

Pensions Committee

10.00 a.m., Tuesday, 17th June 2014

Statement of Investment Principles

Item number	5.5
Report number	
Executive/routine	
Wards	All

Executive summary

This report introduces the Lothian Pension Fund, Lothian Buses Fund and Scottish Homes Pension Fund (the Funds') revised Statement of Investment Principles (SIP) (appendix 1), which replaces that agreed by Committee in June 2013.

Links

Coalition pledges

Council outcomes

CO26- The Council engages with stakeholders and works in partnerships to improve services and deliver agreed objectives.

Single Outcome Agreement

Statement of Investment Principles

Recommendations

- 1.1 That the Committee adopts the revised Statement of Investment Principles.

Background

- 2.1 The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 require administering authorities to prepare, maintain and publish a written Statement of Investment Principles.

Main report

- 3.1 The Statement of Investment Principles is formally reviewed annually whether there are policy changes or not. It has been reviewed and the investment management benchmarks, objectives and structures of the Funds updated. There are no other material changes.

Measures of success

- 4.1 Success of the investment strategies will, among other things, be measured by the achievement of the investment and funding objectives of the Funds.

Financial impact

- 5.1 There are no direct financial implications as a result of this report.

Risk, policy, compliance and governance impact

- 6.1 The Statement of Investment Principles details how the risks, compliance and governance aspects of the Funds are managed. Such a statement is required under the Local Government Pension Scheme Regulations. Appendix C of the Statement illustrates compliance with the CIPFA principles.

Equalities impact

7.1 There are no equalities implications as a result of this report.

Sustainability impact

8.1 The Statement sets out the Funds' approach to responsible ownership and details how voting, engagement and other Environmental, Social and Governance activity will be undertaken. Compliance with the Statement is expected to contribute to the sustainability of the Funds' investments.

Consultation and engagement

9.1 The Consultative Panel for the Funds, comprising member and employer representatives, is integral to governance. The Statement is published on the Funds' website.

Background reading / external references

None

Alastair Maclean

Director of Corporate Governance

Contact: Bruce Miller, Investment Manager

E-mail: Bruce.Miller@edinburgh.gov.uk | Tel: 0131 469 3866

Links

Coalition pledges

Council outcomes CO26 – The Council engages with stakeholders and works in partnerships to improve services and deliver agreed objectives.

Single Outcome Agreement

Appendices

Appendix 1 - Statement of Investment Principles including:
Appendix A – Investment Strategy
Appendix B – Statement of Compliance with UK Stewardship Code
Appendix C – Lothian Pension Funds' Compliance with the CIPFA Principles for Investment Decision Making in the Local Government Pension Scheme

LOTHIAN PENSION FUND, LOTHIAN BUSES PENSION FUND and SCOTTISH HOMES PENSION FUND ('the Funds')

STATEMENT OF INVESTMENT PRINCIPLES (June 2014)

1. Introduction

- 1.1 This Statement of Investment Principles was agreed by the Pensions Committee of the City of Edinburgh Council on 17 June 2014.
- 1.2 The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 require administering authorities to prepare, maintain and publish a written Statement of Investment Principles (SIP). The SIP must be reviewed from time to time in accordance with any material changes in the Policy. In preparing this statement, the Committee has taken professional advice from the Investment Strategy Panel, which includes external advisers.

2. Governance

- 2.1 The City of Edinburgh Council (CEC) is the administering authority for the Lothian Pension Fund, the Lothian Buses Pension Fund and Scottish Homes Pension Fund.
- 2.2 The Pensions Committee ("the Committee") of the City of Edinburgh Council has delegated responsibility for the supervision of the Funds.
- 2.3 This SIP sets out the principles governing decisions about the investments of the Funds. The Committee recognises the importance of corporate governance and corporate responsibility in ensuring the long term financial performance of the companies in which they invest.
- 2.4 The SIP forms part of a framework that includes
 - The Statutory Regulations
 - The Pensions Committee
 - The Investment Strategy Panel
 - The Lothian Pension Funds' Consultative Panel
 - The Funds' Advisors
 - The Funds' Funding Strategy Statement.

