Notice of meeting and agenda

Pensions Committee

2.30pm, Wednesday 17 December 2014

Dunedin Room, City Chambers, High Street, Edinburgh

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

Contact

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1. Order of business

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

2. Declaration of interests

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

3. Deputations

3.1 None

4. Minute

4.1 Previous Minute 23 September 2014 – Submitted for approval as a correct record (circulated)

5. Reports

5.1 Referrals and recommendations from Audit Sub-Committee – verbal update from Convener of the Sub-Committee.

5.2 Agenda Planning – report by the Director of Corporate Governance (circulated)

5.3 Consultative Panel and Pensions Committee Membership - report by the Director of Corporate Governance (circulated)

5.4 Report by External Auditor on the Annual Report 2014 of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund - report by the Director of Corporate Governance (circulated)

5.5 New Scheme Update (Governance) - report by the Director of Corporate Governance (circulated)

5.6 Reform of the Local Government Pension Scheme in Scotland and Regulatory Update (excluding Governance) - report by the Director of Corporate Governance (circulated)

5.7 Pensions Fund Cost Benchmarking - report by the Director of Corporate Governance (circulated)

5.8 Scottish Homes Pension Fund – 2014 Actuarial Valuation and Investment Strategy - report by the Director of Corporate Governance (circulated)

5.9 EU Tax Claims - report by the Director of Corporate Governance (circulated)

5.10 Environmental Social and Governance Activity Update – report by the Director of Corporate Governance (circulated)

5.11 Class Actions – report by the Director of Corporate Governance (circulated)

5.12 Service Plan Update 2014 – 2017 – report by the Director of Corporate Governance (circulated)

5.13 Risk Management – report by the Director of Corporate Governance (circulated)

6. Motions

6.1 If any

Carol Campbell

Head of Legal, Risk and Compliance

Committee Members

Councillor Rankin (Convener), Councillor Child, Councillor Bill Cook, Councillor Orr and Councillor Rose, John Anzani and Darren May.

Information about the Pensions Committee

The Pensions Committee consists of 5 Councillors and 2 external members and is appointed by the City of Edinburgh Council. The Pensions Committee usually meets every eight weeks.

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

Further information

If you have any questions about the agenda or meeting arrangements, please contact Gavin King, Committee Services, City of Edinburgh Council, City Chambers, High Street, Edinburgh EH1 1YJ, Tel 0131 529 4239, e-mail gavin.king@edinburgh.gov.uk.

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

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

Minutes

Pensions Committee

2.30pm, Tuesday 23 September 2014

Present

Councillor Rankin (Convener), John Anzani, Councillor Child, Councillor Cook, Councillor Orr and Councillor Rose (Chair for items 9-12).

Consultative Panel Members Present:

Charlie Boyd, Helen Carter, Eric MacLennan, Owen Murdoch and John Rodgers

1. Minutes

Decision

To approve the minute of the Pensions Committee of 17 June 2014 as a correct record.

2. Referrals and Recommendations from the Audit Sub-Committee

Councillor Rose advised the Committee of the discussion and decisions taken at the Pensions Audit Sub-Committee the previous day.

Decision

To note the update.

(Reference – Pensions Audit Sub-Committee, 22 September 2014.)

3. Agenda Planning

An indication was provided of potential reports for future Pensions Committee and Pensions Audit Sub-Committee meetings in December 2014 and March 2015.

Decision

To note the report.

(Reference – report by the Director of Corporate Governance, submitted.)

4. Audited Annual Report 2014 of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

Details were provided on the Annual Report for the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund which had now been considered by Audit Scotland.

Decision

1) To note the External Auditor's report on the audit of the Annual Report for the year end 31 March 2014 for the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund.

2) To note the Audited Annual Report 2014 for the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.

(Reference – report by the Director of Corporate Governance, submitted.)

5. Review of Investment Options

A summary was provided on the key matters in relation to the investment controls and development of the in-house investment operations. There had been significant progress in reviewing and implementing the recommendations of the external consultant following their review of the in-house investment operations in December 2013. The Fund was also pursuing Financial Conduct Authority authorisation in order to strengthen internal controls and facilitate further development of the in-house investment function.

Decision

To note the progress in implementing the recommendations of the external consultant and in seeking Financial Conduct Authority (FCA) authorisation.

(Reference – report by the Director of Corporate Governance, submitted.)

6. Pensions Fund Investment Staffing

The risk from the lack of remuneration benchmarking and short notice periods for investment staff was highlighted and potential options to manage the risk were outlined. Approval was sought to create a special purpose vehicle to employ certain staff.

Decision

1) To agree option 4 in principle as outlined in the Director of Corporate Governance's report, subject to Council approval, to set up a special purpose vehicle.

2) To recommend to Council that a special purpose vehicle, separate to the Council, is created to employ certain pension fund investment staff.

3) To note that consultation with staff and trade unions would take place following any approval.

4) To recommend to the Council that the Convener of the Pensions Committee is appointed as a Board member of the special purpose vehicle.

5) To request the Director of Corporate Governance to report back to the Pensions Committee on progress including whether it is possible to include all the Pension and Investment staff in a phase two.

(Reference – report by the Director of Corporate Governance, submitted.)

7. Service Plan 2014 – 2017 Update

Details were provided on the first quarter of the 2014 –2017 Service Plan, performance indicators and the key actions to enable the Fund to meet its key objectives. Approval was sought for a contingency budget provision in the event that the investment management function could no longer be operated in-house.

Decision

1) To note the progress of the Fund against the 2014 – 2017 Service Plan.

2) To approve the provision of an annual contingency budget of £10 million for external investment fees to be used in the event of significant team departures.

(Reference – report by the Director of Corporate Governance, submitted.)

8. Chair

At this point in proceedings Councillor Rankin vacated the chair and Councillor Rose was appointed to chair the remainder of the meeting.

9. Update on Employers Participating in Lothian Pension Fund

An update was provided on employers who are currently looking to join the Fund, employers leaving the Fund and the review of the covenant with individual employees.

Decision

1) To note the changes to the employers participating in the Lothian Pension Fund.

2) To note the work being carried out to review the covenant of employers and its use in the 2014 actuarial valuation.

(Reference – report by the Director of Corporate Governance, submitted.)

10. Overpayment of Pension

Approval was sought to write-off an overpayment of pension amounting to £3,121.59.

Decision

Committee agreed not to pursue recovery of an overpayment of pension amounting to £3,121.59.

(Reference – report by the Director of Corporate Governance, submitted.)

11. Update on Reform of Local Government Pension Scheme in Scotland and Regulatory Update

An update was provided outlining the progress made towards implementation of a new Local Government Pension Scheme (LGPS) in Scotland and further regulations covering scheme governance that would follow over the coming months.

Decision

To note the regulatory update.

(Reference – report by the Director of Corporate Governance, submitted.)

12. Risk Management

A summary was provided on the Lothian Pensions Fund's risk management procedures, including details on the operational risk register and quarterly risk overview.

Decision

To note the report.

(Reference – report by the Director of Corporate Governance, submitted.)

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Agenda Planning

Item number	5.2
Report number	
Executive/routine	
Wards	All

Executive summary

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

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

Links

Coalition pledges	
Council outcomes	CO26 –The Council engages with stakeholders and works in partnership to improve services and deliver on agreed objectives.
Single Outcome Agreement	

Report

Agenda Planning

Recommendations

1.1 That Committee notes the agenda planning document.

Background

2.1 In order for the Pensions Committee and Consultative Panel to gain an overview of the content of the Committee Cycle it was agreed that an agenda planning document be submitted each quarter.

Main report

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

March 2015

The following papers are currently scheduled for the Pensions Committee meeting:

- Audit plans and reports (internal and external)
- Pension Fund Governance
- Funding Strategy Statement
- 2014 Actuarial Valuation for Lothian Pension Fund
- 2014 Actuarial Valuation for Lothian Buses Pension Fund
- 2014-17 Service Plan update
- 2015-18 Service Plan and Budget
- Policy Reviews (if any)
- Training Activity (Committee and Panel)
- Internal Investment Risks & Controls (progress in implementing recommendations from external assessment of controls, including FCA and staffing matters)
- Update on Employer Admissions in Lothian Pension Fund
- Risk management summary

3.2 It is proposed that the Pensions Audit Sub-Committee does not meet in March 2015. Audit plans for 2015/16 will be developed in consultation with the Convener of the Audit Sub-Committee before consideration by the Pensions Committee.

June 2015

The following papers are currently scheduled for the Pensions Audit Sub-Committee and Pensions Committee meeting in June 2015:

Pensions Committee	Audit Sub Committee
• Referrals/recommendations from the Pensions Audit-Sub Committee • Lothian Pension Fund Annual Report (& Accounts) Unaudited • Statement of Investment Principles • Investment Strategy Panel Activity • Annual Investment and Funding Update – LPF/LBPF/SHPF • Risk management summary	• Lothian Pension Fund Annual Report (& Accounts) Unaudited • Risk management summary

Measures of success

4.1 The Committee and Consultative Panel will have greater clarity regarding the content of the Committee Cycle.

Financial impact

5.1 None.

Risk, policy, compliance and governance impact

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

Equalities impact

7.1 None.

Sustainability impact

8.1 None.

Consultation and engagement

9.1 The Consultative Panel for the Funds, comprising member and employer representatives, is integral to governance.

Background reading / external references

None.

Alastair Maclean

Director of Corporate Governance

Struan Fairbairn, Legal & Risk Manager

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Links

Coalition pledges	
Council outcomes	CO26 –The Council engages with stakeholders and works in partnership to improve services and deliver on agreed objectives.
Single Outcome Agreement	
Appendices	Appendix 1 - Agenda planning appendix.

