third category covering oversight and governance expenditure. Administration costs such as Actuarial fees and Investment Management expenses such as investment consultancy would instead be shown in the Oversight and governance costs category.

	2016/17 £000	2017/18 £000
Administrative costs	78	78
Investment management expenses*	1,814	2,323
Oversight and governance costs	86	122
	1,978	2,523

* as per note 4c, includes £325k (2016/17 £3325k) in costs above CIPFA guidance

Notes to the Financial Statements

4b Administrative expenses

	2016/17 £000	2017/18 £000
Employee Costs	55	55
The City of Edinburgh Council - other support costs	6	-
System costs	13	14
Actuarial fees	9	11
Internal and External audit fees	2	3
Legal fees	-	-
Printing and postage	4	5
Depreciation	3	3
Office costs	5	5
Sundry costs less sundry income	1	3
	98	99

LPFE Ltd, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer 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.

4c Investment management expenses

	2016/17 £000	2017/18 £000
External management fees -		
invoiced	616	661
deducted from capital (direct investment)	694	1,135
deducted from capital (indirect investment)	325	338
Securities lending fees	20	18
Transaction costs	33	59
Employee costs	82	96
Custody fees	33	28
Engagement and voting fees	6	7
Performance measurement fees	19	23
Consultancy fees	5	3
System costs	18	23
Legal fees	9	10
The City of Edinburgh Council - other support costs	8	-
Depreciation	2	1
Office costs	6	6
Sundry costs less sundry income	4	16
	1,880	2,424

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 7 - Reconciliation of movements in investments and derivatives).

The external investment management fees above include £0.5m in respect of performance-related fees (2016/17 £0.3m).

Notes to the Financial Statements

4c 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 25. This further disclosure highlights an extra £338k in costs (2016/17 £325k)

5 Investment income

	2016/17 £000	2017/18 £000
Income from bonds	186	261
Dividends from equities	7,026	6,996
Income from pooled investment vehicles	452	1,077
Interest on cash deposits	18	33
Stock lending and sundries	103	92
	7,785	8,459
Irrecoverable withholding tax	(144)	(380)
	7,641	8,079

Included within the dividend from equities income for the year is cross border withholding tax yet to be received. These reclaims have a high certainty of success and are completed and managed by the Fund's custodian Northern Trust. For the period of 2017/18 £245k of the stated income relates to tax yet to be received. At the 31st March 2018 £525k (including prior periods) of investment income receivable related to cross border withholding tax. The Fund monitors these claims to ensure its optimum tax efficiency and provides an annual progress report to the Pensions Audit Sub-Committee.

6 Analysis of investments

Investment Assets	Region	31 March 2017 £000	31 March 2018 £000
Bonds			
Public sector index linked gilts quoted	UK	73,313	74,321
		73,313	74,321
Equities			
Quoted	UK	33,935	28,853
Quoted	Overseas	239,668	248,437
		273,603	277,290
Pooled investment vehicles			
Managed funds - property	UK	38,146	41,487
Managed funds - other bonds	UK	30,100	30,490
Timber funds - unquoted	Overseas	8,361	6,838
Infrastructure - unquoted	UK	26,636	28,850
Infrastructure - unquoted	Overseas	12,607	16,774
Private debt funds - unquoted	UK	2,266	2,881
Private debt funds - unquoted	Overseas	4,450	7,146
		122,566	134,466

Notes to the Financial Statements

7 Reconciliation of movement in investments and derivatives

	Market value at 31 March 2017 £000	Purchases at cost & derivative payments £000	Sales & derivative receipts £000	Change in market value £000	Market value at 31 March 2018 £000
Bonds	73,313	4,043	(3,613)	578	74,321
Equities	273,603	28,779	(32,933)	7,841	277,290
Pooled investment vehicles	122,566	5,736	(3,764)	9,928	134,466
Derivatives - fwd foreign exchange	-	15	(11)	(4)	-
	469,482	38,573	(40,321)	18,343	486,077
Other financial assets / (liabilities)					
Cash deposits*	14,074			(605)	18,691
Broker balances*	(18)			11	20
Investment income due*	1,398				1,344
	15,454			(594)	20,055
Net financial assets	484,936			17,749	506,132

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 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 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)
Investment income due*	1,081			-	1,398
	12,819			153	15,454
Net financial assets	390,788			90,672	484,936

** As per CIPFA disclosures the change in market value intentionally does not balance opening/closing market values*

Notes to the Financial Statements

8 Investment managers and mandates

Manager	Mandate	Market value at 31 March 2017 £000	% of total 31 March 2017 %	Market value at 31 March 2018 £000	% of total 31 March 2018 %
Baillie Gifford	Global equities	124,570	25.7	141,217	27.9
In-house	Global high dividend	142,297	29.3	131,248	25.9
In-house	Private equity quoted	6,287	1.3	5,605	1.1
Total global equities		273,154	56.3	278,070	54.9
In-house	Index linked gilts	73,793	15.2	74,630	14.7
Total index linked assets		73,793	15.2	74,630	14.7
Baillie Gifford	Corporate bonds	30,100	6.2	30,490	6.0
In-house	Secured loans unquoted	6,716	1.4	10,027	2.0
Total fixed income assets		36,816	7.6	40,517	8.0
Standard Life	Property	38,146	7.9	41,487	8.2
In-house	Infrastructure unquoted	39,243	8.1	45,625	9.0
In-house	Infrastructure quoted	3,661	0.8	2,950	0.6
In-house	Timber unquoted	8,361	1.7	6,838	1.4
Total other real assets		89,411	18.5	96,900	18.5
In-house	Cash	11,762	2.4	16,015	3.2
Total cash and sundries		11,762	2.4	16,015	3.2
Net financial assets		484,936	100.0	506,132	100.0

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

	Market value at 31 March 2017 £000	% of net assets 31 March 2017	Market value at 31 March 2018 £000	% of net assets 31 March 2018
Standard Life Property Fund	38,146	7.9	41,487	8.2
Baillie Gifford Inv Grade Bond Fund	30,100	6.2	30,490	6.0

10 Securities lending

During the year Lothian Buses Pension Fund participated in a securities lending arrangement with the Northern Trust Company. As at 31 March 2018, £16.8m (2017 £17.4m) of securities were released to third parties. Collateral valued at 106.19% (2017 105.24%) of the market value of the securities on loan was held at that date.

Notes to the Financial Statements

11 Financial Instruments

11a 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 2017			31 March 2018		
Financial assets	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
Investment assets						
Bonds	73,313	-	-	74,321	-	-
Equities	273,603	-	-	277,290	-	-
Pooled investments	122,566	-	-	134,466	-	-
Cash	-	14,074	-	-	18,691	-
Other balances	-	1,398	-	-	1,614	-
	469,482	15,472	-	486,077	20,305	-
Other assets						
City of Edinburgh Council	-	385	-	-	299	-
Cash	-	2,440	-	-	1,809	-
Debtors	-	744	-	-	842	-
	-	3,569	-	-	2,950	-
Assets total	469,482	19,041	-	486,077	23,255	-
Financial liabilities						
Investment liabilities						
Other investment balances	-	-	(18)	-	-	(250)
	-	-	(18)	-	-	(250)
Other liabilities						
Creditors	-	-	(362)	-	-	(335)
Liabilities total	-	-	(380)	-	-	(585)
Total net assets	469,482	19,041	(380)	486,077	23,255	(585)

Total net financial assets	488,143	508,747

Notes to the Financial Statements

11b Net gains and losses on financial instruments

	2016/17 £000	2017/18 £000
Designated as fair value through fund account	90,519	18,343
Loans and receivables	153	(594)
Financial liabilities at amortised cost	-	-
Total	90,672	17,749

11c 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

11c Valuation of financial instruments carried at fair value (cont)

	31 March 2018 Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Investment assets				
Designated as fair value through fund account	349,267	74,321	62,489	486,077
Loans and receivables	20,305	-	-	20,305
Total investments assets	369,572	74,321	62,489	506,382
Investment liabilities				
Designated as fair value through fund account	(250)	-	-	(250)
Total investment liabilities	(250)	-	-	(250)
Net Investment assets	369,322	74,321	62,489	506,132

	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

11d Reconciliation of fair value measurements within level 3

Pooled investments	Market value at 31 March 2017	Level 3 transfers in	Level 3 transfers out	Purchases at cost & derivative payments	Sales & derivative receipts	Unrealised gains / (losses)	Realised gains / (losses)	Market value at 31 March 2018
Infrastructure	39,243	-	-	7,026	(6,215)	4,050	1,520	45,624
Timber	8,361	-	-	-	(1,124)	(641)	242	6,838
Secured loans	6,716	-	-	4,018	(1,153)	429	17	10,027
	54,320	-	-	11,044	(8,492)	3,838	1,779	62,489

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

12 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
- 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

12 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	10.0%
Corporate Bonds	5.6%
Index-Linked Gilts	11.0%
Infrastructure	12.0%
Property	13.0%
Cash	1.0%

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 2018 £000	% of fund %	Potential Change +/- %	Value on increase £000	Value on decrease £000
Equities - Developed Markets	272,465	55.1	20.5	328,320	216,610
Private Equity	5,605	1.1	30.0	7,287	3,924
Timber and Gold	6,838	1.4	18.0	8,069	5,607
Secured Loan	10,027	2.0	10.0	11,030	9,024
Corporate Bonds	30,490	6.0	5.6	32,185	28,795
Index-Linked Gilts	74,630	14.7	11.0	82,802	66,458
Infrastructure	48,574	9.6	12.0	54,403	42,745
Property	41,487	8.2	13.0	46,880	36,094
Cash and forward foreign exchange	16,016	3.2	1.0	16,174	15,858
Total [1]	506,132	100.0	16.0	587,150	425,114
Total [2]			12.6	569,766	442,498
Total [3]			12.6	570,062	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

12 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 2018, cash deposits represented £17.8m, 3.5% of total net assets. This was held with the following institutions:

	Moody's Credit Rating at 31 March 2018	Balances at 31 March 2017 £000	Balances at 31 March 2018 £000
Held for investment purposes			
Northern Trust Global Investment Limited - liquidity funds	Aaa-mf	3,270	2,496
Northern Trust Company - cash deposits	A2	9,882	15,269
The City of Edinburgh Council - treasury management	See below	922	926
Total investment cash		14,074	18,691
Held for other purposes			
The City of Edinburgh Council - treasury management	See below	2,440	1,809
Total cash		16,514	20,500

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

12 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

(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 2018	Balances at 31 March 2017 £000	Balances at 31 March 2018 £000
Money market funds			
Deutsche Bank AG, London	Aaa-mf	18	12
Standard Life Investments Sterling Liquidity Fund	Aaa-mf	-	406
Bank call accounts			
Bank of Scotland	Aa3	336	270
Royal Bank of Scotland	A3	5	10
Santander UK	Aa3	1	7
Barclays Bank	A1	-	-
Svenska Handelsbanken	Aa2	1	13
HSBC Bank PLC	Aa3	1	1
UK Pseudo-Sovereign risk instruments			
Other Local Authorities [1]	Aa1	3,001	2,016
		3,363	2,735

[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 2018 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 2018, the Fund had no over-the-counter foreign currency derivatives.