3. Investment Objectives & Benchmarks

- 3.1 The primary aim of the Funds is to ensure that all members and their dependants receive their benefits when they become payable.
- 3.2 The funding objectives are documented in the Committee's Funding Strategy Statement. The primary funding objectives are:
- to ensure the long-term solvency of the Funds and that of sub funds
 - to minimise the degree of short-term change in employer contribution rates
 - to maximise the returns from investments within reasonable 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
 - where practical and cost effective, to make allowance for the different characteristics of different employers and groups of employers.
- 3.3 The Funds seek to control risk through investing in a diverse range of investments. The Pensions Committee sets an investment strategy for each Fund, taking into account the funding status and liabilities. The strategies are subject to regular review. Details of each Fund's strategic asset allocation are provided in Appendix A.
- 3.4 The Funds' focus within the strategic asset allocation is on risk, income and capital protection. The Funds are assessed relative to a benchmark, but success is also measured in terms of the level and growth of income and the volatility of absolute performance.
- 3.5 The investment objectives of the Funds are to achieve the same return as the benchmark over the long term economic cycle (typically five years or more). Over shorter periods, the Funds should perform better than the benchmark if markets fall significantly.
- 3.6 It is recognised that within Lothian Pension Fund, employers' circumstances vary and there may be demand from individual employers for a lower-risk investment strategy for their section of the Fund. The Fund will consider such requests subject to practical implementation of such strategies and if appropriate, a review of employer contribution rates. It is not practical for the Fund to offer individual employers full flexibility on asset allocation.

4. Investment Management Structure

- 4.1 The Funds employ a combination of managers with the aim of delivering, in aggregate, the objectives of each Fund. Each Fund employs different types of managers depending on the requirements of the Fund.

- 4.2 To reduce the risk that a Fund does not deliver its objective, performance and risk targets and controls are set for each manager relative to their benchmark. The details are included in formal fixed term Investment Management Agreements. In addition, managers and their performance are monitored on a regular basis.
- 4.3 The investment managers are responsible for the selection of individual holdings within each type of investment category within the parameters set out in their agreement.
- 4.4 The selection of investment managers complies fully with European Union directives on competitive tendering.
- 4.5 Specialist transition managers are employed to manage complex changes in investment strategy and/or manager(s).
- 4.6 Details of the Funds' investment managers are provided in Appendix A.

5. Underlying Investments

Types of Investment

- 5.1 The Committee has approved the use of the following different types of investment and income generating mechanisms to achieve their overall investment objectives:
- Listed and Unlisted Equities (including Managed Funds, Unit Trusts, Investment Trusts, Open Ended Investment Companies and Exchange Traded Funds),
 - Bonds including index-linked and fixed interest bonds, issued by both government and corporations;
 - Alternative investments (including Infrastructure, Property, Timber, Agriculture, Currency and other asset classes as agreed by the Investment Strategy Panel),
 - Cash (including Treasury Bills and Money Market Funds),
 - Derivatives,
 - Stock lending,
 - Commission recapture,
 - Underwriting.

The Balance Between Different Types of Investments & Risks

- 5.2 The Funds seek to control risk through investing in a diverse range of investments. The Pensions Committee sets investment strategy for each Fund, taking into account the funding status and liabilities. The strategies are subject to regular review.
- 5.3 Asset liability modelling techniques, which measure the risk of the Fund relative to the liabilities, are used to assist in the strategy reviews, as appropriate.
- 5.4 The risk of the Funds performing differently to their benchmarks is monitored using an independent performance and risk specialist. The internal investment team and the Investment Strategy Panel monitor risks on a quarterly basis.

Expected return on investments

- 5.5 Each Fund expects its investments to produce a return over the long term above that of the investment return assumed in the actuarial valuation.

Realisation of investments

- 5.6 The majority of each Fund's investments are quoted on major stock markets and may be realised relatively quickly if required. A proportion of each Fund's investments (such as property, private equity and infrastructure) would take longer to be realised. The overall liquidity of each Fund's assets is considered in the light of potential demands for cash.