Frequency	Pensions Committee	Audit Sub Committee	Month
Annually	Audit plans and reports (internal and external)	N/A - Draft audits and plan will be developed in consultation with the Convenor of the Audit Sub Committee.	March
	Service Plan and Budget	N/A	March
	Policies/Strategies/Training	N/A	March
	LPF Annual Report (& Accounts) **Unaudited**	LPF Annual Report & Accounts (**Unaudited**)	June
	Statement of Investment Principles	N/A	June
	Investment Strategy Panel Activity	N/A	June
	Annual Investment and funding – LPF/LBPF/SHPF	N/A	June
	LPF Annual Report & Accounts **Audited**	LPF Annual Report & Accounts (**Audited**)	September
	ISA 260 Audit Report	ISA 260 Audit Report	September
	N/A	Pensions Data Quality	September
	N/A	Delegated authorities: Write offs -	September
	N/A	Fraud Prevention	September
	Annual Performance & Benchmarking	N/A	September
	N/A	Audit of Foreign Exchange Transaction Costs	September
	Consultative Panel Membership	N/A	December
	Annual Report by External Auditor	Annual Report by External Auditor	December
	EU Tax Claims & Income Recovery	EU Tax Claims & Income Recovery	December
	Class Actions	Class Actions	December
	N/A	Investment Income Review-Cross-Border withholding tax	December
	Environmental Social and Governance Activity	N/A	December
	N/A	Investment Controls & Compliance	December

Frequency	Pensions Committee	Audit Sub Committee	Month
Semi Annually	Update on Employer Admissions in LPF	N/A	March & September
3 Times per year	Service Plan Update	N/A	March, September & December
	Referrals / recommendations from Pensions Audit-Sub	N/A	June, September & December
Quarterly	Risk management summary	Risk management summary	March, June, September and December
Every 3 years	Actuarial Valuation: LPF/LBPF/SHPF Funding Strategy Statement		December or March
As required	Delegated authorities (provider appointments)	N/A	
	Discretions (death grants etc.)	Audit reports	
	N/A	Internal Audit Reports	
	Regulatory Update	N/A	
	Investment Strategy Reviews (at least every 3 years)	N/A	
	N/A	Risk management (in depth review)	

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Consultative Panel and Pensions Committee Membership

Item number	5.3
Report number	
Executive/routine	
Wards	All

Executive summary

The purpose of this report is to provide the Committee with an update on the Consultative Panel members who have been appointed to Committee and to note that the current appointments are extended until the Local Government Pension regulations change on 1st April 2015.

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	

Report

Consultative Panel and Pensions Committee Membership

Recommendations

1.1 Committee is requested to note the extension of the appointment of the two current external members, John Anzani and Darren May, to the Pensions Committee until 1st April 2015.

Background

2.1 The two appointments from the Consultative Panel to the Pensions Committee are reviewed annually. Two Consultative Panel members were appointed to the Pension Committee in December 2013, John Anzani and Darren May and these positions are now due to be reviewed.

Main report

3.1 The purpose of this report is to provide the Committee with an update on the Consultative Panel members who have been appointed to the Pension Committee and recommend that the current arrangements be extended until March 2015.

3.2 The change of Local Government Pension Scheme governance regulations has meant that as from 1st April 2015 the Lothian Pension Fund's governance will change and the Consultative Panel will cease to exist. This is covered elsewhere on the Committee's agenda.

3.3 Instead of nominating members to the Committee in November 2014, the Consultative Panel have agreed that the current appointments should be extended while the new governance arrangements are put in place.

3.4 The current members who are appointed to the Pension Committee, John Anzani and Darren May are willing to continue in their role until the changes to governance arrangements are made.

Measures of success

4.1 The Lothian Pension Fund continues to be a top performing fund by ensuring effective governance of the scheme.

Financial impact

5.1 None.

Risk, policy, compliance and governance impact

6.1 Current governance arrangements will remain in place while changes to the Lothian Pension Fund's governance are made to comply with the 2015 Local Government Pension Scheme regulations. Because current appointments will be extended a report will not needed to be considered at Council. External appointments to the Pensions Committee will be revisited in the coming months.

Equalities impact

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

Sustainability impact

8.1 An effective Consultative Panel and the appointments to the Committee should ensure the governance arrangements reflect the interests of pension fund stakeholders.

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading / external references

None

Alastair Maclean

Director of Corporate Governance

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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	

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Report by the External Auditor on the Annual Report 2014 of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

Item number	5.4
Report number	
Executive/routine	
Wards	All

Executive summary

This report presents the External Auditor's Annual Report on the 2013/14 audit of the Lothian Pension Funds. The report from Audit Scotland is shown at Appendix 1. This includes commentary from the Investment & Pensions Service Manager as to planned management actions. The report will be presented to Committee by Stephen O'Hagan, Senior Audit Manager, Audit Scotland.

Audit Scotland has already provided "an unqualified opinion that the financial statements (of the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund) give a true and fair view of the transactions of the funds during the year ended 31 March 2014, and of the amount and disposition at that date of their assets and liabilities".

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	

Report

Report by the External Auditor on the Annual Report 2014 of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

Recommendations

1.1 Committee is requested to:

- note the Annual Report on the 2013/14 audit of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund;
- note the Action Plan at Appendix II of the report and seek appropriate updates on progress;
- agree that the plans for internal and external audit are developed in consultation with the Convener of the Pensions Audit Sub-Committee prior to consideration by the Pensions Committee in March 2015;

Background

Unqualified audit opinion

2.1 Audit Scotland has already provided “an unqualified opinion that the financial statements (of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund) give a true and fair view of the transactions of the funds during the year ended 31 March 2014, and of the amount and disposition at that date of their assets and liabilities”.

Main report

Report on the 2013/14 audit by the External Auditor

3.1 The purpose of this report is to present the External Auditor’s Annual Report on the 2013/14 audit of the Lothian Pension Funds. The report from Audit Scotland is shown at Appendix 1. This includes commentary from the Investment & Pensions Manager as to planned management actions. The report will be presented to Committee by Stephen O’Hagan, Senior Audit Manager, Audit Scotland.

3.2 In addition to members of the Pensions Committee and Pensions Audit Sub-Committee, Audit Scotland has also sent the report to the Controller of Audit and has advised that the report will be published on its web-site in due course.

3.3 On pages 3 and 4 of the report, Audit Scotland has highlighted the financial position of Lothian Pension Fund at 31 March 2014, with 'net assets representing 80% of estimated promised retirement benefits'. It is important, however, to emphasise that a significant degree of caution should be applied to any assertion of funding level calculated on this basis. The figures are only prepared for the purposes of International Accounting Standard (IAS)26 and have no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes. Financial positions for the Lothian Buses Pension Fund and Scottish Homes Pension Fund have been derived using the same methodology. The 2014 actuarial valuation process will assess the funding positions, for the purposes of setting employer contribution rates.

3.4 The Fund will be preparing audit plans for internal and external audit work to be undertaken in the next financial year. It is proposed that these plans are developed in consultation with the Convener of the Pensions Audit Sub-Committee prior to consideration by the Pensions Committee in March 2015.

Measures of success

4.1 Planned management action in relation to the points raised by Audit Scotland is stated at Appendix II.

Financial impact

5.1 There are no financial implications arising directly from this report.

Risk, policy, compliance and governance impact

6.1 This annual report summarises the opinions and conclusions of Audit Scotland, in accordance with International Standards on Auditing (UK and Ireland) and the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011. Appendix I (of the Audit Scotland 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 II is an action plan setting out the high level risks identified from the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "Management action/response".

Equalities impact

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

Sustainability impact

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

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading / external references

Not applicable.

Alastair Maclean

Director of Corporate Governance

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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	Audit Scotland report on the 2013/14 audit of Lothian Pension Funds

Lothian Pension Funds

Annual report on the 2013/14 audit

Prepared for City of Edinburgh Council as administering body for Lothian Pension Funds and the Controller of Audit

October 2014

Contents

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Key messages

Financial statements	• We have given an unqualified opinion on the financial statements of Lothian Pension Funds for 2013/14.
Financial position	• Lothian Pension Fund (main fund) had net assets of £4,377 million at 31 March 2014. The actuarial value of estimated promised retirement benefits at 31 March 2014 was £5,483 million. • The net assets of the Lothian Buses and the Scottish Homes Pension Funds were £337 million and £136 million, respectively, at 31 March 2014. The actuarial value of estimated promised retirement benefits at 31 March 2014 for Buses and Homes were £358 million and £138 million, respectively.
Governance & accountability	• The Funds have effective governance arrangements that include a Pensions Committee and a Pensions Audit Sub-Committee. An Investment Strategy Panel provides advice to City of Edinburgh Council's Director of Corporate Governance who has delegated authority for implementing the Funds' investment strategy.
Best Value, use of resources & performance	• Investment performance for the Funds is measured against benchmarks which were agreed by the Pensions Committee in December 2012. For all 3 funds the return on investments for the 2013/14 financial year has met or exceeded these benchmarks.
Outlook	• The most significant area of risk for the Funds concerns investment returns. Although there was a resurgence of financial markets during the financial year, the longer term economic enviroment of weak growth and continuing European fiscal deficits, means that investment performance will be a key issue going forward.

Financial statements

We have given an unqualified audit opinion that the financial statements of the Lothian Pension Funds for 2013/14 give a true and fair view of the financial transactions of the funds during the year ended 31 March 2014, and of the amount and disposition at that date of their assets and liabilities.

Financial position – Funding

Lothian Pension Fund had net assets of £4,377 million as at 31 March 2014. The actuarial value of promised retirement benefits at 31 March 2014 has been estimated by the actuary as £5,483 million. This actuarial estimate would mean a net liability of £1,106 million as at 31 March 2014 (£1,366 million as at 31 March 2013), with net assets representing 80% of estimated promised retirement benefits.