Notes to the Financial Statements

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

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.

The majority (estimated to be approximately 88% (2017 89%)) of the Fund's investments could be converted to cash within three months in a normal trading environment.

13 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.

14 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 £463m (2017 £488m). 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 2017 % p.a.	31 March 2018 % p.a.
Inflation/pensions increase rate	2.4	2.4
Salary increase rate	4.4	4.1
Discount rate	2.6	2.7

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2016 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 2017		31 March 2018	
	Males	Females	Males	Females
Current pensioners	20.4 years	22.9 years	19.7 years	22.3 years
Future pensioners (assumed to be currently 45)	23.5 years	25.9 years	21.9 years	24.8 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

15 Debtors

	2016/17 £000	2017/18 £000
Contributions due - employer	581	664
Contributions due - members	153	173
Sundry debtors	10	5
	744	842

Analysis of debtors

	31 March 2017 £000	31 March 2018 £000
Administering Authority	1	1
Lothian Buses Limited	733	837
Other entities and individuals	10	4
	744	842

16 Creditors

	31 March 2017 £000	31 March 2018 £000
Benefits payable	201	149
Miscellaneous creditors and accrued expenses	161	186
	362	335

Analysis of creditors

	31 March 2017 £000	31 March 2018 £000
Central Government Bodies	-	11
Other entities and individuals	362	324
	362	335

17 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	2016/17 £000	2017/18 £000
Standard Life	8	7
Prudential	70	76
	78	83

Total value at year end	31 March 2017 £000	31 March 2018 £000
Standard Life	155	145
Prudential	294	375
	449	520

Notes to the Financial Statements

18 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

LPFE Ltd, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer 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 2017 £000	31 March 2018 £000
Year end balance of holding account	385	299
	385	299

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 2018, the fund had an average investment balance of £2.8m (2017 £3.0m). Interest earned was £10.5k (2017 £12.1k).

Year end balance on treasury management account	31 March 2017 £000	31 March 2018 £000
Held for investment purposes	922	926
Held for other purposes	2,440	1,809
	3,362	2,735

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 75) of the notes to the Financial Statements.

Governance

As at 31 March 2018, all members of the Pensions Committee, with the exception of 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 reciept 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

18 Related party transactions (cont)

With effect from 1 May 2015, all the employees listed below, with the exception of the City of Edinburgh Council members of staff, 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 2017 £000	Accrued CETV as at 31 March 2018 £000
Stephen Moir*	Executive Director of Resources, City of Edinburgh Council	-	22
Hugh Dunn*	Head of Finance, City of Edinburgh Council	1,251	949
Katy Miller*	Head of Human Resources, City of Edinburgh Council **	29	51
Clare Scott*	Chief Executive Officer, Lothian Pension Fund	221	270
Bruce Miller	Chief Investment Officer, Lothian Pension Fund	267	334
Struan Fairbairn	Chief Risk Officer, Lothian Pension Fund	46	64
John Burns	Chief Finance Officer, Lothian Pension Fund	538	624
Esmond Hamilton	Financial Controller, Lothian Pension Fund	200	238

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

** Appears due to being a Director in LPFE Ltd

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

	31 March 2017 £000	31 March 2018 £000
Short-term employee benefits	380	415
Post-employment benefits - employer pension contributions	78	85

Key management personnel employed by LPFE, had accrued pensions totalling £97,456 (1 April 2017: £81,825) and lump sums totalling £110,889 (1 April 2017: £100,185) 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.

19 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 2017 £000	31 March 2018 £000
Outstanding investment commitments	12,462	11,051
	12,462	11,051

Notes to the Financial Statements

20 Contingent assets and liabilities

At 31 March 2018 the Fund does not have any exposure to any contingent assets/liabilities.

21 Impairment losses

No impairment losses have been identified during the year.

Lothian Buses Pension Fund

Actuarial Statement for 2017/18

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 (FSS), dated March 2018. 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 60 of the Local Government Pension Scheme (Scotland) Regulations 2014 was as at 31 March 2017. This valuation revealed that the Fund's assets, which at 31 March 2017 were valued at £488 million, were sufficient to meet 121% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting surplus at the 2017 valuation was £84 million.

On the more prudent gilts basis, the Fund's assets at 31 March 2017 were sufficient to meet 89% of the liabilities accrued to that date. The resulting deficit at the 2017 valuation, on the gilts basis, was £59 million.

The required contributions for the period 1 April 2018 to 31 March 2021 were set at the 2017 valuation 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 2017 valuation report.

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 and inflation 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 2017/18

The key financial assumptions adopted for the 2017 valuation were as follows:

Financial assumptions	31 March 2017 % p.a.
Discount rate	3.2 %
Salary increase assumption	4.1%
Benefit increase assumption (CPI)	2.4%

The key demographic assumption was the allowance made for longevity. The life expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2016 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.25% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	19.7 years	22.3 years
Future Pensioners *	21.9 years	24.8 years

*Aged 45 as at 31 March 2017

Copies of the 2017 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2017

Asset returns over the period have been lower than the valuation discount rate and real bond yields at 31 March 2018 are at a similar level to 31 March 2017. Combining the impact of these may mean that the funding level at 31 March 2018 has fallen slightly since the last formal valuation.

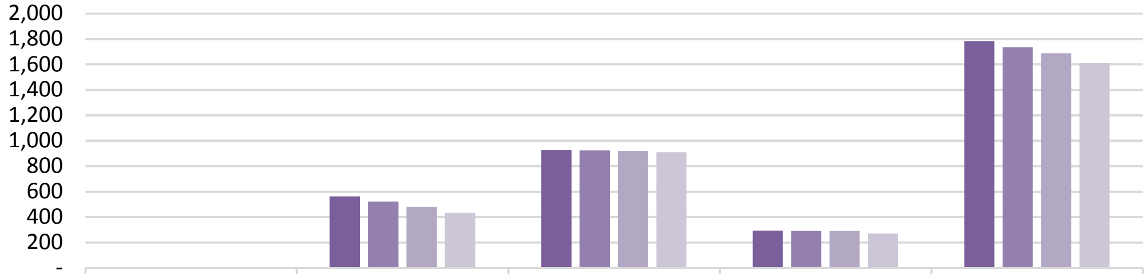
The next actuarial valuation will be carried out as at 31 March 2020. The Funding Strategy Statement will also be reviewed at that time.

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

27 April 2018

Scottish Homes Pension Fund

Scottish Homes Pension Fund membership



	Active	Deferred	Pensioners	Dependants	Total
31 March 2015	-	562	928	293	1,783
31 March 2016	-	522	922	291	1,735
31 March 2017	-	478	919	289	1,686
31 March 2018	-	433	908	269	1,610

Investment strategy

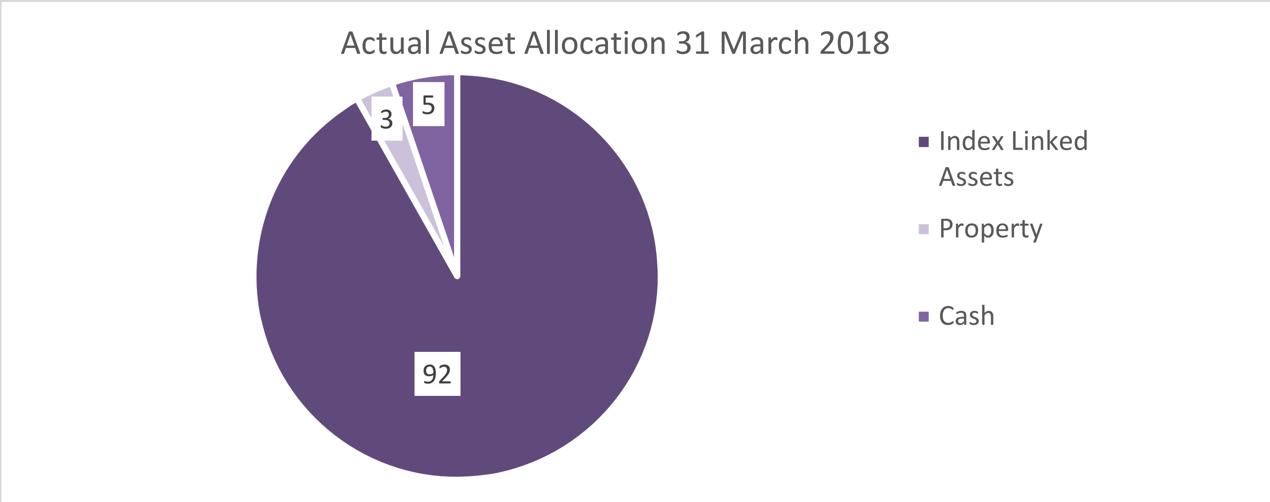
The funding level of the Scottish Homes Pension Fund at 31 March 2017 was 104.7%, an increase from 88.8% at the 2014 valuation.

The Fund's actuary monitors the intra-valuation fluctuations in the funding level using a system that reflects movements in interest rates and asset markets. Over the year to 2018, these fluctuations have been small as the mix of assets owned by the Fund are mostly index-linked gilts, which move proportionately with liability values.

	Strategic Allocation 31 March 2017 %	Strategic Allocation 31 March 2018 %
Equities	17.5	-
Bonds	77.5	100.0
Property	5.0	-
Cash	-	-
Total	**100.0**	**100.0**

The initial changes to the strategy allocation were triggered by movements in interest rates and asset prices that affected the actuary's funding level estimate. However, the final change increasing Bonds to 100% was prompted by the results of the triennial Actuarial Valuation at 31 March 2017, which indicated that the funding level was higher than previously estimated. This was partly because the actuary made some revisions to the financial and demographic assumptions to reflect actual experience over the intervening three years.

The Fund's Equity and Bond portfolios were managed by the internal team over the last year. The Property portfolio was managed by Schroder in a pooled fund of UK commercial real estate. Over the year, the Equity allocation was invested in a portfolio of shares of global companies that generate robust and growing dividends. The Bond allocation was invested in a portfolio of UK index-linked gilts designed to match the liability payments of the Fund as closely as possible.



Investment performance

The objectives of the Fund over the past year, were:

• 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 benchmark comprises global equity, index-linked gilt and property indices. Over 2017/18, these returned +2.4%, -0.2% and +11.3% respectively.