Stock Lending

- 5.7 Lothian Pension Fund and Lothian Buses Pension Fund lend a proportion of their investments in order to maximise additional income. Stock lending is conducted within the parameters prescribed in the regulations. Stock lending does not prevent any investments from being sold. Safeguards are in place to reduce the risk of financial loss in the event of default. These safeguards include receiving liquid collateral in excess of the value of the loan, indemnity agreement with the lending agent and regular reviews of credit-worthiness of potential borrowers.

Responsible Investment

- 5.8 The Pensions Committee believes that investing responsibly can affect the financial performance of companies. It has a responsibility to take environmental, social and governance issues seriously and where appropriate, to act upon them.
- 5.9 The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting high quality corporate governance and reporting.
- 5.10 The Funds seek to adhere to the FRC'S UK Stewardship Code, and encourage our appointed asset managers to do so too. Details of adherence to the Code are provided in Appendix B.

Safekeeping of Assets

- 5.11 The services of a global custodian are employed to ensure the safekeeping of investments.

Performance measurement

- 5.12 An independent provider is employed to calculate performance for the Funds. Each quarter, the Investment Strategy Panel considers the performance of the combined assets and each manager's portfolio against their respective benchmark. The Pensions Committee reviews performance on an annual basis.

6. Compliance

Regulations and Investment Limits

- 6.1 The Funds are compliant with the statutory restrictions set out in the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010.

The Regulations contain limits on the percentage of a pension fund that may be invested in certain asset types and provide for the limits to be raised, subject to certain requirements being met. The Committee resolved that the limits applicable to the Funds' investments in partnerships be raised in order to accommodate the strategic allocation to Alternative Investments, including infrastructure, and to Private Equity. The Committee decision was that:

- The limit in respect of all contributions into any single partnership be raised from 2% to 5%.
- The limit in respect of all contributions into partnerships be raised from 5% to 15%.

The Committee took proper advice in respect of this decision from the Investment Strategy Panel and from officers. This decision will apply for the period for which the Funds' strategic investment benchmarks include allocations to investments which involve investment in partnerships, unless investment considerations require an earlier review. This decision is compliant with the Regulations.

CIPFA Principles for Investment Decision Making in the Local Government Pension Scheme

- 6.2 Regulations require administering authorities to publish the extent to which they comply with guidance issued by the Scottish Ministers, which in turn refer to guidance issued by Chartered Institute of Public Finance and Accountancy. The Funds' compliance with the guidance is provided in Appendix C.

7. Review

- 7.1 The Pensions Committee will review this statement annually or more frequently if appropriate. The Committee will consult with such persons as it considers appropriate and take proper advice when revising the statement.

Lothian Pension Fund

Investment Strategy

	Benchmark from 31/03/14 (%)	Strategy 2012-2017 (%) [1]	Permitted Range % [1]
Listed Equities	64	60	
Private Equity	6	5	
Total Equities	70	65	50 – 75
Inflation linked Assets	5	7	0 – 20
Alternatives	24	28	20 – 35
Cash	1	0	0 – 10
TOTAL	100	100	

[1] Revised benchmark agreed by Committee October 2012 which will be implemented gradually over time.

Investment Management Structure at 30 April 2014

- 5 Global Equity Managers (external: Nordea, Cantillon, Harris; internal: 2 mandates), 8 Regional Equity Managers (external: Baillie Gifford, Invesco, Mondrian and UBS; internal: UK All Cap, UK Mid Cap, US and Europe ex-UK)
- Private equity investments in a range of direct funds, fund-of-funds and listed vehicles, some of which are managed internally.
- 1 Bond Manager (Internal)
- Alternative Investments include a range of direct funds, fund-of-funds and listed vehicles invested in infrastructure, secured loans, property and timber, some of which are managed internally.
- 1 Currency Manager (internal)
- Cash (Internal)