The estimated liability prepared by the actuary is not a full actuarial statement but rather a figure prepared for the purposes of statutory accounting.

The Lothian Buses Pension Fund was closed to new members in 2008. As at 31 March 2014, the Fund had net assets of £337 million. The actuarial value of promised retirement benefits at the accounting date has been estimated by the actuary as £358 million. The actuarial estimate would mean a net liability of £21 million with net assets representing 94% of estimated promised retirement benefits.

As at 31 March 2014, the Scottish Homes Pension Fund had net assets of £136 million. The actuarial value of promised retirement benefits at the accounting date has been estimated by the actuary as £138 million. The actuarial estimate would mean a net liability of £2 million, with net assets representing 99% of estimated promised retirement benefits. There are no active members of the fund, while the Scottish Government acts as guarantor.

The actuary undertakes a triennial valuation on each fund to calculate funding levels, and this is used to set employer contribution rates. At the last triennial revaluations in 2011, the funding levels for the main Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund were 96%, 112% and 86% respectively. The 2014 triennial valuation is currently being prepared by the actuary and will be used to set contribution rates from April 2015.

Financial position – Administration

The Funds' actual expenditure compared to the approved budget disclosed an underspend of £0.959 million for the year to 31 March 2014, mainly due to an underspend of £0.381 million on investment managers fees.

Governance and accountability

The Funds have effective governance arrangements that include a Pensions Committee supported by a Pensions Audit Sub-

Committee and an advisory Consultative Panel with representatives from employers, pensioners and trade unions.

We also concluded that the Pension Funds have adequate internal controls (including internal audit) and satisfactory arrangements for the prevention and detection of fraud and corruption.

Best Value and performance

The performance of the Funds' investments is measured against benchmarks agreed by the Pensions Committee in 2012. Three different benchmarks were approved to accommodate the different asset types held by the Funds. For 2013/14 investment performance for Lothian Pension Fund was 1.6% ahead of the benchmark level (Lothian Buses was 3.8% ahead, Scottish Homes matched the benchmark). The longer term periods of assessment used by the Funds outperformed benchmark levels by a smaller margin for Lothian Pension Fund and Lothian Buses Pension Fund with Scottish Homes again matching the benchmark.

Outlook

Global financial markets have provided positive returns for investors in 2013/14, however sustaining this performance in the long term will be challenging. A combination of factors will likely impact on the performance of investments; fragile European public finances; the prospects of monetary policy tightening in the US and a loss of economic momentum, particularly in China where policy makers are grappling with high levels of credit. With investment performance key to the funding position of the LGPS, this may impact on employer contributions in the longer term.

The Public Services Pensions Act 2013 passed by UK parliament will mean changes to the way local government pension funds operate and pension benefits are accrued by members. Changes to meet the new Act are required to be implemented by 6 April 2015.

Parts of the changes mean that the accrual of benefits by members will now be provided for on a CARE (Career Averaged Revalued Earnings) basis. Member's benefits accrued after 1 April 2015 will be based on a fraction of their pensionable pay for every year they are a member of the LGPS. These changes will entail additional administrative and record keeping obligations being placed on employers and Lothian Pension Fund in determining member benefits. The Funds' pension administration system is being developed to address this challenge.

The triennial valuation at 31 March 2014 which will set the employer contribution rates for the next three years starting from 1 April 2015 will be finalised in early 2015. Lothian Pension Funds' expectation is that the monetary value of its deficit will have increased, driven by the low gilt yields serving to reduce the discount.

The implementation of the investment strategies 2012-2017 continue with the key focus of reducing risk primarily through changing the Funds' equity holdings, or reducing these and moving into index-linked assets and alternatives, where appropriate.

Introduction

1. This report is a summary of our findings arising from the 2013/14 audit of the Lothian Pension Funds. The purpose of the annual audit report is to summarise the auditor's opinions and conclusions, and to report any significant issues arising from the audit. The report is divided into sections which reflect our public sector audit model.

2. Our responsibility, as the external auditor of the Lothian Pension Funds, is to undertake our audit in accordance with International Standards on Auditing (UK and Ireland) and the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011.

3. The management of the Lothian Pension Funds is responsible for:

   - preparing financial statements which give a true and fair view
   - implementing appropriate internal control systems
   - putting in place proper arrangements for the conduct of its affairs
   - ensuring that the financial position is soundly based.

4. This report is addressed to the members of City of Edinburgh Council and the Controller of Audit and should form the basis of discussions with the Pensions Committee as soon as possible after it has been issued. Reports should be made available to stakeholders and the public, as audit is an essential element of accountability and the process of public reporting.

5. This report will be published on our website after it has been considered by the Pensions Committee. The information in this report may be used for the Accounts Commission's annual overview report on local authority audits. The overview report is published and presented to the Local Government and Regeneration Committee of the Scottish Parliament.

6. The concept of audit risk is of key importance to the audit process. During the planning stage of our audit we identified a number of key audit risks which involved the highest level of judgement and impact on the financial statements. We set out in our annual audit plan the related sources of assurance and the audit work we proposed to undertake to secure appropriate levels of assurance. Appendix I sets out the significant audit risks identified at the planning stage and how we addressed each risk in arriving at our opinion on the financial statements.

7. Appendix II is an action plan setting out the high level risks we have identified from the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "Management action/response".

8. We recognise that not all risks can be eliminated or even

minimised. What is important is that Lothian Pension Funds understands its risks and has arrangements in place to manage these risks. The Pension Funds and the Proper Officer should ensure that they are satisfied with proposed management action and have a mechanism in place to assess progress and monitor outcomes.

9. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures; consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.

Acknowledgement

10. The co-operation and assistance given to us by officers during the conduct of our audit is gratefully acknowledged.

Financial statements

Performance	Net Assets	Investments	Funding Level
Return on investments 6.8%	Increase in Net assets £282.9	Change in market value £171.4m	Value of promised retirement benefits £5,483m
Benchmark 5.2%	Net assets £4,377.5m	Investment Income £124.5m	Net asssets as a percentage of promised retirement benefits 80%

Source: Lothian Pension Funds Financial Statements – main fund data

Audit opinion

11. We have given an unqualified opinion that the financial statements of the Lothian Pension Funds for 2013/14 give a true and fair view of the financial transactions of the funds during the year ended 31 March 2014, and of the amount and disposition at that date of their assets and liabilities.

Other information published with the financial statements

12. Auditors review and report on other information published with the financial statements, including the sections titled Review of the Year, How the Fund Works, Investments and Financial Performance, the Annual Governance Statement and the Governance Compliance Statement. We have nothing to report in respect of these statements.

Legality

13. Through our planned audit work we consider the legality of the Pension Funds' financial transactions. In addition the Pensions and Accounting Manager has confirmed that, to the best of his knowledge and belief, the financial transactions of the pension fund are in accordance with relevant legislation and regulations. There are no legality issues arising from our audit which require to be brought to the attention of those charged with governance.

Accounting issues arising

Presentational and monetary adjustments

14. A number of presentational adjustments were identified during the course of the audit. These were discussed and agreed with management who agreed to amend the unaudited financial statements.

15. Additionally, there was one monetary error identified during the course of the audit, relating to the accounting for a rebate of custodian system fees received. Paragraph 24 of this report provides more details on this issue. Officers considered this error to be immaterial to the financial statements and we concurred with this view. No amendment was made to the accounts as a consequence.

16. Local authority bodies in Scotland are required to follow the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14, supported by International Financial Reporting Standards (IFRS). We concluded that the financial statements had been prepared in accordance with extant guidance.

Report to those charged with governance

17. We presented our report to those charged with governance (ISA 260) to the Pensions Audit Sub-Committee, on 22 September 2014, and the Pensions Committee on 23 September 2014. The primary purpose of that report is to communicate the significant findings arising from our audit prior to finalisation of the independent auditor's report. The main points are set out in the following paragraphs.

18. **Investment Management Expenses**: In 2012/13 we highlighted that investment management expenses disclosed in the Pension Fund Accounts and supporting notes did not fully reflect the fees charged. CIPFA recently published guidance on accounting for pension scheme management costs, to assist fund comparability.

19. Whilst the June 2014 publication date for this guidance made it too late in the accounts preparation cycle for pension funds generally to apply it in 2013/14, Lothian Pension Funds' officers had been working closely with CIPFA on the development of the guidance.

20. Information from investment managers allowed the fund to apply the principles of the CIPFA guidance and recognise these particular investment management costs as a cost in the fund account, rather than a reduction in the change in market value of investments. As part of our audit we reviewed the reasonableness of the methodology applied and sample checked the calculations undertaken to determine the investment management costs.

Refer to Action Plan Point 1

21. **Additional Voluntary Contributions (AVCs):** The financial statements include disclosure notes setting out AVCs made by employees in the Lothian Pension Fund and Lothian Buses Pension Fund. However, the notes did not separately identify the contributions and fund values between funds. Officers sought the required information from fund managers to facilitate reporting of additional voluntary contributions separately for the Lothian and Lothian Buses Pension Funds. This was subsequently provided but too late for inclusion in the 2013/14 accounts. Suitable assurance has been obtained for 2014/15.

22. Further narrative was added to accompany the AVC notes in each Fund. It emphasised that the sums presented relate to both Lothian Pension Fund and Lothian Buses Pension Fund members.

23. **Group Transfer:** The Lothian Pension Fund account disclosed a group transfer out of £5.287 million. The transfer related to 37 employees of the Edinburgh College of Art who transferred employment to the University of Edinburgh in August 2011. Unlike individual transfers, which are recognised in the fund accounts on a cash basis, group transfers should be accounted for on an accruals basis. However, no accrual was included in the accounts for 2011/12 or 2012/13 as the respective actuaries had not agreed the transfer value. Further narrative was included in Lothian Pension Fund account to provide detail on the characteristics of this transfer.