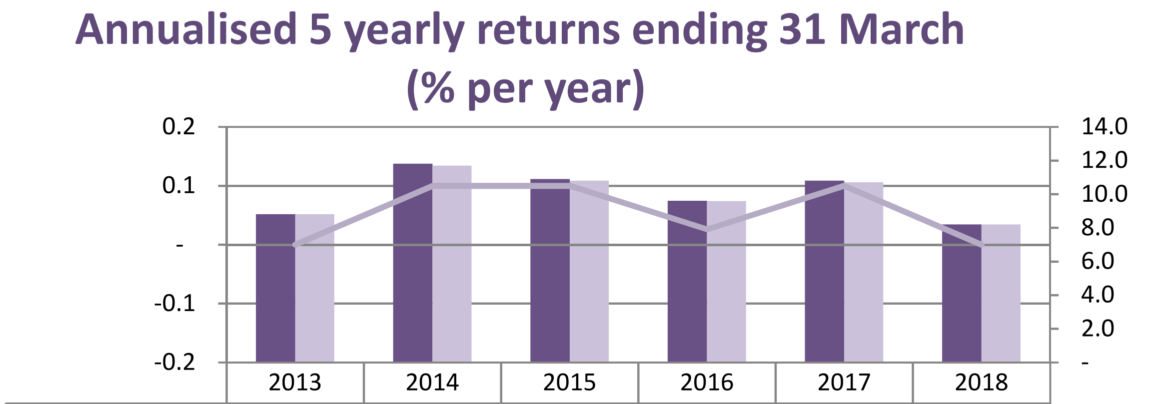
The Fund's annualised performance over the year and longer-term periods is shown in the table below.

Annualised returns to 31 March 2018 (% per year)	1 year	5 years	10 years
Scottish Homes Pension Fund	0.3	8.2	8.5
Benchmark	0.7	8.2	8.5
Actuarial Valuation Assumptions *	1.7	3.2	3.8
Retail Price Index (RPI)	3.3	2.3	2.8
Consumer Price Index (CPI)	2.5	1.4	2.3
National Average Earnings	2.4	2.6	1.6

* estimated

The Fund has performed in line with its strategic allocation (benchmark) over the long run. The difference between the Fund return and the benchmark over the last year reflects the fact that the equity allocation was invested in a portfolio of low risk shares that lagged the higher risk benchmark. This equity portfolio was funded during 2016/17 to generate higher income with which to pay pensions, following analysis of the Fund's cash flow requirements. Over 2017/18, it generated a significantly higher income yield (3.8%) than the benchmark (2.5%).
Now that the Fund has achieved full funding faster than expected and the Fund is fully invested in index-linked gilts to minimise funding level risk, it is appropriate to change the investment objectives.

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



	2013	2014	2015	2016	2017	2018
Fund	8.8	11.8	10.9	9.6	10.8	8.2
Benchmark	8.8	11.7	10.8	9.6	10.7	8.2
Relative (LHS)	-	0.1	0.1	0.0	0.1	-

Scottish Homes Pension Fund

Fund Account for year ended 31 March 2018

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 investment dealings and the Scottish Government's annual contributions, as well as the cost of providing benefits and administration of the Fund.

2016/17 £000		Note	2017/18 £000
	Income		
675	Contributions from the Scottish Government	***3***	675
-	Transfers from other schemes		-
675			**675**
	Less: expenditure		
6,789	Pension payments including increases		6,666
563	Lump sum retirement payments		767
-	Lump sum death benefits		4
120	Transfers to other schemes	***4***	47
68	Administrative expenses	***5b***	69
7,540			**7,553**
(6,865)	**Net withdrawals from dealing with members**		**(6,878)**
	Returns on investments		
877	Investment income	***6***	2,474
26,569	Change in market value of investments	***7, 10b***	(1,615)
(212)	Investment management expenses	***5c***	(165)
27,234	**Net returns on investments**		**694**
20,369	**Net increase/(decrease) in the Fund during the year**		**(6,184)**
150,275	**Net assets of the Fund at 1 April 2017**		170,644
170,644	**Net assets of the Fund at 31 March 2018**	***10***	**164,460**

Net Assets Statement as at 31 March 2018

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

31 March 2017 £000		Note	31 March 2018 £000
	Investment Assets		
127,970	Bonds		148,064
4,450	Equities - UK		-
23,771	- Overseas		-
7,998	Pooled investment vehicles - UK property		-
3,602	Cash Deposits		9,094
459	Other investment assets		4,904
168,250			**162,062**
	Investment Liabilities		
-	Other investment liabilities		-
-			-
168,250	**Net investment assets**	***8***	**162,062**
	Current assets		
146	The City of Edinburgh Council	***16***	194
2,232	Cash balances	***11, 16***	2,240
31	Debtors	***14***	12
2,409			**2,446**
	Current liabilities		
(15)	Creditors	***15***	(48)
(15)			**(48)**
2,394	**Net current assets**		**2,398**
170,644	**Net assets of the Fund at 31 March 2018**	***10***	**164,460**

The unaudited accounts were issued on 27 June 2018 and the audited accounts were authorised for issue on 26 September 2018.

JOHN BURNS FCMA CGMA
Chief Finance Officer, Lothian Pension Fund
26 September 2018

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 114.

2 Events after the Reporting Date

There have been no events since 31 March 2018, 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

	2016/17 £000	2017/18 £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. After 31 March 2017 actuarial valuation Scottish Government will not provide deficit funding for the period April 2018 to March 2021 but have agreed to pay £70,000 every year towards the administration of the Fund.

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

	2016/17 £000	2017/18 £000
Group transfers	-	-
Individual transfers	120	47
	120	47

5a Total Management expenses

	2016/17 £000	2017/18 £000
Administrative costs	38	35
Investment management expenses	149	107
Oversight and governance costs	93	92
	280	234

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

	2016/17 £000	2017/18 £000
Employee costs	26	24
The City of Edinburgh Council - other support costs	3	-
System costs	7	8
Actuarial fees	24	30
External audit fees	1	1
Printing and postage	2	2
Depreciation	1	1
Office costs	3	2
Sundry costs less sundry income	1	1
	68	69

LPFE Ltd, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer the three pension Funds. The Division receives an allocation of the overheads of the Council. In turn the Division 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

	2016/17 £000	2017/18 £000
External management fees - invoiced	50	-
External management fees - deducted from capital (direct)	55	54
External management fees - deducted from capital (indirect)	-	-
Transaction costs	40	30
Employee costs	29	31
Custody fees	14	7
Engagement and voting fees	2	2
Performance measurement fees	5	10
Consultancy fees	2	16
System costs	6	7
Legal fees	3	1
The City of Edinburgh Council - other support costs	3	-
Office costs	2	2
Sundry costs less sundry income	1	5
	212	165

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 7 - Reconciliation of movements in investments).

The Fund has not incurred any performance-related investment management fees in 2017/18 or 2016/17.

Notes to the Financial Statements

6 Investment income

	2016/17 £000	2017/18 £000
Income from fixed interest securities	536	1,449
Dividends from equities	62	799
Income from pooled investments - property	265	270
Interest on cash deposits and sundries	16	29
	879	2,547
Irrecoverable withholding tax	(2)	(73)
	877	2,474

7 Reconciliation of movement in investments

	Market value at 31 March 2017 £000	Purchases at cost £000	Sales & proceeds £000	Change in market value £000	Market value at 31 March 2018 £000
Bonds	127,970	33,345	(11,838)	(1,413)	148,064
Equities	28,221	932	(28,451)	(702)	-
Pooled investment vehicles	7,998	-	(8,621)	623	-
	164,189	34,277	(48,910)	(1,492)	148,064
Other financial assets / (liabilities)					
Cash deposits*	3,602			(123)	9,094
Investment income due/amounts payable*	459			-	4,904
	4,061			(123)	13,998
Net financial assets	168,250			(1,615)	162,062

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 2016 £000	Purchases at cost £000	Sales & proceeds £000	Change in market value £000	Market value at 31 March 2017 £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
Investment income due/amounts payable*	177			-	459
	188			80	4,061
Net financial assets	148,598			26,569	168,250

** As per CIPFA disclosures the change in market value intentionally does not balance opening/closing market values*

Notes to the Financial Statements

8 Investment managers and mandates

Manager	Mandate	Market value at 31 March 2017 £000	% of total 31 March 2017 %	Market value at 31 March 2018 £000	% of total 31 March 2018 %
In-house	High Div Equity	29,037	17.3	87	0.1
Total global equities		29,037	17.3	87	0.1
In-house	UK Index linked gilts	128,477	76.4	148,858	91.9
Total bonds		128,477	76.4	148,858	91.9
Schroders	Property	7,998	4.8	4,363	2.7
Total property		7,998	4.8	4,363	2.7
In-house	Cash	2,738	1.6	8,754	5.4
Total cash		2,738	1.6	8,754	5.4
Net financial assets		168,250	100.0	162,062	100.0

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

	Market value at 31 March 2017 £000	% of total 31 March 2017 %	Market value at 31 March 2018 £000	% of total 31 March 2018 %
UK Gov 4.125% Index Linked 22/11/17	10,955	6.4	21,410	13.0
UK Gov 2.5% Index Linked 17/07/24	10,637	6.2	12,431	7.6
UK Gov 2.5% Index Linked 16/04/20	10,538	6.2	12,309	7.5
UK Gov 1.875% Index Linked 22/11/22	10,517	6.2	12,530	7.6
UK Gov 1.125% Index Linked 22/11/27	9,003	5.3	11,149	6.8
UK Gov 1.125% Index Linked 22/11/37	7,800	4.6	12,465	7.6
UK Gov 1.25% Index Linked 22/11/27	11,905	7.0		-

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.

Notes to the Financial Statements

10a Classification of financial instruments (cont)

Financial assets	31 March 2017 Designated as fair value through fund account £000	31 March 2017 Loans and receivables £000	31 March 2017 Financial liabilities at amortised cost £000	31 March 2018 Designated as fair value through fund account £000	31 March 2018 Loans and receivables £000	31 March 2018 Financial liabilities at amortised cost £000
Investment assets						
Bonds	127,970	-	-	148,064	-	-
Equities	28,221	-	-	-	-	-
Pooled investments	7,998	-	-	-	-	-
Cash	-	3,602	-	-	9,094	-
Other balances	-	459	-	-	4,904	-
	164,189	4,061	-	148,064	13,998	-
Other assets						
City of Edinburgh Council	-	146	-	-	194	-
Cash	-	2,232	-	-	2,240	-
Debtors	-	31	-	-	12	-
	-	2,409	-	-	2,446	-
Assets total	164,189	6,470	-	148,064	16,444	-
Financial liabilities						
Other liabilities						
Creditors	-	-	(15)	-	-	(48)
Liabilities total	-	-	(15)	-	-	(48)
Total net assets	164,189	6,470	(15)	148,064	16,444	(48)

	31 March 2017	31 March 2018
Total net financial instruments	170,644	164,460

10b Net gains and losses on financial instruments

	2016/17 £000	2017/18 £000
Designated as fair value through fund account	26,489	(1,492)
Loans and receivables	80	(123)
Financial liabilities at amortised cost	-	-
Total	26,569	(1,615)

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 2018			
	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
Investment assets				
Designated as fair value through fund account	-	148,064	-	148,064
Loans and receivables	13,998	-	-	13,998
Total investment assets	13,998	148,064	-	162,062
Investment liabilities				
Designated as fair value through fund account	-	-	-	-
Total investment liabilities	-	-	-	-
Net investment assets	13,998	148,064	-	162,062

Notes to the Financial Statements

10c Valuation of financial instruments carried at fair value (cont)

	31 March 2017			
	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
Investment assets				
Designated as fair value through fund account	36,219	127,970	-	164,189
Loans and receivables	4,061	-	-	4,061
Total financial assets	40,280	127,970	-	168,250
Investment liabilities				
Designated as fair value through fund account	-	-	-	-
Total financial liabilities	-	-	-	-
Net investment assets	40,280	127,970	-	168,250

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 -)
Index-Linked Gilts	11.0%
Cash	1.0%

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 2018 £000	% of fund %	Potential Change +/- %	Value on increase £000	Value on decrease £000
Index-Linked Gilts	148,856	91.9	11.0	165,157	132,555
Cash	13,204	8.1	1.0	13,334	13,074
Total [1]	162,060	100.0	10.1	178,491	145,629
Total [2]			10.1	178,387	145,733
Total [3]			9.1	176,847	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].