APPENDIX A

Lothian Buses Pension Fund

Investment Strategy

	Benchmark at 31/03/14 (%)	Strategy 2012-2017(%) [1]	Range within asset class (%)
Equities			
Listed Global Equities	62.5	55	
Private Equity	0.0		
Subtotal	62.5	55	45-65
Bonds			
Index Linked Gilts	10.0	15	10-30
Subtotal	10.0	15	
Alternative Investments			
Property	10.0		
Other, including corporate bonds	17.5	30	
Subtotal	27.5	30	10-35
Cash	-	-	0-10
TOTAL	100.0	100	

[1] Revised Strategy agreed by Committee in October 2012. The revised strategy will be implemented gradually.

Investment Management Structure at 30 April 2014

- Global equities: internal and Baillie Gifford
- Listed Private equity: internal
- Index linked Gilts: internal and Baillie Gifford
- Corporate bonds: Baillie Gifford
- Property: Standard Life
- Alternative Investments: internal and include secured loans, timber and infrastructure managed via a range of listed vehicles, direct funds and fund-of-funds.
- Cash (Internal)

APPENDIX A

Scottish Homes Pension Fund

Investment Strategy

	Strategic Benchmark at 01/04/2014 %	Strategy for 2012-2017 [1] %	Range for 2012-2017 [1] %
Equities			
UK	6.6	30	20-35
US	9.3		
Europe (ex UK)	6.0		
Pacific inc Japan	5.7		
Emerging markets	2.4		
Sub-total	30.0		
Bonds			
UK Fixed Interest Gilts	13.0	65	60-75
UK Index Linked Gilts	52.0		
Subtotal	65.0		
Property	5.0	5	5-10
Cash	0.0	0	0-5
TOTAL	100.0	100	100

[1] Agreed by Committee October 2012

Investment Manager Arrangements at 30 April 2014

Equities and bonds: State Street.
Property: Schroders.

Statement of Compliance with UK Stewardship Code

<p>Principle 1 Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.</p>	<p>We acknowledge our role as an asset owner under the Stewardship Code and therefore seek to hold to account our fund managers and service providers in respect of their commitments to the Code.</p> <p>In practice our policy is to apply the Code through</p> <p>a) The appointment of Hermes Equity Ownership Services (EOS) to assist in fulfilling our fiduciary responsibilities as long term shareholders. We believe that the monitoring of shareholdings by Hermes EOS enables us to provide the highest standards of stewardship on behalf of the beneficiaries of the pension funds.</p> <p>Hermes EOS has the expertise in corporate engagement to carry forward this work on an international basis. Their aim is to bring about positive long-term change at companies through a focussed and value-oriented approach.</p> <p>Engagements undertaken by Hermes EOS on our behalf are guided by the Hermes Responsible Ownership Principles http://www.hermes.co.uk/Portals/8/The_Hermes_Ownership_Principles_UK.pdf</p> <p>Besides engagement on an individual company level, through Hermes EOS, we also work to establish effective regulatory regimes in the various markets in which we invest to encourage governance structures that facilitate accountability of companies to their owners, give companies the certainty they need to plan for the future and to level the playing field to ensure companies are not disadvantaged for prioritising long-term profitability.</p> <p>b) As well as Hermes EOS, three of our Fund Managers, Baillie Gifford, State Street and UBS, take direct responsibility for stewardship issues, voting and engagement, in the funds which they manage on our behalf. These managers publish Statements of Compliance with the Stewardship code.</p> <p>Details are available on their websites at</p> <p>www.bailliegifford.com/pages/UKInstitutional/CorporateGovernance/CorporateGovernanceSRI.aspx</p> <p>http://www.ubs.com/global/en/asset_management/responsible_investment.html</p> <p>http://www.ssga.com/webapp/features/proxy_voting_policy.jsp?country=GB&language=EN</p> <p>c) Through our membership of the Local Authority Pension Fund Forum (LAPFF), we keep informed of potential issues of concern at both individual companies and across the market as a whole, which leads to collaborative engagement.</p>
------------------------------------------------------------------------------------------------------------------------------------------------------------	------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------