24. **Custodian Fees:** During 2013/14 it was highlighted to officers by the custodian system provider, Northern Trust, that the Funds were due a rebate on custodian fees previously paid. The rebate due to Lothian Pension Fund and Lothian Buses Pension Fund was £0.219 million and £0.021 million respectively. Although the discount partly related to fees paid in prior years (£0.131 million for Lothian and £0.015 million for Buses), the rebate amounts were recognised fully in the current financial year. This accounting treatment was assessed as having no material effect on the financial statements and we concurred with this assessment.

25. **Unfunded Pension Payments:** The unaudited Lothian Pension Fund Account included a debtor balance of £2.869 million on the balance sheet which related to unfunded benefit payments. These amounts were items such as the award of discretionary years, where the pension costs are met by the

individual employers. In prior years, they were recognised on the City of Edinburgh Council ledger, however following system access changes they were posted to the Pension Fund ledger for 2013/14.

26. The debtors balance on the Lothian Pension Fund account was reduced by £2.869 million to recognise this is properly a City of Edinburgh Council debtor. A compensating increase of £2.869 million was made to the City of Edinburgh holding account balance, to recognise the pay over of the £2.869 million is no longer due. The impact of these adjustments on the current assets in the pension fund accounts was nil.

Outlook

27. The financial statements of the Pension Funds are prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). The main new standards to be adopted in 2014/15 include:

- IFRS 13 Fair value measurement
- IAS 32 Financial Instruments: Presentation
- Annual improvements to IFRSs 2009-2011 cycle

28. These new standards are not expected to have a significant impact on the Pension Funds financial statements.

29. The revised Local Authority Accounts (Scotland) Regulations 2014 apply to financial years 2014/15 onwards. The regulations set out in more detail what is required in respect of financial management and internal control, and in respect of the annual accounts themselves. The significant changes include:

- the requirement for the unaudited accounts to be considered by the Pensions Committee. This can take place following submission to the auditor and up to 31 August if necessary. In addition the audited accounts must be considered and approved for signature by the Pensions Committee by 30 September with publication on the Authority's website by 31 October.
- the Pensions Committee will be required to carry out an annual review of the fund's system of internal control, together with the requirement to approve an annual governance statement or equivalent.
- the Pensions Committee will be required to consider the efficiency and effectiveness of internal audit.

30. The Pension Funds' already undertake a number of the revised regulation requirements. Going forward, the Funds will need to ensure that all the conditions of the revised regulations are implemented.

Financial position

31. Audited bodies are responsible for conducting their affairs and for putting in place proper arrangements to ensure that their financial position is soundly based.

32. Auditors consider whether audited bodies have established adequate arrangements and examine:

- financial performance in the period under audit
- compliance with any statutory financial requirements and financial targets
- ability to meet known or contingent, statutory and other financial obligations
- responses to developments which may have an impact on the financial position
- financial plans for future periods.

33. These are key areas in the current economic circumstances. This section summarises the financial position and outlook for the Fund.

Financial results

34. Lothian Pension Funds prepares an annual administration budget for the delivery of its service plan to members. This budget for administration related costs is routinely reported to the Pensions Committee, where any variances are reviewed.

35. As detailed in the 2013/14 financial statements, there was a total underspend of £0.959 million against budgeted administration costs for the financial year. The most significant element of underspend was down to savings realised through the use of in-house investment management.

Funding position

36. The most recent triennial valuation for Lothian Pension Funds was reported in February 2012. The report highlighted that the main fund's assets valued at 31 March 2011 were sufficient to meet 96% of its liabilities accrued up to that date, resulting in a funding shortfall of £142 million. This represents an improved position from the previous triennial valuation (as at March 2008) which reported a funding position of 85% (a funding shortfall of £524 million).

37. The movement in funding position has been significantly influenced by recent changes including pension increases being linked to the Consumer Price Index and the way life expectancy is treated. These movements are summarised in **Exhibit 1**.

Exhibit 1: Movement in main fund valuations 2008 to 2011

Fund Details	2008 £million	2011 £million
Assets	2,903	3,477
Liabilities	(3,427)	(3,619)
Net Liability	(524)	(142)
Funding Level	85%	96%

Source: actuary's valuations from 2008 and 2011

38. The funding levels calculated at the last triennial revaluations in 2011 for the Lothian Buses Pension Fund and Scottish Homes Pension Fund were 112% and 86% respectively. The 2014 triennial valuations are currently being prepared by the actuary and will be used to set contribution rates from April 2015.

39. The actuarial values of promised retirement benefits for each fund are calculated annually by the actuary for the purposes of international accounting standards. These annual values are not relevant for calculating funding levels or setting employer contribution levels.

40. The Lothian Pension Fund actuarial annual statement at 31 March 2014 estimated a value of promised retirement benefits as £5,483 million (2012/13: £4,946 million). Net assets of £4,377 million at 31 March 2014 were sufficient to meet 80% of this value. This increase in the net liability is mainly due to a fall in real bond yields. The liability is not a full actuarial valuation, but an estimate of the present value of the future liabilities of the fund, based on the fund actuary's assumptions regarding the future discount rate, longevity of members and rate of inflation.

41. Based on the 31 March 2014 actuarial annual statement for the Lothian Buses Pension Fund, the net assets of £337 million represent 94% of existing promised benefits of £358 million. This fund stopped admitting new members in 2008; consequently the long term trend will be for the number of active members to decrease.

42. The Scottish Homes Pension Fund has no active members contributing to the fund. Based on the 2013/14 actuarial statement, net assets of £136 million at 31 March 2014 represent 99% of estimated promised retirement benefits of £138 million. As guarantor of the fund, the Scottish Government is liable to meet any shortfall in funding.

43. The Funds' actuary carried out a modelling exercise during 2012/13 to provide updated cash flow projections based on Fund membership at 31 March 2013. This work produced a contribution stability mechanism, designed to provide certainty of pension contributions for certain Fund employers for future years, whilst still maintaining appropriate funding levels to the Fund.

44. The modelling exercise also confirmed that Lothian Pension

Fund is expected to move to a negative cash flow position in the near future. The Fund will use investment income to pay pensions when this occurs, rather than reinvesting. As identified in our Annual Audit Plan, the Funds are taking action to monitor the membership profile over the long term.

Outlook

45. The longer term outlook for the Funds will remain challenging as significant budget reductions continue to be required by Local Government employers in future years. Member bodies are likely to seek to deliver efficiencies through reductions in staffing levels and recruitment, which would impact on the number of active members in Lothian Pension Fund. Reductions in the number of active members will place a greater emphasis of the Funds' investments for the generation of income to meet payments for members' benefits.

46. In the short-term, the introduction of auto enrolment has contributed to an increase in active membership numbers from 28,869 to 30,622. These numbers may increase further as other employers progress through the auto enrolment process.

47. In addition to the Funds' obligations to members, their financial position is determined by the performance of their investments. In the current environment of low Bond yields and interest rates, obtaining the required rates of return to sustain the financial position will require careful consideration of the types of investments that are made. Any investments in alternative products by the Funds will require vigilant management to limit their exposure to any downside risks and ensure a reliable rate of return.

Governance and accountability

48. Members of the Pensions Committee and the Pensions and Accounting Manager are responsible for establishing arrangements for ensuring the proper conduct of the affairs of the Funds and for monitoring the adequacy and effectiveness of these arrangements.

Corporate governance

49. The corporate governance framework for the Funds is centred on the Pensions Committee which is supported by a Pensions Audit Sub-Committee. City of Edinburgh Council's Director of Corporate Governance has delegated authority for the implementation of the Funds' investment strategy. An Investment Strategy Panel provides advice on these matters.

50. Based on our observations and audit work our overall conclusion is that the governance arrangements within the Funds are operating effectively.

Governance processes and committees

51. City of Edinburgh Council acts as the administering authority for the Funds. It is responsible for managing and administering the scheme for scheduled and admitted bodies.

52. The Council has delegated the administration, management and investment of the Pension Funds to the Pensions Committee. The committee comprises councillors from City of Edinburgh Council and representatives from employers and members of the schemes.

53. A Consultative Panel exists to enhance participation in the development and scrutiny of matters relating to the Pension Fund. It is the main mechanism for engagement with the Funds' stakeholders and enables their involvement in the decision-making process. The panel meets quarterly on the same cycle as the committee. Two members of the panel are also members of the Pensions Committee.

54. Day to day administration of the Funds is carried out by the Investment and Pensions Division which is part of the council's Corporate Governance department. The Head of Finance serves as the Section 95 Officer for all of the council's accounting arrangements. However for the Lothian Pension Funds, this Section 95 responsibility has been delegated to the Pensions and Accounting Manager.

Investment Operations

55. A review of investment governance arrangements of the pension funds was instigated in December 2013 at the request of the Director of Corporate Governance. External consultants were appointed to review investment operations, particularly those relating to internally managed investments.

Investment controls

56. The review by the external consultants concluded that the existing systems and controls were generally sufficient for the Funds' current investment activities. A number of key risks were identified including those around the investment staff remuneration and retention policies. It was noted by the consultants that the Funds did not externally benchmark salaries and that notice period provisions in investment staff contracts were not in line with market practice. The consultants also noted that adherence to the council's human resources policies and procedures limited the Funds' ability to mitigate these staffing risks.