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.

Notes to the Financial Statements

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

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 2018, cash deposits represented £20.4m, 12.5% of total net assets. This was held with the following institutions:

	Moody's Credit Rating at 31 March 2018	Balances at 31 March 2017 £000	Balances at 31 March 2018 £000
Held for investment purposes			
Northern Trust Company - cash deposits	A2	3,602	1,077
The City of Edinburgh Council - treasury management	See below	-	8,017
		3,602	9,094
Held for other purposes			
The City of Edinburgh Council - treasury management	See below	2,232	2,240
Total cash		9,436	20,428

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 -

(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.

Notes to the Financial Statements

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

	Moody's Credit Rating at 31 March 2018	Balances at 31 March 2017 £000	Balances at 31 March 2018 £000
Money market funds			
Deutsche Bank AG, London	Aaa-mf	12	44
Standard Life Investments	Aaa-mf	-	1,520
Bank call accounts			
Bank of Scotland	A1	223	1,013
Royal Bank of Scotland	A3	3	37
Santander UK	Aa3	1	27
Barclays Bank	A1	-	1
HSBC Bank		-	4
Svenska Handelsbanken	Aa2	-	50
UK Pseudo-Sovereign risk instruments			
Other Local Authorities [1]	Aa1	1,993	7,561
UK Government Treasury Bills	Aa1	-	-
		2,232	10,257

[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 2018 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.

Notes to the Financial Statements

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 £134m (2017 £145m). 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.

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 2017 % p.a.	31 March 2018 % p.a.
Inflation/pensions increase rate	2.4%	2.4%
Discount rate	2.6%	2.7%

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2016 model, assuming that the current rate of improvements has reached a peak and will converge to a long term rate of 1.75% p.a.. Based on these assumptions, the average future life expectancies, in years, at age 65 are summarised below:

	31 March 2017		31 March 2018	
	Males	Females	Males	Females
Current pensioners	24.5 years	25.4 years	22.4 years	24.8 years
Future pensioners (assumed to be currently 45)	26.8 years	28.6 years	24.8 years	27.8 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 2017 £000	31 March 2018 £000
Sundry debtors	31	12
	31	12

Analysis of debtors

	31 March 2017 £000	31 March 2018 £000
Administering Authority	1	1
Other entities and individuals	30	11
	31	12

Notes to the Financial Statements

15 Creditors

	31 March 2017 £000	31 March 2018 £000
Benefits payable	-	3
Miscellaneous creditors and accrued expenses	15	45
	15	48

Analysis of creditors	31 March 2017 £000	31 March 2018 £000
Other entities and individuals	15	48
	15	48

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.

LPFE Ltd which is a wholly owned subsidiary 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 2017 £000	31 March 2018 £000
Year end balance of holding account	146	194
	146	194

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 2018, the fund had an average investment balance of £6.3m (2017 £2.1m). Interest earned was £29k (2017 £8k).

Year end balance on treasury management account	31 March 2017 £000	31 March 2018 £000
Held for investment purposes	-	8,011
Held for other purposes	2,232	2,240
	2,232	10,251

Scheme Guarantor

The scheme guarantor (by definition) is a related party to the scheme. The Scottish Government's contributions to the Fund can be found in note 3 (page 99) of the notes to the Financial Statements.

Governance

As at 31 March 2018, all members of the Pensions Committee, with the exception of 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.

Notes to the Financial Statements

16 Related party transactions (cont)

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 City of Edinburgh Council members of staff, 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 2017 £000	Accrued CETV as at 31 March 2018 £000
Stephen Moir*	Executive Director of Resources, City of Edinburgh Council	-	22
Hugh Dunn*	Head of Finance, City of Edinburgh Council	1,251	949
Katy Miller*	Head of Human Resources, City of Edinburgh Council **	29	51
Clare Scott*	Chief Executive, Lothian Pension Fund	221	270
Bruce Miller	Chief Investment Officer, Lothian Pension Fund	267	334
Struan Fairbairn	Chief Risk Officer, Lothian Pension Fund	46	64
John Burns	Chief Finance Officer, Lothian Pension Fund	538	624
Esmond Hamilton	Financial Controller, Lothian Pension Fund	200	238

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

** Appears due to being a Director in LPFE Ltd

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

	31 March 2017 £000	31 March 2018 £000
Short-term employee benefits	380	415
Post-employment benefits - employer pension contributions	78	85

Key management personnel employed by LPFE, had accrued pensions totalling £97,456 (1 April 2017: £81,825) and lump sums totalling £110,889 (1 April 2017: £100,185) 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 2017/18

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 (FSS), dated March 2018, 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.

As the Fund was well ahead of its Target Funding Level at the 2017 valuation, it took the decision to derisk its investment strategy and now invests 100% of its assets in index-linked gilts.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2014 was as at 31 March 2017. This valuation revealed that the Fund's assets, which at 31 March 2017 were valued at £170.6 million, were sufficient to meet 104.7% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting surplus at the 2017 valuation was £7.7 million.

The Guarantor's contributions for the period 1 April 2018 to 31 March 2021 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 2017 valuation report.

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 2017 valuation were as follows:

Financial assumptions	31 March 2017
Benefit increase assumption (CPI)	Bank of England nominal yield curve
Discount rate	Bank of England implied (RPI) curve less 1.0% p.a.

Scottish Homes Pension Fund

Actuarial Statement for 2017/18

The key demographic assumption was the allowance made for longevity. The life expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2016 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.75% 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

*Aged 45 as at 31 March 2017

Copies of the 2017 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2017

Asset returns over the period have been slightly higher than the valuation discount rate and real bond yields at 31 March 2018 are at a similar level to 31 March 2017. Combining the impact of these leads to a broadly similar overall funding position at 31 March 2018 compared to the last formal valuation.

The next actuarial valuation will be carried out as at 31 March 2020. 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

27 April 2018

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 2017/18 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 2017/18 financial year and report on the net assets available to pay pension benefits as at 31 March 2018. 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.

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 management of the Funds. LPFI Limited's purpose is to provide FCA regulated services to the Funds and other Local Government Pension Scheme funds. 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 Lothian Pension Fund is responsible for administering the three Funds. The costs include charges from LPFE Limited and LPFI Limited for services rendered. The Fund receives an allocation of the overheads of the Council, this is based on the amount of central services consumed. In turn, these costs are allocated 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.

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 Standard Interpretations Committee (SIC) 15, subsequently endorsed by the International Accounting Standards Board (IASB), 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
Freehold and leasehold properties	Level 3	Valued at fair value at the year-end using the investment method of valuation by John Symes-Thompson FRICS of independent valuers, CBRE Ltd in accordance with RICS Valuation – Global Standards 2017	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 (2015)	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 2018.

Lothian Pension Fund Unquoted	Assessed Valuation range (+ or -)	Value at 31 March 2018 £m	Value on increase £m	Value on decrease £m
Private Equity	30%	90.4	117.5	63.3
Infrastructure	12%	727.6	814.9	640.3
Timber	18%	111.4	131.5	91.3
Private Secured Loans	10%	133.2	146.5	119.9
Property	13%	459.3	519.0	399.6
		1,403.9	1,643.6	1,163.6

Lothian Buses Pension Fund Unquoted	Assessed Valuation range (+ or -)	Value at 31 March 2018 £m	Value on increase £m	Value on decrease £m
Infrastructure	12%	45.6	51.1	40.1
Timber	18%	6.8	8.0	5.6
Private Secured Loans	10%	10.0	11.0	9.0
		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

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:

The Code requires implementation from 1 April 2018 and there is therefore no impact on the 2017/18 financial statements.

- IFRS 9 Financial Instruments
- IFRS 15, Revenue from Contracts with Customers including amendments to IFRS 15 Clarifications to IFRS 15 Revenue Contracts with Customers
- amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses
- amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative

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 2018 was £1,062.5m (2016 £1,014.2m).

For the Lothian Buses Pension Fund, the value of unquoted private equity, infrastructure and timber investments at 31 March 2018 was £62.5m (2017 £54.3m).

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 2018 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 2018	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in the real discount rate	10	814
1 year increase in member life expectancy	4	334
0.5% increase in salary increase rate	2	167
0.5% increase in pensions increase rate	7	582

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 2018	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in the real discount rate	10	48
1 year increase in member life expectancy	4	20
0.5% increase in salary increase rate	2	10
0.5% increase in pensions increase rate	7	48

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 2018	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in the real discount rate	5	7
1 year increase in member life expectancy	4	6
0.5% increase in pensions increase rate	5	7

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 Annual 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 Audited Annual Accounts for signature.

HUGH DUNN
Head of Finance of The City of Edinburgh Council
26 September 2018

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 2017/18 (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 2018).

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 2018, and their income and expenditure for the year ended 31 March 2018.

JOHN BURNS, FCMA CGMA
Chief Finance Officer of Lothian Pension Fund
26 September 2018

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 report of Lothian Pension Fund and its group, Lothian Buses Pension Fund and Scottish Homes Pension Fund (the funds) for the year ended 31 March 2018 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Lothian Pension Fund Fund Account, the Lothian Pension Fund 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 2017/18 (the 2017/18 Code).

In our opinion the accompanying financial statements:

- give a true and fair view in accordance with applicable law and the 2017/18 Code of the financial transactions of the funds during the year ended 31 March 2018 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 2017/18 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 for opinion

We conducted our audit in accordance with applicable law and International Standards on Auditing (UK) (ISAs (UK)). 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 Standard, 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.

Conclusions relating to going concern basis of accounting

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Chief Finance Officer has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the funds' ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Responsibilities of the Chief Finance Officer and the City of Edinburgh Council 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.