Statement of Compliance with UK Stewardship Code

<p>Principle 2 Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.</p>	<p>Our relationship with Hermes EOS enables us effectively to manage conflicts of interest in relation to our stewardship work. Hermes EOS conflicts of interest policy, which explains how it manages conflicts on our behalf, can be found at http://hermes.yellowtailcms.co.uk/Portals/8/Conflicts_of_interest_policy.pdf.</p> <p>We also encourage the asset managers employed by the Funds to have effective policies addressing potential conflicts of interest.</p> <p>In respect of conflicts of interest within the Funds, Pensions Committee members are required to make declarations of interest prior to Committee meetings.</p> <p>Our policy of constructive engagement with companies is consistent with the Funds' fiduciary responsibilities.</p>
<p>Principle 3 Institutional investors should monitor their investee companies.</p>	<p>Day-to-day responsibility for monitoring our equity holdings is delegated to Hermes EOS, Baillie Gifford, State Street and UBS. We expect them to monitor companies, intervene where necessary, and report back regularly on activity. Details are provided quarterly on the Funds' website. This includes both the total number of company meetings where the Funds have voted and details of individual companies where we have voted against company management.</p> <p>LAPFF also monitors and engages with companies and provides an 'Alerts' service which highlights concerns over corporate governance issues.</p> <p>The internal investment management team adhere to the Funds' compliance policy on insider information. In order to foster a positive working relationship with an individual company and to build trust, Hermes EOS may be willing to become an insider. In such circumstances, the relevant information will not be passed to the internal team until after it is no longer inside information.</p>

Statement of Compliance with UK Stewardship Code

<p>Principle 4 Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.</p>	<p>As highlighted above, responsibility for day-to-day interaction with companies is delegated, including the escalation of engagement when necessary.</p> <p>We expect the approach to engagement on our behalf to be value orientated and focussed on long term sustainable profitability. We expect Hermes EOS, Baillie Gifford, State Street and UBS to disclose their guidelines for such activities in their own statements of adherence to the Code.</p> <p>We may also propose escalation of activity through the Local Authority Pension Fund Forum.</p> <p>Consistent with our fiduciary duty to beneficiaries, we also participate in shareholder litigation. We pursue compensation for any losses sustained because of inappropriate actions by company directors in order to encourage improved conduct in the future.</p>
<p>Principle 5 Institutional investors should be willing to act collectively with other investors where appropriate</p>	<p>We seek to work collaboratively with other institutional shareholders in order to maximise the influence that we can have on individual companies. We do this through:</p> <ul style="list-style-type: none"> - membership of the Local Authority Pension Fund Forum, which engages with companies over environmental, social and governance issues on behalf of its members. - the appointment of Hermes EOS also signals our commitment to the benefits of collective shareholder engagement. Hermes EOS pools together investors' resources to create an engagement service which aims to protect and enhance shareholder value. Hermes EOS represents us at many national, regional and global organisations through which we seek to enhance our effectiveness by working collaboratively with other institutions. Among these are: the UNPRI and its Clearinghouse for engagements (as well as a number of more localised UNPRI initiatives); the International Corporate Governance Network; the Asian Corporate Governance Association; the Canadian Coalition for Good Governance , Eumedion and the NAPF's Shareholders Advisory Group. Hermes EOS seeks to work with these organisations and also alongside other individual investors to effect change most efficiently. - being a signatory of the UN Principles for Responsible Investment (PRI) in our own right. - being a signatory since 2009 to the Carbon Disclosure Project (CDP) Information Request. The information gathered by CDP forms the largest database of corporate climate change information in the world.