57. One of the options identified was the creation of a special purpose vehicle separate from the council which would allow the board of this vehicle to decide on appropriate terms and conditions. The vehicle would be wholly owned by the council. At the September 2014 meeting of the Pensions Committee members agreed in principle that a special purposes vehicle should be established. This option was subsequently approved by City of Edinburgh Council.

Financial Conduct Authority (FCA) authorisation

58. On 24 March 2014, the Pensions Committee agreed that the Lothian Pension Funds would seek Financial Conduct Authority (FCA) authorisation.

59. The purpose of seeking this authorisation is to

- further strengthen the governance of the investment activities of the pension funds,
- ensure that the current activities of the Funds' investment function continue to be carried out within the appropriate regulatory regime
- further facilitate the ongoing development of this team to generate further cost efficiencies and savings for the benefit of the stakeholders of the Funds.

60. At their October 2014 meeting, City of Edinburgh Council approved the creation of one or, if appropriate following legal and tax advice, two special purpose vehicles wholly owned and controlled by City of Edinburgh Council for the purposes of:

- seeking Financial Conduct Authority (FCA) authorisation for the activities of this team
- directly employing certain key staff associated with Lothian Pension Fund's investment function.

61. The costs and efficiencies generated by these special purpose vehicles will be borne by and attributed to the pension funds.

62. Creation of the special purpose vehicles will have a number of implications for the audit of the pension funds in future years. The impact of these changes will be considered as part of the planning process for the 2014/15 audit of the Pension Funds.

Governance Compliance Statement

63. Pension administration regulations require an administering authority to prepare and publish a governance compliance statement to measure their pension fund's governance arrangements against the standards set out in the guidance issued by the Scottish Ministers. Having reviewed the governance compliance statement we are satisfied that it complies with the guidance issued by the Scottish Ministers.

64. The governance structures have been seen to be working well with no issues with regard to openness, reporting or scrutiny. The information reported in the governance compliance statement is consistent with our knowledge and understanding of the Funds' governance arrangements, based on our audit knowledge, attendance at meetings, and review of papers and minutes.

65. The Code of Practice on local authority accounting in the United Kingdom 2014/15 has been amended to require pension fund bodies to include either:

- a separate statement on system of internal financial control (SSIFC), or
- additional disclosures, reports or statements as necessary in order to meet the requirements of that statement.

66. The Funds have addressed this in 2013/14 and in previous years by including an Annual Governance Statement in their annual report as a matter of best practice. This statement has been based primarily on the content of the council's Annual Governance Statement. Whilst some of the content within the council's statement is pertinent to the Funds, there are aspects which are of less relevance.

Refer to Action Plan Point 2

Internal control

67. While auditors concentrate on significant systems and key controls in support of the opinion on the financial statements, their wider responsibilities require them to consider the financial systems and controls of audited bodies as a whole. However, the extent of this work is also informed by an assessment of risk and the activities of internal audit.

68. The Funds' financial systems are run alongside those of the City of Edinburgh Council and some of the council's systems are used by the Investments and Pensions Division. We obtained confirmation from the external auditors of the council that there were no significant weaknesses in the internal controls for those systems utilised by the Investments and Pensions Division for 2013/14.

69. As part of our work we also took assurance from key controls within the Funds' financial systems. From our work on these

systems, no significant control weaknesses were identified.

Internal audit

70. Internal audit is an important element of the Funds' governance structure. The internal audit service is provided by City of Edinburgh Council via a co-source arrangement with PricewaterhouseCoopers.

71. We reviewed internal audit at the planning stage of our audit and concluded that they operated in accordance with the Public Service Internal Audit Standards and had sound documentation standards and reporting procedures in place.

72. During 2013/14, internal audit carried out a review of the implementation of the Funds' new payroll module. The work concluded that the project was being appropriately managed with sufficient governance and risk management controls and safeguards being in place. This work was considered in our assessment of the internal controls put in place by the Funds.

73. The Public Sector Internal Audit Standards require internal audit to deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement. The annual internal audit opinion should conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control. It should also contain certain information, including a summary of the work that supports the opinion; a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme.

74. Internal audit provided an opinion in compliance with the above requirements, and it was presented to the Pensions Committee on 17 June 2014 along with other key assurance statements, as part of the consideration of the unaudited financial statements.

Arrangements for the prevention and detection of fraud

75. The Funds comply with the relevant fraud and irregularity policies of Edinburgh City Council and these have been reviewed as part of the council wide audit. Overall we concluded that arrangements for the prevention and detection of fraud are adequate and there are no issues which we require to include in this report.

76. The Funds participate in the National Fraud Initiative (NFI). The NFI uses electronic data analysis techniques to compare information held on individuals by different public sector bodies and different financial systems, to identify data matches that might indicate the existence of fraud or error.

77. As part of our local audit work we monitor City of Edinburgh

Council's approach to participation in NFI both in terms of the submission of the required datasets and their approach to and progress investigating the subsequent data matches. A total of 1,086 pension matches were identified from the most recently completed exercise. Of these 330 were 'recommended matches'. These matches identify people who are in receipt of a pension but also appear on DWP and registrars records as being deceased, or who appear on another payroll system.

78. During 2013/14, the Pension and Investment Division officers were engaged in investigating matches and resolving outcomes. The Division identified overpayments £0.3 million from the matches reviewed, with these amounts currently being recovered.

Arrangements for maintaining standards of conduct and the prevention and detection of corruption

79. Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and have proper arrangements in place for implementing and monitoring compliance with standards and codes of conduct, standing orders and financial instructions. Auditors consider whether bodies have adequate arrangements in place. Overall we concluded that arrangements are adequate and there are no issues that we require to include in this report.

80. Pension staff, as employees of the council, are bound by the council's employee Code of Conduct. Additionally, committee members are expected to have high standards of character and personal conduct and must declare their interests where relevant. Furthermore, committee members receive training on standards in public life.

Outlook

81. Progress continues to be made by the Funds towards the implementation of the new Local Government Pensions Scheme (LGPS) in Scotland.

82. There are a number of challenges for the Funds including the move to pensions on a career average basis. There will be a requirement to maintain pension records for each individual that will bring together a range of entitlements arising from benefits built up under different pension regimes. This will not only increase administrative workload initially, but will also undoubtedly generate many more enquiries from fund members seeking clarification on their benefits on an ongoing basis.

83. Each pension fund in Scotland will also be required to establish a Pension Board by 1 April 2015 which will be responsible for assisting with compliance with scheme regulations and the requirements of the pensions regulator.

84. Regular updates have been provided to the pensions committee on progress being made with implementing the changes, however, the timescales involved are short and there is a risk that not all the required changes will be made in time.

Refer to Action Plan Point 3

Best value, performance and use of resources

Best Value

85. The Pension Funds have not been subject to a Best Value review; however, it is covered by the overall Best Value arrangements of the administering authority.

Performance

Investment Performance

86. Investments are managed both by external fund mangers and the Funds' internal investment management team. Through the use of mandates, responsibility for the management of the Funds' investments has been divided up. **Exhibit 2** shows the allocation of investments to fund managers for Lothian Pension Fund as at 31 March 2014.

87. Approximately 45% of the Lothian Buses Pension Fund is managed by in-house investment mangers, with the remainder allocated between 2 separate external investment managers.

88. The Scottish Homes Pension Fund investments are managed exclusively by external investment managers. The Fund's equity and bond investments account for 95% of its assets at 31 March 2014. These have been managed passively by external investments managers, State Street, since 2010.

Exhibit 2: Fund managers' allocation2013-14 (main fund)

Fund Manager	Market Value £'000	% of Total Fund Value
Ballie Gifford	152,847	3.5
Cantillon	238,423	5.5
Harris	175,955	4.1
Invesco	140,806	3.2
In-house Investment Managers	2,781,112	64.1
Mondrian	92,455	2.1
Nordea	163,920	3.8
Standard Life	322,037	7.4
Rogge	184,569	4.2
UBS	91,186	2.1
Total	4,343,310	100

Source: Lothian Pension Fund audited financial statements 2013/14

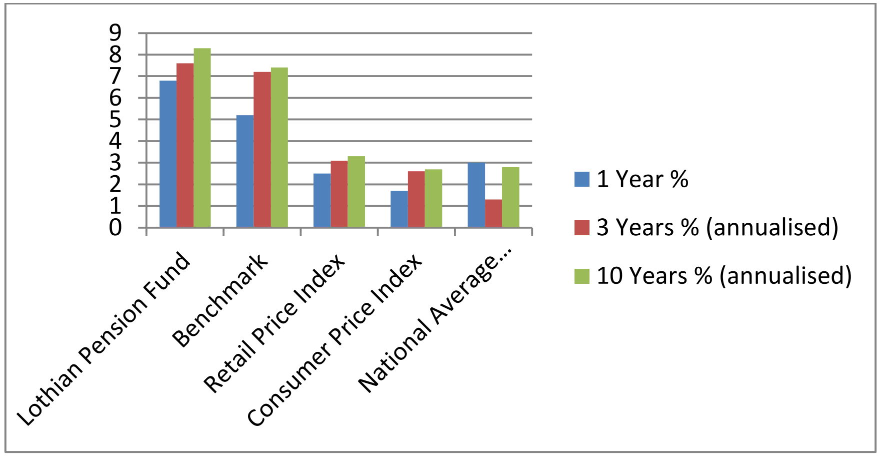
89. The main mechanism for measuring investment performance is through an analysis of the returns achieved by each of the Funds' fund managers. Each active Investment Manager has a defined performance benchmark and objective, against which performance will be measured. Their performance, in terms of achieving benchmarks, is subject to independent verification by an external specialist provider and is regularly reported to the pensions committee and investment strategy panel.

90. Investment returns of Lothian Pension Fund have outperformed benchmark targets over the short, medium and longer term, as illustrated in **Exhibit 3**. The table also shows that over a period of one, three and ten years the pension fund has outperformed measures of inflation i.e. the consumer price index, the retail price index and national average earnings.