In preparing the financial statements, the Chief Finance Officer is responsible for assessing the funds' ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless deemed inappropriate.

The City of Edinburgh Council is responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit 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) 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.

A further description of the auditor's responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.
Other information in the annual report

The Chief Finance Officer is responsible for the other information in the annual report. 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, our responsibility is to read all the other information in the annual report and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Report on other requirements

Opinions on matters prescribed by the Accounts Commission

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
26 September 2018

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: the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund (the Funds). The Lothian Pension Fund group comprises the investment and pensions team employed by LPFE Limited (LPFE) supporting the Council in its separate statutory capacity as the administering authority of the Funds (Administering Authority) and LPFI Limited (LPFI), the groups regulated investment vehicle (together the LPF Group).

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 Joint Investment Strategy Panel; and
- the LPF Group.

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 Council is responsible for ensuring that its business in administering 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, senior officers and external representatives are responsible for implementing effective arrangements for governing the affairs of the LPF Group, and facilitating the effective exercise of its functions, including arrangements for the management of risk. The Pensions Committee oversees the operational administration of the Funds by the LPF Group.

The LPF Group 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 LPF Group 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 LPF Group operates within the wider governance framework of the Council but within specific ringfenced governance structures focused on the Funds themselves. The governance framework comprises the systems, processes, cultures and values by which the LPF Group directs and controls the Funds. It also describes the way the LPF Group engages with and accounts to its stakeholders in relation to the management of the administration of the Funds. It enables the LPF Group to monitor the achievement of its objectives and consider whether those objectives have led to the delivery of appropriate, cost-effective services. The framework also applies to any subsidiary companies which are members of the LPF Group, namely LPFI and LPFE. The LPF Group is also directly regulated by The Pensions Regulator, the Financial Conduct Authority (regarding its regulated investment activity), the Scottish Information Commissioner and is subject to other corporate and public sector rules and regulations.

The LPF Group's ongoing compliance with its governance framework and regulatory obligations is monitored on an ongoing basis by the Pensions Committee, the Audit Sub-Committee and the Pension Board.

The wider Council's Local Code of Corporate Governance is regularly reviewed and considered by the Governance, Risk & Best Value Committee. It has implemented arrangements for monitoring each element of the framework and providing evidence of compliance. The Council's Democracy, Governance and Resilience Senior 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 LPF Group places reliance upon certain of 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 LPF Group and the Funds governance framework within the Council, include:

- Identifying the objectives of the Funds in the Funding Strategy Statement, Statement of Investment Principles and Service Plan.
- Since April 2015, The Pensions Regulator has been responsible for setting standards of governance and administration for the Local Government Pension Scheme. The LPF Group has taken steps to fully integrate compliance with these standards within the overall governance framework.
- A systematic approach to monitoring service performance by the Pensions Committee, Pensions Audit Sub-Committee, Pension Board (each including external stakeholder representation), Independent Professional Observer and senior officers.
- A structured programme to ensure that Pensions Committee and Pension Board 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 and LPFI operating within their respective constitutional documentation and the relevant companies regulations.
- LPFI operating within the relevant governance policies and procedures to ensure compliance with the Financial Conduct Authority's rules, regulations and guidance.

- For LPF Group and Fund matters, the Pensions Committee, Pensions Audit Sub-Committee and Pension Board are responsible for scrutiny and challenge and a quarterly risk reporting process is in place to ensure full consideration of such matters.
- Officers of the LPF Group are managed separately through the processes and procedures of LPFE, overseen by its board of directors, with terms and conditions and a human resources performance review and management strategy tailored to the express needs of the Funds and their stakeholders.
- The directors of LPFE and LPFI have obligations to report to the Pensions Committee as the governing body for the Funds and Council in being the sole shareholder. In addition, the board and staff of LPFI are each individually regulated by the Financial Conduct Authority and so bound by the associated Principles and Standards of governance best practice.

Elements of the governance framework of the Council that are relevant to the LPF Group and Funds include:

- The Council is embedding a culture of commercial excellence to ensure that its services always deliver Best Value. That is ongoing and seeks to improve standards in buying practices and processes across the Council including, to the extent applicable, the LPF Group and the Funds which bear the cost of its operation and administration.
- The submission of reports, findings and recommendations from the external auditor, other inspectorates and internal audit, to the Pensions Committee, Pensions Audit Sub-Committee for all matters affecting the LPF Group and Funds and, in certain circumstances strictly for Council wide oversight purposes, the Corporate Leadership Group, Governance, Risk and Best Value Committee and wider Council.
- 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 the LPF 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 been sub-delegated to the Chief Finance Officer of the LPF Group.
- The Chief Internal Auditor has overall responsibility to review, appraise and report to management and the Governance, Risk and Best Value Committee, and for matters relating to the LPF Group and Funds to the Pensions Committee and Pensions Audit Sub-Committee, on the adequacy of relevant internal control and corporate governance arrangements and on risks relating to approved policies, programmes and projects.
- The Council's Democracy, Governance and Resilience Manager, reporting to the Head of Strategy and Insight, has responsibility for advising the Council on corporate governance arrangements and supports the LPF Group on certain aspects of its governance arrangements.
- The Governance, Risk and Best Value Committee, and for LPF Group and 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 LPF Group and 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 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.
- 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. A separate policy on Pensions Committee and Pension Board member training has been adopted and is overseen by the LPF Group's officers.
- Mandatory training for Councillors newly appointed to the Pensions Committee is programmed within the Induction and Training programme for Elected Members. This focuses on governance, investment management and strategy and how the LPF Group and Funds work. Committee members are reminded of the requirement to undertake a minimum of 21 hours of training per financial year to fulfil their role on the Pensions 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 LPF Group has adapted policies to take into account the specific nature of its business and regulation.
- The Whistleblowing policy provides a process for disclosure in the public interest about the Council and its activities by officers, Elected Members and others. The LPF Group has an adapted policy to take into account the specific nature of its business and regulation.
- A Register of Members' Interests and Registers of Officers' interests are maintained and available for public inspection.

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 LPG Group and Funds. Following the establishment of the wholly-owned subsidiary companies, LPFE and LPFI, the Council continues to have appropriate assurance processes and procedures in relation to the responsible officers involved in the administration of those companies and so the wider LPF Group administering 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 considers that significant enhancements are required to the LPF control environment and governance and risk management frameworks, and is raising a 'red' rated opinion, with our assessment towards the middle of this category."

In compliance with standard accounting practice, the Head of Finance, of the City of Edinburgh Council 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 2018. It is the Head of Finance's 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 the LPF Group has provided a statement of the effectiveness of the internal financial control system for the year ended 31st March 2018 for the Funds. It is the Chief Finance Officer's opinion "that based on internal audit work undertaken during the year, has highlighted a need for significant enhancements to the control environment and associated governance and risk management frameworks. The control improvements implicit in this opinion will be examined and corresponding required improvements as they relate to financial systems implemented as a matter of urgency."

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 LPF Group in its administration of the Funds. We consider the governance and internal control environment operating during the financial year from 1 April 2017 to 31 March 2018 to provide reasonable and objective assurance that any significant risks impacting on the LPF Group and its ability to achieve its objectives in properly administering the Funds have and will continue to be identified and suitably proportionate actions have and will be taken to avoid or mitigate the impact of any such risks.

The LPF Group has identified certain key areas for improvement, summarised as follows:

- ICT: Continuing to engage with ICT service provider and the City of Edinburgh Council to monitor and drive improvements in the ICT services which the LPF Group receives, whilst in tandem continuing to assess the position around the LPF Group procuring a separate ICT provider to solely and independently service its specific ICT requirements in support of its strategic business plan.
- Human resources: To continue to implement the new human resources strategy specific to LPF Group's requirements.
- Independent professional observer: To appoint a replacement Independent Professional Observer in support the work and governance of the Pensions Committee and the Pension Board.
- Pension Board: To ensure that vacancies in the Pension Board are filled timeously and by suitable candidates and that this body of external stakeholder representatives receives the training and support that it requires on an ongoing basis.
- Business continuity: To continue to assess and refresh the business continuity plan on an ongoing basis ensuring sufficient engagement with staff.
- Information governance: Having completed a full information governance compliance project prior to the implementation of new data protection laws on 25 May 2018, to continue to implement ongoing actions to ensure continuing best practice information governance and security within the LPF Group, including monitoring and engaging with third party suppliers where appropriate.
- Financial services regulatory compliance: To continue to instruct external compliance audits on the operations and governance of LPFI in order to ensure best practice compliance and assurance around its existing operations (and in preparation for its extended collaborative business model) and take action to address the recommendations from those audits on an ongoing basis.
- Wider governance: To continue to maintain and reinforce separate governance and controls specific to the needs of the LPF Group, the pensions funds it administers and its distinct duties to employer and member stakeholders; consistently throughout the LPF Group's governance structures. To ensure that oversight by the City of Edinburgh Council is supported in a manner consistent with these duties.

The LPF Group will ensure that these are treated as a priority and that progress towards implementation will be reviewed through the governance structures and processes established for the LPF Group and summarised herein.

ANDREW KERR	**STEPHEN MOIR**	**CLARE SCOTT**
Chief Executive	**Executive Director of Resources**	**Chief Executive**
The City of Edinburgh Council	**The City of Edinburgh Council**	**Lothian Pension Fund**
26 September 2018	**26 September 2018**	**26 September 2018**

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 2018 and over the financial year.

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	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: - Five City of Edinburgh Council elected members - Two external members, one drawn from the membership of the Funds and one drawn from the employers that participate in the Funds.
Structure	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	The Pensions Committee includes two external places for pension fund stakeholders i.e. one each from the employer and member representatives. Fund members and employers are also represented within the Funds' Pension Board. Membership includes five employer representatives and five member representatives. 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. Two members of the Pension Board attend the Pensions Audit Sub-Committee.

Principle		Full Compliance	Comments
Structure	That where a secondary committee or board has been established, the structure ensures effective communication across both levels.	Yes	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. Implementation of investment strategy is delegated to the Executive Director of Resources who then delegates to the Head of Finance, who takes advice from the Joint Investment Strategy Panel. The Panel meets quarterly and reports to the Pensions Committee annually. The Joint Investment Strategy Panel consists of the Head of Finance of the City of Edinburgh Council and the Chief Executive Officer, Chief Finance Officer, Chief Investment Officer of the LPF Group plus three experienced external industry advisers. The Pensions Committee receives annual updates from LPFE and LPFI.
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	The Pension Board consists of a mix of representatives: - 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.