Statement of Compliance with UK Stewardship Code

<p>Principle 6 Institutional investors should have a clear policy on voting and disclosure of voting activity.</p>	<p>The emphasis of our voting policy is to promote best practice. We seek to vote on all shares held. The Funds have an active stock lending programme but consider recalling stock from a loan where it appears that this would be an appropriate way to safeguard the Funds' financial interests.</p> <p>Our preference is for managers to vote on the Funds' behalf and for responsible stewardship to be integral to the investment decision making process.</p> <p>We are comfortable with delegation of voting to Baillie Gifford and UBS for the funds they manage. State Street vote on our behalf because the investment is in a pooled fund. The managers' voting policies can be found at the websites mentioned above.</p> <p>For the remaining funds, Hermes EOS votes consistently, across the portfolios it covers, and makes voting decisions based on a thorough analysis of publicly available information and always take account of a company's individual circumstances. Hermes EOS informs companies where it has concerns and seeks a resolution prior to taking the decision to vote against management. In this way, it uses our votes as a lever for positive change at companies.</p> <p>Underpinning voting decisions are Hermes EOS Regional Corporate Governance policies which can be found at the "How we invest" section of our website.</p> <p>We disclose our historic voting information on our website. This includes the total number of companies where the Funds voted and details of individual companies where we have voted against company management.</p> <p>We disclose in arrears so that we are transparent and accountable but dialogue with companies in our portfolios is not compromised.</p>
<p>Principle 7 Institutional investors should report periodically on their stewardship and voting activities.</p>	<p>We report annually on stewardship activity through a specific section in the Funds' annual report and accounts and on our website.</p> <p>We also report annually on stewardship issues to the Pensions Committee.</p> <p>We have reviewed this Statement in June 2014. We will review the Statement annually.</p>
	<p>For further information please contact Marlyn.McConaghie@edinburgh.gov.uk</p>

Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund (the Funds), Compliance with the CIPFA Principles for Investment Decision Making in the Local Government Pension Scheme.

The Funds comply with the six CIPFA Principles. Details of the principles and the Funds' compliance are described below.

Principle 1 – Effective decision making

Administering authorities should ensure that decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to take them effectively and monitor their implementation; and Those persons or organisations should have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.

- The Funds' Trustee Training Policy (comprising a compulsory training seminar for all new trustees and ongoing training of at least three days per year for all Committee Members) provides Committee members with sufficient knowledge to be able to evaluate and challenge the advice they receive. All committee members have met the pro rata minimum requirement for training during the reporting period, 1 April 2013 to 31 March 2014.
- Standards relating to the administration of the Committee's business are strictly up-held.
- The Pensions Committee focuses on setting the strategy for the Funds and monitoring performance. The Committee delegates the day-to-day running of the Funds to the Director of Corporate Governance.
- The Director of Corporate Governance is responsible for the provision of the training plan for Committee to help them to make effective decisions to ensure that they are fully aware of their statutory and fiduciary responsibilities, and to regularly remind them of their stewardship role.
- The Investment Strategy Panel oversees the Funds' investments. This includes implementing the agreed strategies, reviewing structure, funding monitoring, performance and risk and tactical asset allocation. The Investment Strategy Panel meets quarterly and is made up of experienced investment professionals, including independent advisers.
- The in-house team undertakes day-to-day monitoring of the Funds. The team includes personnel with suitable professional qualifications and experience to provide the necessary skills, knowledge, advice and resources to support the Investment Strategy Panel and the Pensions Committee.

- Conflicts of interest are managed actively. At each Committee meeting, elected members (acting as ‘trustees’ of the Funds) are asked to highlight conflicts of interest. The Lothian Pension Funds’ Consultative Panel, which includes representative members and employers, attend Committee meetings. Committee take into account the Consultative Panel’s views when making decisions. A Code of Conduct applies to members of the Committee and Consultative Panel.
- The Funds have a Compliance Policy which ensures conflicts of interest are highlighted and managed appropriately.

Principle 2 – Clear Objectives

Overall investment objectives should be set out for the fund that take account of the scheme’s liabilities, the potential impact on local council tax payers, the strength of the covenant of the participating employers, and the attitude to risk of both the administering authority and the scheme employers, and these should be clearly communicated to advisers and investment managers.