91. Lothian Buses Pension Fund investment returns exceeded the required performance benchmark levels for 2013/14. The portfolio as a whole made returns of 8.9% against the benchmark target of 5.1%.

92. Scottish Homes Pension Fund investment returns met the required performance benchmark levels for 2013/14 of 2.1%. As described at paragraph 86, these are managed passively.

Exhibit 3: Investment Performance – Lothian Pension Fund



Source: Pensions Committee, Investment Performance Update, June 2014

Administration performance

93. The Funds' Administration Strategy was approved by the Pensions and Trusts Committee in March 2010. A revised strategy has since been approved by the committee in September 2013. It contains the standards which are required of the participating employers to ensure that the Funds meet their statutory obligations and are able to deliver services efficiently. The strategy contains a variety of performance measures against which the Funds and the participating employers are assessed.

94. In accordance with Regulation 60A of the LGPS

(Administration) (Scotland) Regulations 2008, the Funds' annual report discloses performance against the measures detailed in the Pension Administration Strategy. In relation to 2013/14 the Funds' performance was broadly in line with the annual targets set. Two targets – concerning stakeholder satisfaction and employer contributions payments - were narrowly missed.

Investment strategies

95. The Funds' investment strategies 2012-17, as agreed by the Pensions Committee in October 2012, have continued to be implemented during 2013/14. The key objective of the Funds' investment strategies is to reduce risk. For the main Fund and Lothian Buses Pension Fund, this has been progressed in 2013/14 through changes within equity portfolios to equities with less volatility, along with an increased exposure to index-linked assets and alternatives.

96. For alternatives, new investments have been made in the main fund, however, there has only been a small change in the percentage of the fund assets in alternatives because of the growth of the fund size. For Lothian Buses, increasing their exposure to alternatives is dependent on identifying attractive opportunities with the fund continuing to appraise investment opportunities.

97. For the Scottish Homes Pension Fund, the strategy has been to reduce the allocation to equities and property and increase the allocation to bonds. In 2013/14, as the actual funding level moved closer to the target funding level, the long term strategy was accelerated which resulted in the current and long term strategies matching.

National performance reports

98. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. Reports in the last year which may be of interest to members and officers are detailed in **Exhibit 4.**

Exhibit 4: A selection of National Performance Reports 2013/14

Report	Key messages
How Councils Work – Charging for Services: Are You Getting It Right?	Councils should have clear policies in place for charging and concessions and councillors should have a lead role in determining these policies
Overview of Local Government in Scotland 2013/14	Underlines the need for councillors to maintain a good understanding of the rapidly changing economic, social and political context.
How Councils Work – Option Appraisals: Are You Getting It Right?	Councillors have a crucial role in option appraisals.

Appendix I – Significant audit risks

The table below sets out the key audit risks identified at the planning stage and how we addressed each risk in arriving at our opinion on the financial statements.

Audit Risk	Assurance procedure
Investment Manager Expenses Investment management expenses disclosed in the Funds' accounts and supporting notes do not currently reflect the full amount of investment management fees charged. Fees deducted from capital values are not shown. **Risk:** *members cannot gauge whether best value is being obtained.*	We reviewed the Funds' approach to investment manager fees deducted from capital against the final issued guidance ***** during our work on the 2013/14 financial statements. *******The guidance was issued following the preparation of the financial statements (June 2014), however the Funds' officers had been working closely with CIPFA during the development of this guidance.*
Payroll System Migration A new payroll system was implemented during the year. The system is integrated with the pre-existing pension administration system ***Risk****: the new payroll system is not implemented with the necessary controls to ensure pension payments are processed in a secure and accurate manner*	Internal Audit has performed a review of the project, considering whether it was appropriately managed with sufficient governance and risk management controls and safeguards being in place. There were no critical issues identified from the report, which was considered during our work reviewing the internal controls put in place by the fund. Our review of the Funds' internal controls also considered the controls in place for the payroll system used previously by the funds (council system) which continued to be in use during the 2013/14 year. No significant control issues were identified from our work on the council's payroll system.

Appendix II – Action plan

<table>
<tr><th>Action plan point / para</th><th>Issue, risk and recommendation</th><th>Management action/response</th><th>Responsible officer</th><th>Target date</th></tr>
<tr><td>1 / 20</td><td>Investment Management Expenses
As identified in our ISA260 report, the Funds have used information from Investment Fund Managers to calculate fees deducted from capital within their 2013/14 financial statements.
Risk
The methodology applied for calculating investment management fees is not consistent with the guidance on Investment management fees issued by CIPFA in June 2014.The application of the methodology is inconsistent across funds throughout Scotland, preventing meaningful comparison.
Recommendation
In relation to the 2014/15 financial statements, the Funds should review their approach to calculating management fees against the CIPFA guidance. Consideration should also be given to reviewing the approach taken against those of other Local Government Pension Schemes.</td><td>As the LPF Financial Controller “had been working closely with CIPFA during the development of this guidance”, it is not envisaged that there should be any material issue of non-compliance with published CIPFA guidance 2014/15. This will, of course, be verified.
LPF will be very interested in the comparability of investment management fee disclosures and consequent benchmarking with other LGPS funds. It may not be possible to ascertain this, however, prior to the determination of suitable methodology and completion by other Funds of the 2014/15 accounts.</td><td>Esmond Hamilton, Financial Controller</td><td>31 May 2015</td></tr>
</table>

Action plan point / para	Issue, risk and recommendation	Management action/response	Responsible officer	Target date
2 / 64	**Annual Governance Statement** The Funds have included an Annual Governance Statement in their annual report as a matter of best practice. This statement has been based primarily on the content of the council's Annual Governance Statement. Whilst some of the content within the council's statement is pertinent to the Funds, there are aspects which are of less relevance. **Risk** *There is a risk that the disclosures in the Annual Governance Statement are not focused on the governance arrangements of the Pension Funds.* **Recommendation** The Funds consider the current format and content of the Annual Governance Statement.	As is customary, the format and content of the Annual Governance Statement of the Lothian Pension Funds will be reviewed in the context of the Council's role as administering authority of the pension funds.	Clare Scott, **Investment & Pensions Service Manager**	31 May 2015

Action plan point / para	Issue, risk and recommendation	Management action/response	Responsible officer	Target date
3 / 82	**Pension Reform** Progress continues to be made by the Funds towards the implementation of the new Local Government Pensions Scheme (LGPS) in Scotland, including the introduction of career average pensions and Pension Boards by 1 April 2015. This is likely to increase administrative workload initially; generate more enquiries from fund members seeking clarification on their benefits on an ongoing basis, and require changes to the pension administration system. ***Risk*** *The Funds will have insufficient resource to deal with the increased workload leading to delays in providing information to members. In addition, there is a risk that not all the required changes will be in place by 1 April 2015.* **Recommendation** The funds should ensure that a comprehensive strategy is in place to manage the changes required by the Pensions Act.	The significant challenges represented by the implications of the LGPS 2015 are recognised. Project planning and preparatory work is underway to try to ensure successful implementation. Review of progress against targets will be undertaken	Clare Scott, **Investment & Pensions Service Manager**	31 March 2015 and implementation beyond

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

New Scheme Update (Governance)

Item number	5.5
Report number	
Executive/routine	
Wards	All

Executive summary

The City of Edinburgh Council ("**CEC**") will require to make certain changes to the governance of the pension funds it administers in order to take into account the arrangements anticipated in the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014 ("**2014 Regulations**"), which seeks to implement the provisions of the Public Service Pensions Act 2013 ("**2013 Act**"). Changes need to be implemented by 1 April 2015.

This report proposes CEC's preferred governance model to ensure compliance with the 2014 Regulations and the 2013 Act. The changes are based on the current draft 2014 Regulations. However, given the potential for these regulations to be amended and the pressing timescale to implement the governance changes, it is proposed that the Committee authorise the Director of Corporate Governance in consultation with the Convener to make changes as may be required. An update on the new governance and its implementation will be provided to Committee in March 2015.

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	

Report

New Scheme Update (Governance)

Recommendations

The Committee is requested to:

1.1 Note the Lothian Pension Fund response to the draft 2014 Regulations (Appendix 1);

1.2 Approve the Nomination Procedure for external members of the Pensions Committee and members of the Pension Board (Appendix 2);

1.3 Approve the Constitution for the Lothian Pension Fund Pension Board (Appendix 3);

1.4 Approve the updated Training Policy for Pensions Committee and Pension Board (Appendix 4);

1.5 Agree that the Director of Corporate Governance in consultation with the Convener is authorised to approve, on behalf of the Committee, any changes to the Constitution, Nomination Procedure or Training Policy required to address (a) subsequent amendments to the 2014 Regulations (b) any changes that may be deemed necessary for the purposes of satisfying the requirements of the 2014 Regulations, the 2013 Act and/or CEC's own requirements and/or (c) necessary improvements or other amendments to cure any errors or ambiguities; and

1.6 Agree that this paper be referred to the City of Edinburgh Council for information.

Background

2.1 Following consideration by the Committee and Consultative Panel, CEC submitted its response to the consultation on the draft 2014 Regulations on 11 November 2014. This response expressed certain concerns as to the form and construction of the proposed regulations. A copy of CEC's consultation response is detailed at Appendix 1 for ease of reference.

2.2 A summary of the new bodies which will be created by the 2014 Regulations, including their remit and powers, is shown in the table below.