Principle		Full Compliance	Comments
Representation	Where appropriate, independent professional observers, and expert advisers (on an ad-hoc basis).	Yes	An Independent Professional Observer was appointed in March 2013 to help Committee scrutinise advice. This contract expired in February 2018 and a selection process is underway to reappoint this role. As above, external investment advisers sit on the Joint Investment Strategy Panel. 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. A non-executive director was appointed to the board of LPFI on 7 February 2017 and LPFE on 19 March 2018. An external compliance consultant supports the LPF Group on its ongoing compliance with the Financial Conduct Authority rules, regulations and guidance.
	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	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. The Pensions Committee takes account of the views of the Pension Board when making decision.
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	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. The non-elected members confirm that they have read, signed and will abide by a Code of Conduct (specifically tailored for the Pensions Committee and Pension Board) prior to their appointment to those bodies. The elected members are required to read, sign and abide by the Councillors' Code of Conduct.

Principle		Full Compliance	Comments
Selection and Role of Lay Members	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	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. A Code of Conduct also applies to all members of the Pensions Committee and the Pension Board. The declaration of board members interest is a standard item on the agenda for the meetings for the LPFE and LPFI board meetings.
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 LPF Group's Nomination and Appointments Policy clearly documents how employer and member representatives will be elected to the Pensions Committee and Pension Board. LPFI and LPFE board members conduct meetings and other matters in accordance with their respective articles of association and shareholders' agreements.
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 LPF Group's website www.lpf.org.uk. Board members and staff working for LPFI and LPFE also attend separate training for the purposes of their knowledge, understanding and (where appropriate) compliance with Financial Conduct Authority regulations.

Principle		Full Compliance	Comments
Training / Facility Time / Expenses	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 Joint 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 such meetings. Further meetings are held if necessary. The LPFE board now meet five time a year (in February, May, August, October and December) and the LPFI board meet monthly.
	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	

Principle		Full Compliance	Comments
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	Pensions Committee papers and minutes are publicly available on the Council's website and all Pensions 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 and the LPF Group. 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.
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 LPF Group's website. The LPF Group also communicates regularly with employers and scheme members.

ANDREW KERR
Chief Executive
The City of Edinburgh Council
26 September 2018

STEPHEN MOIR
Executive Director of Resources
The City of Edinburgh Council
26 September 2018

CLARE SCOTT
Chief Executive
Lothian Pension Fund
26 September 2018

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
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:	In-house

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 the details on the back page.

LOTHIAN PENSION FUNDS

pensions@lpf.org.uk

0131 529 4638

www.lpf.org.uk

Lothian Pension Fund, Atria One, 144 Morrison Street, Edinburgh EH3 8EX

Appendix 3

LPFE Limited

Financial Statements

For the year ended 31 March 2018

Registered number SC497543

LPFE LIMITED

Financial statements

For the year ended 31 March 2018

Contents	**Page**

LPFE LIMITED

Company information

Board of Directors:	Hugh Dunn Clare Scott Alasdair Rankin Katy Miller Stephen Moir Leslie Robb	
Company Secretaries:	D.W Company Services Limited Struan Fairbairn	Resigned 16 March 2018
Registered office	4th Floor Saltire Court 20 Castle Terrace Edinburgh Lothian EH1 2EN	
Bankers:	The Royal Bank of Scotland plc	
Auditor:	Scott-Moncrieff Chartered Accountants Exchange Place 3 Semple Street Edinburgh EH3 8BL	

LPFE LIMITED

Directors' report

For the year ended 31 March 2018

The directors present their report and audited financial statements for the year ending 31 March 2018.

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 and the Scottish Homes Pension Fund ("the Funds") and, separately, to Falkirk Council in their capacity as the administering authority of the Falkirk Council Pension Fund. All pension funds are part of the Local Government Pension Scheme in Scotland.

Results, dividends and mutual trading surplus

The loss for the year after tax was £1,535,060 (2017 - £6,275 profit) and after allowing for items included under "Other comprehensive income" a loss of £853,960 (2017 - £396,275 loss). The directors do not recommend payment of 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 £40,112 (2017 - £2,464) in respect of accrued holiday pay and £1,536,000 (2017 - £22,000) for adjustments to pension costs under IAS19, the underlying trading profit is £41,052 (2017 - £30,739). The £1,536,000 IAS19 pension adjustment includes a net liability of £1,377,000 in respect of the accrued pension benefits of the staff that transferred their employment from the City of Edinburgh Council during the year. The additional gains recognised under "Other comprehensive income" amounting to £681,100 (2017: £402,550 additional costs) all relates 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 the profit arising from the mutual trade can be returned to the Council. Although there was an underlying trading profit of £40,858 (2017: £30,739), 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 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 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) on that entity beginning to trade during the year.

In February 2018, the transfer of the employment of 43 staff from the City of Edinburgh to the company under TUPE arrangements was completed. This means that the entire staff working for Lothian Pension Fund are now employed by LPFE Limited. Having the whole team together under the same employer will provide more opportunities to develop services for Lothian Pension Fund's members and employers. The company has entered into an appropriate admission arrangement 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 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.

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 which means that it is in a position to adapt to any future staffing requirements.

Directors

The directors who served during the period were:

Hugh Dunn	
Clare Scott	
Alasdair Rankin	
Katy Miller	
Stephen Moir	Appointed 6 September 2017
Leslie Robb	Appointed 19 March 2018

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: 28 May 2018
Stephen Moir
Chairperson

LPFE LIMITED

Independent auditor's report to the members of LPFE Limited

For the year ended 31 March 2018

Opinion

We have audited the financial statements of LPFE Limited ('the company') for the year ended 31 March 2018 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.

In our opinion:

- give a true and fair view of the state of the company's affairs as at 31 March 2018 and its loss 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.

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.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. 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 company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our 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 audit opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate, or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report on this regard.

Opinion on Other Matter(s) Prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and

- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

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, or returns adequate for our audit have not been received from branches not visited by us; or

- the 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.

Responsibilities of directors

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, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Independent auditor's report to the members of LPFE Limited (continued)

For the year ended 31 March 2018

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain 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) 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.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Councils website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's 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:28 May 2018

LPFE LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2018

	Note	2018 £	2017 £
Continuing Operations			
Revenue	1e	1,592,314	1,189,855
Gross profit		1,592,314	1,189,855
Administrative expenses		(3,099,188)	(1,176,881)
(Loss)/profit from operations	2	(1,056,874)	12,974
Finance costs	3	(28,380)	(6,720)
(Loss)/profit before tax		(1,535,254)	6,254
Corporation tax credit	4	194	21
(Loss)/profit for the year		(1,535,060)	6,275
Other comprehensive income:			
Those that are not recyclable net of tax:			
Actuarial gains/(losses) on retirement benefit obligation	15	506,000	(483,000)
Deferred tax charge thereon	10	175,100	80,450
Total comprehensive loss for the year		(853,960)	(396,275)

The accompanying notes on pages 12 to 28 form part of these financial statements

LPFE LIMITED

Statement of Financial Position

As at 31 March 2018

	Note	As at 31 March 2018 £	As at 31 March 2017 £
Non-current assets			
Deferred tax asset	10	291,550	116,450
Total non-current assets		291,550	116,450
Current assets			
Trade and other receivables	7	340,881	166,801
Cash and cash equivalents	8	10,450	13,381
Total current assets		351,331	180,182
Total assets		642,881	296,632
Equity and Liabilities			
Equity attributable to equity holders of the parent			
Share capital	11	1	1
Retained earnings	12	(1,392,689)	(538,729)
		(1,392,688)	(538,728)
Liabilities			
Non-current liabilities			
Retirement benefits obligation	15	1,715,000	685,000
Total non-current liabilities		1,715,000	685,000
Current liabilities			
Trade and other payables	9	320,569	150,360
Total current liabilities		320,569	150,360
Total liabilities		2,035,569	835,360
Total equity and liabilities		642,881	296,632

The financial statements were authorised for issue by the Board of Directors on
28 May 2018
And were signed on its behalf by:

Stephen Moir
Director

Registered number SC497543

The accompanying notes on pages 12 to 28 form part of these financial statements

LPFE Limited

Statement of Changes in Equity

As at 31 March 2018

	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		1	(538,729)	(538,728)

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2017		1	(538,729)	(538,728)
Comprehensive income				
Profit for the year		-	(1,535,060)	(1,535,060)
Other comprehensive income				
Actuarial losses on retirement benefit obligation in year	15	-	506,000	506,000
Deferred tax on retirement benefit obligation	10	-	175,100	175,100
Balance at 31 March 2018		1	(1,392,689)	(1,392,688)

The accompanying notes on pages 12 to 28 form part of these financial statements

LPFE LIMITED

Statement of Cash Flows

For the year ended 31 March 2018

	2018 £	2017 £
Cash flow from operating activities		
Profit for the year	(1,535,060)	6,275
Adjustments for:		
Defined benefit pension – current service cost	336,000	172,000
Defined benefit pension – employer contribution	(204,000)	(156,000)
Defined benefit pension – business combinations	1,377,000	-
Defined benefit pension – finance costs	27,000	6,000
Other finance costs	1,380	720
Changes in assets and liabilities:		
(Increase) in receivables and other financial assets	(174,080)	(19,008)
Increase in payables	135,285	17,342
Cash flows from operations	(36,475)	27,329
Interest paid	(1,195)	(901)
Net cash flows from operating activities	(37,670)	26,428
Cash flow from investing activities	-	-
Net cash flows from investing activities	-	-
Cash flow from financing activities		
Movement in loan facility	34,739	(18,112)
Net cash flows from financing activities	34,739	(18,112)
Net (decrease)/increase in cash and cash equivalents	(2,931)	8,316
Cash and cash equivalents at beginning of year	13,381	5,065
Cash and cash equivalents at end of year	10,450	13,381
Cash at bank and in hand	10,450	13,381

The accompanying notes on pages 12 to 28 form part of these financial statements

1. Statement of significant accounting policies

LPFE Limited is a limited company incorporated in Scotland. The address of its registered office and principal place of business are disclosed on page 1. The principal activities of the company are described within the directors' report on pages 2 to 4.

The financial statements of LPFE Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS), IFRIC Interpretation 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 2017:

- IAS 7, Statement of Cash Flows

No changes have materially impacted the calculation of the figures in the statement of cash flows in the financial statements but where relevant disclosures have been made in the notes to comply with the standard.

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 1, Presentation of Financial Statements	1 January 2018
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
IAS 12, Income Taxes*	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 their effects are as follows:

IAS 1 has been amended after the issue of IFRS 9 with the main effect on the company being to amend the presentation and disclosure of assets held at amortised cost. Given the nature of the company's financial assets this standard is not expected to have a material impact on the company's financial statements in the period of initial application.

IAS 39 requirements will be replaced by IFRS 9 on Financial Instruments, with the main effect on the company being to re-categorise financial assets and liabilities together with IFRS 7 on Financial Instruments Disclosures. The disclosures will be amended in the company's financial statements as required.

IFRS 16 on leases is not expected to have a material impact on the financial statements as the company currently has no material lessee or lessor transactions.

1. Statement of significant accounting policies (continued)

Guidance in issue but not in force (continued)

IAS 12 on income taxes has been amended with reference to recognition of income tax on dividends paid. The company currently is not expected to pay a dividend therefore this amendment is not expect to affect the financial statements.