- The Statement of Investment Principles and the Funding Strategy Statement define the Funds’ primary funding objectives.
- Asset-liability modelling is undertaken with the help of external advisers to aid the setting of investment strategy in order to understand risks. Each Fund has a scheme-specific investment strategy.
- The attitude to risk of employers and the administering authority is specifically taken into account in the setting of strategy.
- Reviews of investment strategy focus on the split between broad asset classes (equities, bonds and alternative investments).
- Investment Management Agreements set clear benchmarks and risk parameters to achieve and include the requirement to comply with the Funds’ Statement of Investment Principles.
- Appointments of advisers are reviewed regularly. Investment and actuarial advisers are appointed under separate contract. Procurement of advisers is conducted within European Union procurement regulations.
- The setting of the Funding Strategy included specific consideration of the need to maintain stability in employer contribution rates.

Principle 3 – Risk and liabilities

In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of liabilities.

These include the implications for council tax payers; the strength of the covenant of participating authorities; the risk of their default, and longevity risk.

- The Funds take advice from the scheme's actuary regarding the nature of its liabilities. Asset-liability modelling is undertaken periodically to aid the setting of investment strategy, and these exercises specifically take account of covenant strength and longevity risk.
- It is recognised that within Lothian Pension Fund, employers' circumstances vary and there may be demand from individual employers for a lower-risk investment strategy for their section of the Fund. The Fund will consider such requests subject to practical implementation of such strategies and if appropriate, a review of employer contribution rates. It is not practical for the Fund to offer individual employers full flexibility on asset allocation.
- The Funding objectives for the Funds are expressed in relation to the solvency and employer contribution rates. The Funds regularly assesses the covenants of the Funds' participating employers.
- The Director of Corporate Governance is responsible for ensuring appropriate controls of the Funds. Controls are subject to internal audit and results of audits are submitted to the Pensions Audit Sub Committee and/or the Pensions Committee.
- The Funds maintain a risk register which is reviewed on a quarterly basis.

Principle 4 – Performance assessment

Arrangements should be in place for the formal measurement of the performance of the investments, investment managers and advisers.

Administering authorities should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.

- The Funds' performance and risk analysis is produced by an independent external provider.
- The internal investment team and Investment Strategy Panel assess Fund Managers' performance on a regular basis.
- The Funds' contracts with its advisers are regularly market tested.
- The Investment Strategy Panel assesses its own performance on a regular basis, typically annually.

- Training and attendance of members of the Pensions Committee and the Consultative Panel are monitored and reported on a regular basis. The composition of the Committee and Consultative Panel is reviewed on a regular basis.

Principle 5 – Responsible ownership

Administering authorities should adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee Statement of Principles on the responsibilities of shareholders and agents.

A statement of the authority's policy on responsible ownership should be included in the Statement of Investment Principles.

Administering authorities should report periodically to members on the discharge of such responsibilities.

- The Funds' policy on responsible ownership is included in the statement on the FRC's Stewardship Code (see Appendix B of the Statement of Investment Principles).
- Details of the Funds' voting and engagements are available on the Funds' website. The Funds' annual report and accounts includes a summary of the Funds' approach to responsible investment. A summary of the report and accounts is sent to members. The full report is available on the website and is sent to members on request.

Principle 6 – Transparency and reporting

Administering authorities should act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives; and Provide regular communication to members in the form they consider most appropriate.

- Meetings of the Pensions Committee are open to the public. Members of the public are allowed to provide deputation at Committee meetings. All Committee papers are available on the City of Edinburgh Council's website. The Lothian Pension Funds' Consultative Panel, which includes representatives from all major stakeholders, joins the Committee at all meetings.
- The Committee's remit covers wider pension scheme issues, other than the management and investment of funds.
- The Funds' policy statements, including the Communications Strategy, Statement of Investment Principles and Funding Strategy Statement are maintained regularly. Stakeholders are consulted on changes. Documents are available on the Funds' website.
- The Funds produce an Annual Report & Accounts, a summary of which is sent to members. The full report is available on the website, and is sent to members on request.
- The Funds also produce regular newsletters for members as well as an annual benefit statement. Regular briefings are also provided to employers. The Funds' website is updated regularly.