	Remit	Powers and Enforcement
Scheme Manager	The administering authority of the Pension Funds, responsible for organising and administering the pension funds.	n/a.
Scheme Advisory Board (SAB)	A national independent body advising Scottish Ministers on the operation of LGPS in Scotland and any changes required to the scheme. Also advises Scheme Managers and Pension Boards.	The regulations provide that the Scottish Ministers, Scheme Manager or Pension Board ***must have regard*** to any advice given by the SAB.
Pension Board	Assisting the Scheme Manager in relation to compliance with the regulations, applicable law, The Pensions Regulator requirements and anything else anticipated by the 2014 Regulations.	May requisition further reports. May request that the Committee review decisions where the Pension Board is in disagreement. Where there is a continuing disagreement with the Pensions Committee, the SAB may require that a joint report is published in the Scheme Manager's annual report and/or website.
The Pensions Regulator (TPR)	Regulator of UK work-based pension schemes and provides guidance to trustees and employers on what is required of them to ensure good administration and to protect member benefits.	Investigates schemes, trustees and employers and can requisition documents and other information if relevant. Where issues are identified, TPR may issue direction/penalty notices, or pursue action in civil or criminal court where appropriate. With the exception of funding issues, the TPR's powers will now apply equally to the LGPS.

Main report

3.1 This report proposes the City of Edinburgh Council's preferred governance model to ensure compliance with the 2014 Regulations and the 2013 Act. The new governance arrangements comprise:

- Pensions Committee, broadly unchanged from the current arrangement;
- Pensions Audit Sub-Committee, broadly unchanged from the current arrangement;
- A new Pension Board, replacing the current Lothian Pension Funds' Consultative Panel; and
- The Fund's Training Policy, updated to take account of the new arrangements and the role of the Pension Board.

3.2 **Pensions Committee:** it is assumed that the constitution, membership and remit of the Committee will remain unchanged. The Committee would continue to include one member and one employer representative, each with full voting and participation rights.

3.3 A draft nomination procedure for the employer and member representatives is detailed in Appendix 2 to this report. It is proposed that these members would be elected direct, rather than via the Consultative Panel.

3.4 **Audit-Sub Committee**: it is assumed that the constitution, membership and remit of the Audit Sub-Committee will remain unchanged.

3.5 **Pension Board:** a Pension Board will be created with a remit to assist the Committee in ensuring that it acts in compliance with applicable law, regulation and codes or practice. A proposed constitution for the Pension Board is detailed in Appendix 3 to this report.

3.6 It is envisaged that membership of the Pension Board will be five individuals put forward by the Trade Unions representing the members of the pension funds and five individuals nominated from those put forward by the employer bodies in the pension funds. It is envisaged that Members of the Pension Board will also attend meetings of the Audit Sub-Committee.

3.7 **Consultative Panel:** it is proposed that the Consultative Panel will be wound-up with effect from 31 March 2015.

3.8 **Training:** the Fund's Training Policy has been updated to take account of the establishment of the Pension Board and its particular remit. A draft revised Training Policy is detailed in Appendix 4 to this report. The proposed requirement for the Pension Board members to have a minimum of 3 days training is included in the draft.

3.9 This Model is based on the current draft 2014 Regulations. However, given the potential for the final regulations to be different to the draft version, and the pressing timescale to implement the governance changes, it is proposed that the Director of Corporate Governance, in consultation with the Convener be authorised to adapt the governance changes/model as may be required. Particular areas which may be reviewed on receipt of the final 2014 Regulations are as follows:

- Change the definition of Employee Members to include representatives from the membership other than those nominated by trade unions; and
- Section [2.6] relating to substitutes. This has been included as required by the regulation but due to the additional resource required to maintain training, preference would be to remove this clause.

3.10 The 2014 Regulations come into effect on 1 April 2015 therefore it is imperative that the new governance arrangements are put into place over the coming months. The outline and indicative timetable for implementation is as follows:

	Timetable
Communicate new governance arrangements to members and employers via website	24 December 2014
Invite nominations to Pension Board and for external members of Pensions Committee	24 December 2014
Deadline for nominations	Mid February 2015
Nominations considered & selections made	Early March 2015
External Pensions Committee members endorsed by City of Edinburgh Council	12 March 2015
Induction Training	Mid March 2015
Final meeting of Pensions Committee and Consultative Panel	25 March 2015
Pension Board in place	1 April 2015
First joint meeting of the Pensions Committee and Pension Board under the 2014 Regulations	June 2015

3.11 An update on the governance changes and its implementation will be provided to Committee in March 2015.

Measures of success

4.1 CEC's amended governance arrangements for the administration of the pension funds need to be in place by 1 April 2015 to ensure compliance with the 2014 Regulations and the 2013 Act.

4.2 The new governance arrangements facilitate improved and efficient ongoing compliance of the pensions funds, without unnecessarily impeding the strategic decision making of the Committee or the day-to-day administration of the funds.

4.3 Any duplication between the remit, operation and associated costs of the Committee, Audit-Sub Committee and the Pension Board is kept to a minimum.

Financial impact

5.1 There will be some additional costs to CEC associated with operating a further body within the governance structure to administer the pension funds. These costs might potentially be exacerbated further by the additional training and adviser costs that are anticipated by the 2014 Regulations.

Risk, policy, compliance and governance impact

6.1 The 2014 Regulations and the 2013 Act are intended to facilitate better governance of the overall LGPS in Scotland and the individual pension funds. However, CEC has already addressed many of the key concerns in its current governance structure and so does not necessarily anticipate any improvements for the fund in the short term. Improvements may however follow in the longer term, through the effective operation of the governance framework/training programmes and more active input from the Pensions Regulator and, potentially, the National Scheme Advisory Board.

6.2 It is recommended that this paper is referred to the City of Edinburgh Council to raise awareness of the governance changes and the potential impact on the administration of the pension funds.

6.3 CEC's scheme of delegation and Committee terms of reference may require to be updated to take into account the governance changes proposed by this report.

Equalities impact

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

Sustainability impact

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

Consultation and engagement

9.1 Notwithstanding this subject of this paper, the Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is currently integral to the governance of the pension funds administered by CEC.

Background reading / external references

Draft the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014
http://www.sppa.gov.uk/index.php?option=com_content&view=article&id=486&Itemid=252

Alastair Maclean

Director of Corporate Governance

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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 – Lothian Pension Fund response to the draft 2014 Regulations Appendix 2 – Nomination Procedure for external members of the Pensions Committee and members of the Pension Board Appendix 3 – Constitution for the Lothian Pension Fund Pension Board Appendix 4 – Training Policy

Annex B

The Local Government Pension Scheme (Governance) (Scotland) Regulations 2014

RESPONDENT INFORMATION FORM

Please Note this form **must** be returned with your response to ensure that we handle your response appropriately

1. Name/Organisation

Organisation Name

City of Edinburgh Council, acting in its capacity as administering authority for the Lothian Pensions Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund

Title Mr ☐ Ms ☐ Mrs ☒ Miss ☐ Dr ☐ ***Please tick as appropriate***

Surname

Scott

Forename

Clare

2. Postal Address

Investment and Pensions Service Manager, Atria One, 144 Morrison Street, Edinburgh

Postcode EH3 8EX	**Phone** 0131 469 3865	**Email** clare.scott@edinburgh.gov.uk

3. Permissions - I am responding as…

Individual ☐ / **Group/Organisation** ☒

Please tick as appropriate

(a) Do you agree to your response being made available to the public (in Scottish Government library and/or on the Scottish Government web site)?

Please tick as appropriate ☐ **Yes** ☐ **No**

(b) Where confidentiality is not requested, we will make your responses available to the public on the following basis

Please tick ONE of the following boxes

Yes, make my response, name and address all available ☐

or

Yes, make my response available, but not my name and address ☐

or

Yes, make my response and name available, but not my address ☐

(c) The name and address of your organisation ***will be*** made available to the public (in the Scottish Government library and/or on the Scottish Government web site).

Are you content for your ***response*** to be made available?

Please tick as appropriate ☒ **Yes** ☐ **No**

(d)	We will share your response internally with other Scottish Government policy teams who may be addressing the issues you discuss. They may wish to contact you again in the future, but we require your permission to do so. Are you content for Scottish Government to contact you again in relation to this consultation exercise? ***Please tick as appropriate*** ☒ **Yes** ☐ **No**

Annex B

This response details the comments of the City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund) ("**Lothian Pension Fund**") on the draft Local Government Pension Scheme (Governance) (Scotland) Regulations 2014 (the "**2014 Regulations**") which are intended to implement the spirit and intention of the Public Service Pensions Act 2013 (the "**2013 Act**"). In summary, the Lothian Pension Fund has concerns that the 2014 Regulations do not constitute sufficiently competent legislation and, despite reflecting the Heads of Terms agreed by SLOGPAG (Scottish Local Government Pension Advisory Group), without material change would not reflect the spirit and intention of the 2013 Act. This could jeopardise the principles of good governance of the Local Government Pension Scheme in Scotland.

In the view of the Lothian Pension Fund the legislative process leading to the drafting of the regulations would have benefitted from greater and more direct input from pensions experts and practitioners.

A - KEY POINTS

1. **Appropriate breadth of appointments for Pension Boards:** There continues to be a concern that the 2014 Regulations focus on employer and member *representation*, but without sufficient recognition of the technical *compliance* function that Pension Boards are to carry out in the best interests of the relevant stakeholders. The Lothian Pension Fund is strongly of the view that there needs to be sufficient flexibility to populate Pension Boards with suitably qualified persons. This would include employer and member representatives, in accordance with the 2013 Act, but not to the exclusion of all others. The 2014 Regulations, as currently construed, would potentially lead to practical issues around (1) those persons appointed to the board not having sufficient knowledge and understanding to perform the role and potentially becoming reliant on external advisors, and (2) the Pension Board not being able to draw on sufficient numbers of suitable persons and replacements to maintain a quorum for the body. In each case, this may result in considerable operational and cost inefficiencies that would not be in the interests of the fund and relevant stakeholders.