IFRS 15 deals with contracts to provide goods or services in recording income from service contracts the company currently recognises costs, particularly staff costs, when incurred. The service contract has no performance obligations and there is little ambiguity surrounding the transaction price as services are charged for purely to cover costs incurred. Therefore the directors consider the company already compliant with IFRS 15 and expect little change on implementation.

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 financial statements have been prepared on the historical cost basis.

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:

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.

1. Statement of significant accounting policies (continued)

b. Current and deferred income tax (continued)

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.

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.

1. Statement of significant accounting policies (continued)

f. Value added tax (continued)

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.

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.

1. Statement of significant accounting policies (continued)

i. Financial instruments (continued)

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.

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).

2. (Loss)/profit from operations

	2018 £	2017 £
(Loss)/profit from operations has been determined after deducting:		
Auditor's remuneration:		
Audit services	4,900	4,800
Non-Audit services	8,100	3,798

3. Finance costs

	2018 £	2017 £
Loan interest payable to group entities (note 14)	1,380	720
Pension interest costs (note 15)	27,000	6,000
	28,380	6,720

4. Corporation tax credit

	2018 £	2017 £
Current tax:		
Corporation tax credit	(194)	(21)
Tax on profits for the year	(194)	(21)

Corporation tax credit is calculated at 19% (2017: 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:

	2018 £	2017 £
(Loss)/profit for the year before taxation	(1,535,254)	6,254
(Loss)/profit for the year at the effective rate of corporation tax of 19% (2017 – 20%)	(291,698)	1,251
Effects of:		
Mutual trade adjustment	265,242	(1,753)
Expenses not deductible for tax purposes	26,262	438
Trading losses carried forward	-	42
Other adjustments	-	1
Current tax credit	(194)	(21)

5. Employee benefits expense

The average number of persons employed by the company (including directors) during the year was 20 (2017: 11).

The aggregate payroll costs were as follows:

	2018	2017
	£	£
Wages and salaries	1,136,832	849,767
Social security costs	134,079	104,078
Defined benefit pension obligation - current service cost	336,000	172,000
	1,606,911	1,125,845

6. Directors' remuneration

Two directors received emoluments from the company during the period. The directors' emoluments for the period were as follows:

	2018	2017
	£	£
Aggregate emoluments	102,801	92,000
Employer pension contributions	20,685	18,860

One director had an accrued pension entitlement of £20,225 (2017: £16,799) and a lump sum entitlement of £12,938 (2017: £11,843) at the end of the year. The other director does not have any pension provision provided by the company.

All other directors are employed by the City of Edinburgh Council.

7. Trade and other receivables

	2018	2017
	£	£
Trade receivables	35,927	29,433
Amounts due from group entities	295,304	137,354
Prepayments and accrued income	9,650	14
	340,881	166,801

The directors consider the fair value of receivables to be in line with carrying values.

8. Cash and cash equivalents

	2018	2017
	£	£
Cash at bank and in hand	10,450	13,381

9. Current liabilities

	2018 £	2017 £
Trade payables	13,315	3,109
Accruals and deferred income	140,782	39,813
Social security and other taxes	155,804	107,425
Amounts due to group entities	10,668	13
	320,569	150,360

10. Deferred tax

	2018 £	2017 £
At 31 March 2017	116,450	36,000
Charge for the year to other comprehensive income	175,100	80,450
At 31 March 2018	291,550	116,450

The elements of deferred tax are as follows:

	2018 £	2017 £
Defined benefit pension scheme liability	291,550	116,450
	291,550	116,450

11. Share Capital

	2018 £	2017 £
Allotted, called up and fully paid		
Ordinary shares of £1 each	1	1
	1	1

12. Reserves

	Retained Earnings £
At 31 March 2016	(142,454)
Profit for the year	6,275
Actuarial (loss) on retirement benefit obligation	(483,000)
Deferred tax on retirement benefit obligation	80,450
At 31 March 2017	(538,729)
(Loss) for the year	(1,535,060)
Actuarial gain on pension plan	506,000
Deferred tax on retirement benefit obligation	175,100
At 31 March 2018	(1,392,689)

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

14. Related party transactions

	2018 £	2017 £
Lothian Pension Fund (pension fund administered by City of Edinburgh Council)		
Sale of services during the period	1,449,997	1,073,448
Receivables at the period end	287,782	104,803
Loan facility balance (payable)/receivable at the period end	(10,470)	24,269
Interest payable during the period	1,380	720
Interest payable but still accruing at the period end	198	13
Lothian Buses Limited (company under common control)		
Balance receivable for group tax losses surrendered	-	1,321
LPFI Limited (company under common control)		
Sale of services during the period	20,236	6,940
Receivables at the period end	7,306	6,940
Balance receivable for group tax losses surrendered	215	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:

	2018 £	2017 £
Short-term employee benefits	472,188	432,805
Post-employment benefits - employer pension contributions	84,962	77,616
	557,150	510,421

Key management personnel had accrued pensions totalling £97,456 (2017: £81,825) and lump sums totalling £110,889 (2017: £100,185) at the end of the period.

All other key management personnel are employed by the City of Edinburgh Council.

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 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 March 2017 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:

	%	**2018 £'000**	**%**	**2017 £'000**
Equity Securities:				
Consumer	14%	1,187	15%	425
Manufacturing	15%	1,288	15%	429
Energy and Utilities	6%	542	7%	210
Financial Institutions	9%	769	7%	197
Health and Care	5%	425	6%	166
Information Technology	6%	528	5%	140
Other	6%	543	7%	195
Debt Securities:				
Corporate Bonds (investment grade)	0%	-	0%	-
Corporate Bonds (non-investment grade)	2%	169	0%	-
UK Government	10%	839	10%	284
Other	0%	-	0%	6
Private Equity:				
All	2%	158	3%	91
Real Estate				
UK Property	6%	556	7%	191
Overseas property	0%	9	0%	-
Investment Funds and Unit Trusts:				
Equities	1%	83	0%	-
Commodities	0%	-	0%	8
Bonds	0%	-	1%	42
Infrastructure	12%	1,025	9%	253
Other	0%	20	2%	60
Cash and Cash Equivalents:				
All	6%	511	5%	131
	100%	8,652	100%	2,828

15. Retirement benefits obligation (continued)

The amounts recognised in the statement of financial position are determined as follows:	**2018 £'000**	**2017 £'000**
Fair value of plan assets	8,652	2,828
Present value of scheme liabilities	(10,367)	(3,513)
Net pension liability	(1,715)	(685)

The movement in the defined benefit obligation over the year is as follows:

	2018 £'000	**2017 £'000**
Brought forward	3,513	2,277
Current service cost	336	172
Interest cost on obligation	131	86
Plan participants contributions	91	76
Benefits paid	(4)	-
Effects of business combinations	7,088	
Actuarial (gains)/losses arising from changes in financial assumptions	(536)	902
Actuarial losses arising from changes in demographic assumptions	120	-
Other actuarial (gains)	(372)	-
Balance at year end	10,367	3,513

The movement in the fair value of plan assets of the year is as follows:

	2018 £'000	**2017 £'000**
Brought forward	2,828	2,097
Benefits paid	(4)	-
Effect of business combinations	5,711	-
Interest income on plan assets	104	80
Contributions by employer	204	156
Contributions by member	91	76
Return on assets excluding amounts included in net interest	(282)	419
Balance at year end	8,652	2,828

15. Retirement benefits obligation (continued)

The amounts recognised in the Statement of Profit or Loss are as follows:

	2018 £'000	2017 £'000
Interest received on pension scheme assets	(104)	(80)
Interest cost on pension scheme liabilities	131	86
Finance (income)/cost	27	6
Current service cost	336	172
Effect of business combinations	1,377	-
	1,740	178

Amounts recognised in other comprehensive income:

	2018 £'000	2017 £'000
Actuarial gains/(losses) in the defined benefit obligation	788	(902)
Actuarial (losses)/gains in the fair value of defined benefit assets	(282)	419
	506	(483)

The principal actuarial assumptions used in this valuation were:

	2018	2017
Inflation/pension increase rate	2.3%	2.4%
Salary increase rate	4.0%	4.4%
Discount rate	2.7%	2.7%

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.

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)	
	2018	2017	2018	2017
0.5% decrease in real discount rate	13%	14%	1,354	508
0.5% increase in the salary increase rate	4%	7%	455	237
0.5% increase in the pension increase rate	8%	7%	859	252

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	21.7	24.3
Future pensioners	24.7	27.5

Expected employer contributions to the benefit plans for the year ended 31 March 2019 are £415,000, based on a pensionable payroll cost of £1,742,000.

16. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable. Financial instruments do not include prepayments, VAT, taxation, social security and deferred income.

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:

	2018 £	2017 £
Financial Assets		
Cash and cash equivalents	10,450	13,381
Trade and other receivables	333,531	166,787
Total Financial Assets	343,981	180,168
Financial Liabilities		
Trade and other payables	164,765	42,935
Total Financial Liabilities	164,765	42,935

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 2018 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 three customers. By far the largest customer is the City of Edinburgh Council and the company is securely funded by the Council. Falkirk Council is a smaller customer. The third customer is LPFI Limited which is a related party. Given the financial stature of both Councils and LPFI Limited 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.

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 2018 £	1 to 5 Years 2018 £	Total 2018 £
Financial liabilities due for payment				
Trade and other payables		(164,765)	-	(164,765)
Total expected outflows		(164,765)	-	(164,765)
Financial assets — cash flows realisable				
Cash and cash equivalents		10,450	-	10,450
Trade and other receivables		333,531	-	333,531
Total anticipated inflows		343,981	-	343,981
Net inflow of financial instruments		179,216	-	179,216

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 £385,000 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.

17. Movements in financing (assets)/liabilities arising from financing activities

	Current loans & borrowings
At 1 April 2016	(6,157)
Cash flows	
Repayment of financing loans from group companies	(18,112)
At 31 March 2017	(24,269)

	Current loans & borrowings
At 1 April 2017	(24,269)
Cash flows	
Financing loans from group companies drawdown	34,739
At 31 March 2018	10,470

LPFI Limited

Financial Statements

For the year ended 31 March 2018

Registered number SC497542

LPFI LIMITED

Financial statements

For the year ended 31 March 2018

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LPFI LIMITED

Company information

Board of Directors:	*Chairman*	
	Hugh Dunn	
	Executive Directors	
	Struan Fairbairn John Burns William Bruce Miller Clare Scott	
	Non-executive Director	
	Leslie Robb	
Company Secretary:	D.W. Company Services Limited	Resigned 16 March 2018
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 2018

The directors present their report and audited financial statements for the year ended 31 March 2018.

Principal activity

The current principal activity of the company is the provision of Financial Conduct Authority ("FCA") regulated investment services to the 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 £34,619 (2017: £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) ("Lothian"), 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 Lothian 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 Lothian for the provision of short term working capital.

LPFI Limited does not employ staff directly. Staffing and business support services are provided to the company under separate intra-group agreements with LPFE Limited and Lothian respectively. LPFE Limited is also wholly owned by Lothian. The company provides certain investment services to Lothian via an intra-group investment services agreement.

HMRC has agreed that any profits arising 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. During the year the company provided services in relation to a number of infrastructure investments

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.

Directors

The directors who served during the year were:

Hugh Dunn
Struan Fairbairn
John Burns
William Bruce Miller
Clare Scott
Leslie Robb

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.

LPFI LIMITED

Directors' report (continued)

For the year ended 31 March 2018

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: 28 May 2018

Hugh Dunn
Chairman

LPFI LIMITED

Independent auditor's report to the members of LPFI Limited

For the year ended 31 March 2018

Opinion

We have audited the financial statements of LPFI Limited ('the company') for the year ended 31 March 2018 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.

In our opinion:

- give a true and fair view of the state of the company's affairs as at 31 March 2018 and 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.

Use of our report

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.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. 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 company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our 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 audit opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate, or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report on this regard.

Opinion on Other Matters Prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- 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.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

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, or returns adequate for our audit have not been received from branches not visited by us; or
- the 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.

Responsibilities of directors

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, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain 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) 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.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Councils website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's 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: 28 May 2018

LPFI LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2018

	Note	2018 £	2017 £
Continuing Operations			
Revenue	1e	130,212	23,988
Gross profit		130,212	23,988
Administrative expenses		(87,305)	(23,348)
Profit from operations	2	42,907	640
Finance costs	3	(168)	(100)
Profit before income tax expense		42,739	540
Corporation tax charge	4	(8,120)	(108)
Profit for the year		34,619	432
Other comprehensive income		-	-
Total comprehensive income for the year		34,619	432

The accompanying notes on pages 12 to 22 form part of these financial statements

LPFI LIMITED

Statement of Financial Position

As at 31 March 2018

	Note	As at 31 March 2018 £	As at 31 March 2017 £
Current assets			
Trade and other receivables	6	58,965	13,246
Cash and cash equivalents	7	83,209	70,661
Total current assets		142,174	83,907
Total assets		142,174	83,907
Equity and Liabilities			
Equity attributable to equity holders of the parent			
Share capital	10	60,000	50,000
Retained earnings	11	35,051	432
		95,051	50,432
Liabilities			
Non-current liabilities			
Trade and other payables	9	-	16,000
Total non-current liabilities		-	16,000
Current liabilities			
Trade and other payables	8	47,123	17,475
Total current liabilities		47,123	17,475
Total liabilities		47,123	33,475
Total equity and liabilities		142,174	83,907

The financial statements were authorised for issue by the Board of Directors on 28 May 2018 and were signed on its behalf by:

Hugh Dunn
Director

Registered number SC497542

The accompanying notes on pages 12 to 22 form part of these financial statements

LPFI LIMITED

Statement of Changes in Equity

As at 31 March 2018

	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		50,000	432	50,432

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2017		50,000	432	50,432
Comprehensive income				
Profit for the year		-	34,619	34,619
Share movements				
Shares allotted during the year	10	10,000	-	10,000
Balance at 31 March 2018		60,000	35,051	95,051

The accompanying notes on pages 12 to 22 form part of these financial statements

LPFI LIMITED

Statement of Cash Flows

For the year ended 31 March 2018

	2018 £	2017 £
Cash flow from operating activities:		
Profit for the year	34,619	432
Adjustments for:		
Finance costs	168	100
Changes in assets and liabilities:		
(Increase) in receivables and other financial assets	(45,719)	(13,246)
Increase in payables	29,737	17,386
Cash flows from operations	18,805	4,672
Interest paid	(257)	(11)
Net Cash flows from operating activities	18,548	4,661
Cash flow from financing activities:		
Loans (repaid)/received from group entities	(16,000)	16,000
Share capital issued	10,000	49,999
Net cash flows from financing activities	(6,000)	65,999
Net increase in cash and cash equivalents	12,548	70,660
Cash and cash equivalents at beginning of year	70,661	1
Cash and cash equivalents at end of year	83,209	70,661
Cash at bank and in hand	83,209	70,661

The accompanying notes on pages 12 to 22 form part of these financial statements

1. Statement of significant accounting policies

LPFI Limited is a limited company incorporated in Scotland. The address of its registered office and principal place of business are disclosed on page 1. The principal activities of the company are described within the directors' report on pages 2 to 4.

The financial statements of LPFI Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS), IFRIC Interpretation 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 January 2017:

- IAS 7, Statement of Cash Flows

No changes have materially impacted the calculation of the figures in the statement of cash flows in the financial statements but where relevant disclosures have been made in the notes to comply with the standard.

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 1, Presentation of Financial Statements	1 January 2018
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
IAS 12, Income Taxes*	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 their effects are as follows:

IAS 1 has been amended after the issue of IFRS 9 with the main effect on the company being to amend the presentation and disclosure of assets held at amortised cost. Given the nature of the company's financial assets this standard is not expected to have a material impact on the company's financial statements in the period of initial application.

IAS 39 requirements will be replaced by IFRS 9 on Financial Instruments, with the main effect on the company being to re-categories financial assets and liabilities together with IFRS 7 on Financial Instruments Disclosures. The disclosures will be amended in the company's financial statements as required.

IFRS 16 on leases is not expected to have a material impact on the financial statements as the company currently has no lessee or lessor transactions.

IAS 12 on income taxes has been amended with reference to recognition of income tax on dividends paid. The company currently has no intention of paying a dividend therefore this amendment is not expect to affect the financial statements.

1. Statement of significant accounting policies (continued)

Guidance in issue but not in force (continued)

IFRS 15 deals with contracts to provide goods or services, in recording income from service contracts the company currently recognises costs, particularly staff costs, when incurred. The service contract has no performance obligations and there is little ambiguity surrounding the transaction price as services are charged for purely to cover costs incurred. Therefore the directors consider the company already compliant with IFRS 15 and expect little change on implementation.

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 financial statements have been prepared on the historical cost basis.

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:

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.

1. Statement of significant accounting policies (continued)

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.

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.

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.

2. Profit from operations

	2018 £	2017 £
Profit from operations has been determined after deducting:		
Auditor's remuneration:		
Audit services	3,400	3,250
Non-Audit services	6,470	1,600

3. Finance costs

	2018 £	2017 £
Loan interest payable to group entities (note 13)	168	100
	168	100

4. Corporation tax charge

	2018 £	2017 £
Current tax:		
Corporation tax charge	7,926	87
Inter- company tax	194	21
Tax on profits for the year	8,120	108

Corporation tax expense is calculated at 19% (2017: 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:

	2018 £	2017 £
Profit for the year before taxation	42,739	540
Profit for the year at the effective rate of corporation tax of 19% (2017 – 20%)	8,120	108

5. Employee Benefits Expense

The aggregate payroll costs for the year consisted of fees paid to a non-executive director. These were as follows:

	2018	2017
	£	£
Wages and salaries	12,000	2,000
Social security costs	651	89
	12,651	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 £5,116 (2017: £2,344) for services provided by directors employed by LPFE Limited during the year.

6. Trade and other receivables

	2018	2017
	£	£
Trade debtors	34,200	3,988
Prepayments	-	9,258
VAT recoverable	24,765	-
	58,965	13,246

The directors consider the fair value of receivables to be in line with carrying values.

7. Cash and cash equivalents

	2018	2017
	£	£
Cash at bank and in hand	83,209	70,661

8. Trade and other payables

	2018	2017
	£	£
Trade creditors	508	-
Accruals	30,084	5,745
Social security and other taxes	-	4,233
Corporation tax	7,926	87
Amounts due to group entities	8,605	7,410
	47,123	17,475

9. Non-current liabilities

	2018 £	2017 £
Amounts due to group entities	-	16,000
	-	16,000

10. Share Capital

	2018 £	2017 £
Allotted, called up and fully paid		
Ordinary shares of £1 each	60,000	50,000
	60,000	50,000

The company issued 10,000 Ordinary shares of £1 each during the year at par value.

11. Reserves

	Retained Earnings £
At 31 March 2016	-
Profit for the year	432
At 31 March 2017	432
Profit for the year	34,619
At 31 March 2018	35,051

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

13. Related parties

	2018 £	2017 £
Lothian Pension Fund (pension fund administered by City of Edinburgh Council)		
Business support costs	1,083	360
Payables at the period end	1,083	360
Loan facility balance payable at the period end	-	16,000
Loan facility repaid during the year	16,000	-
Interest payable during the period	168	100
Interest payable but still accruing at the period end	-	89
LPFE Limited (company under common control)		
Staff and other cost recharges	20,236	6,940
Payables at the period end	7,306	6,940
Group tax losses utilised	194	21
Balance payable for group tax losses utilised	215	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:

	2018 £	2017 £
Short-term benefits (note 5)	12,651	2,089
	12,651	2,089

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 £5,116 (2017: £2,344) for services provided by key management personnel employed by LPFE Limited during the year.

14. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable. Financial instruments do not include prepayments, VAT, taxation, social security and deferred tax.

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:

	2018 £	2017 £
Financial assets		
Cash and cash equivalents	83,209	70,661
Trade and other receivables	34,200	3,988
Total financial assets	117,409	74,649
Financial liabilities		
Current liabilities - Trade and other payables	15,197	13,155
Non-current liabilities - Trade and other payables	-	16,000
Total financial liabilities	15,197	29,155

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 2018 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.

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

	Within 1 Year 2018 £	1 to 5 Years 2018 £	Total 2018 £
Financial liabilities due for payment			
Trade and other payables	(15,197)	-	(15,197)
Total expected outflows	(15,197)	-	(15,197)
Financial assets — cash flows realisable			
Cash and cash equivalents	83,209	-	83,209
Trade and other receivables	34,200	-	34,200
Total anticipated inflows	117,409	-	117,409
Net inflow of financial instruments	102,212	-	102,212

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 customers settling invoices for services provided.

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.

15. Movements in financing (assets)/liabilities arising from financing activities

	Share capital	Current loans & borrowings	Total
At 01 April 2016	1	-	1
Cash flows			
Financing loans from group companies withdrawn	-	16,000	16,000
Issue of share capital	49,999	-	49,999
At 31 March 2017	50,000	16,000	66,000

	Share capital	Current loans & borrowings	Total
At 01 April 2017	50,000	16,000	66,000
Cash flows			
Repayment of financing loans from group companies	-	(16,000)	(16,000)
Issue of share capital	10,000	-	10,000
At 31 March 2018	60,000	-	60,000

Appendix 5

Lothian
PENSION FUND

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 2018 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 year to 31 March 2018 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 2017/18 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 2018 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 2017/18 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.

Yours faithfully

John Burns

Chief Finance Officer (Section 95 Officer for the Pension Funds)