2. **Active role of the Scheme Advisory Board:** The 2013 Act anticipated that the Scheme Advisory Board ("**SAB**") will play a key role in advising, in Scotland, the Scottish Ministers on the wider operation of the LGPS in Scotland and the desirability of any changes to the scheme. Given the complexities surrounding scheme change, it will be important that the SAB is properly constituted to include appropriate representation of the funds, the employers and the members of the funds and ensure that those individuals have appropriate levels of knowledge, skill and expertise. It will also be important that the SAB does have an active role in advising the Scottish Ministers, rather than simply advising on the request of the Scottish Ministers, to ensure that the Scottish Ministers continue to have an active involvement and awareness of LGPS matters.

3. **Common purpose and duties:** The Pensions Boards and SAB should each operate as a single body with a common purpose and duty to act in the best interests of the relevant stakeholders in the fund and (where appropriate) the wider LGPS scheme. The bodies only therefore need to appoint a single secretary and a single set of advisors to support their respective functions. Such decisions would be made by agreement of the members of the relevant body in accordance with its constitution. It would be confusing, potentially divisive and inefficient to operate a dual "member versus employer" structure within a single body of the nature of the SAB and Pensions Boards. With that in mind, Lothian Pension Fund is of

the view that all reference to this dual structure (e.g. “two sides” etc.) should be removed from the 2014 Regulations.

Six member representatives (including trade unions) and six employer representatives are currently able to attend and participate in the Pensions Committee meetings of the Lothian Pensions Fund as members of the Consultative Panel. In addition, two of those individuals, an employer and member representative also participate as full members of the Pensions Committee, with voting rights on the strategic decisions of the funds. Lothian Pension Fund’s experience is that these participants are fully integrated within the governance of the Lothian Pension Fund and are happy to exercise their rights, and instruct/accept advice etc., as a single collective body.

4. **Representation of members:** The Lothian Pension Fund does not think it is appropriate to interpret the reference to member representatives in the 2013 Act as being limited to trade union representation. The Lothian Pension Fund would envisage trade union representatives playing a critical role here, but not to the exclusion of providing representation for the significant number of members who are not affiliated or members of a trade union body. The 2013 Act does not make specific reference to trade union representatives, rather providing for collective representation for members of the funds, and nor do the English Regulations adopt this approach.

5. **Efficiencies across UK LGPS:** The Lothian Pension Fund notes that the 2014 Regulations reflect a different approach to implementing the 2013 Act to the proposed Local Government Pensions Scheme (Amendment) Regulations 2014 (the “**English Regulations**”), designed to address the same points for the 89 LGPS funds in England and Wales. The Lothian Pension Fund would note that unless there is good reason to depart from the approach taken in the English Regulations there would be significant benefit in the 2014 Regulations being aligned with the English Regulations, given the synergies and efficiencies that could be achieved in pooling knowledge and experience across all the LGPS funds across the UK. For instance, it is reasonably foreseeable that certain areas of the 2014 Regulations will require some amendment or may raise finer points of interpretation arising from the practical application of the regulations. Where the English and Scottish regulations are broadly aligned, the Scottish funds would benefit from independent legal opinions, Scheme Manager and government department views and/or the opinions of the Pensions Regulator arising from the experiences of the 89 funds in England and Wales. If, however, the 2014 Regulations materially deviate from the English regulations without good reason, the Scottish funds would not be able to benefit from the potentially significant efficiencies and savings that could be obtained here.

6. **Standard of knowledge and understanding:** The 2014 Regulations could further clarify the levels of knowledge and understanding required of Pensions Board members by cross referring to the Pension Regulator’s Codes of Practice and other guidance in this area. An equivalent approach could also be taken in relation to members of the SAB. This would help inform the prospective members of the expectations on them in performing their roles and also those responsible for providing training for such individuals.

B - DETAILED COMMENTS

REGULATION	COMMENT
Scheme Advisory Board	
2(1)	**Constitution and remit:** The regulation should formally constitute and establish the SAB. See 110(1) of the English Regulations.
2(2)	The word "main" should be deleted as being ambiguous and confusing. The functions of the SAB will be as stated in the 2014 Regulations, with any other functions requiring to be expressly detailed therein. See 110(2) and (3) of the English Regulations.
	As above, the SAB should simply be constituted to advise the Scottish Ministers, rather than only doing so at their request. See 110(2) of the English Regulations.
	Provisions should be included around the SAB's ability to determine its own constitution, procedures etc. See 110(4) of the English Regulations.
	Provisions should be included around funding the costs of the SAB, how the costs will be split and/or determined and whether there will be any budget oversight for the SAB. We note that the English Regulations do seek to address this to some extent in paragraph 113.
2(3)	**Enforceability:** This provision is not sufficiently clear in setting out the intention behind the requirement of a body to "have regard to the advice". This may result in uncertainty and potential legal challenge, which would not be in the best interests of LGPS stakeholders.
3(1) and 3(2)	**Membership**: As above, the Lothian Pension Fund does not believe that restricting the membership of the SAB to a "bipartite body" of local government employer and trade union representatives would provide sufficient flexibility to ensure that this body includes appropriately representative and qualified persons from time to time to perform the relevant functions. The Lothian Pension Fund would advocate the less prescriptive approach taken in the English Regulations, so that there would be more flexibility to include representatives from the Scottish funds and/or any independent members with particularly relevant expertise.
	The Lothian Pension Fund does not think it is appropriate to interpret the reference to member representatives in the 2013 Act as being limited to trade union representation. The Lothian Pension Fund would envisage trade union representatives playing a critical role here, but not to the exclusion of providing representation for the significant number of members who are not affiliated or members of a trade union body. The 2013 Act does not make specific reference to trade union representatives, rather providing for collective representation for members of the funds. The English Regulations and those for other Scottish public service pension schemes do not adopt this approach.
	Knowledge and expertise: The words "inform their role" could be replaced with "perform their role to an appropriately competent standard of knowledge, skill and care and with regard to any relevant guidance issued by the Pensions Regulator from time to time".
3(4)	**Secretaries:** As above, the Lothian Pension Fund does not think it would be appropriate for a single body to have two secretaries. This would simply create confusion in the role (e.g. taking, combining and agreeing two different sets of minutes would not be productive etc.) and cause unnecessary

	duplication, confusion and bureaucracy. A single secretary should be appointed by agreement of the members of the SAB and the constitution could deal with such matters as rotation, term, re-appointment, removal etc.
3(5)	**Advisers:** As above, the Lothian Pension Fund does not believe that the 2014 Regulations should expressly refer to the right of any particular member or membership group attending the meeting to have advisers present, as the body itself should appoint its own advisers - acting collectively and with their common duty to the Scottish Ministers and stakeholders of the funds in mind. The presence of multiple advisers would not be appropriate for the operation of a body of this nature nor would it be conducive to effective and efficient governance. For instance, how would the chairperson manage the nature and type of adviser to be present and the associated costs, and duplication of costs, that would need to be met. In addition, the SAB is constituted to advice the Scottish Ministers on the relevant matters and so it would not be appropriate for the advisers of the Scottish Ministers to attend, and potentially influence, the meetings and decisions of the SAB itself.
4	**Conflicts of Interest:** The conflict language could be aligned with the English Regulations for the purposes of simplicity and to support ongoing efficiencies that could be generated across the wider UK LGPS.
Pensions Boards	
5	**Constitution and remit:** The drafting of section 5(1) and (2) should be combined to more clearly state the responsibilities of the Pensions Boards. In addition, limb (c) should be removed as being unnecessary and creating ambiguity. The remit of the Pensions Board should be clearly set out in section 5 and not elsewhere. We note that 106(1)(a) of the English Regulations clearly encapsulates the responsibilities of the Pensions Board in one single provision. See also the below comments on paragraph 8 of the 2014 Regulations.
6(1)	**Membership:** As above, the Lothian Pension Fund does not believe that restricting the membership of the Pensions Board to a “bipartite body” of local government employer and trade union representatives would provide sufficient flexibility to ensure that this body includes appropriately representative and qualified members from time to time to perform the relevant functions. The Lothian Pension Fund would advocate the less prescriptive approach taken in the English Regulations, paragraph 107, recognising that the 2013 Act already provides sufficient comfort around the equality of employer and member representatives. In addition, the regulation should expressly set out that the Scheme Manager shall determine the membership of the Pension Board and the manner in which the appointment/removal process, terms of appointment, constitution etc. shall operate in consultation with the members and employers.
6(2)	As above, the Lothian Pension Fund does not think it is appropriate to interpret the reference to member representatives in the 2013 Act as being limited to trade union representation. The Lothian Pension Fund would envisage trade union representatives playing a critical role here, but not to the exclusion of providing representation for the significant number of members who are not affiliated or members of a trade union body. The 2013 Act does not make specific reference to trade union representatives, rather providing for collective representation for members, and nor do the English Regulations adopt this approach.

	In addition, employers do not have a collective organisation from which nominations can be sought. CoSLA represent the Councils in Scotland, but the Scheme Manager will require to operate appropriate selection procedures for the employer representatives on the Pensions Boards.
	Knowledge and expertise: The words "inform their role" could be replaced with "perform their role to an appropriately competent standard of knowledge, skill and care and otherwise in accordance with the requirements and guidance of the Pensions Regulator from time to time."
6(4)	**Secretaries:** as above for the SAB.
6(5)	**Advisors:** as above for the SAB.
7	**Conflicts of interests:** as for SAB.
8	**Implementation of remit:** the remit of the Pensions Board is set out in paragraph 5 and paragraph 8 of the 2014 Regulations in fact details the matters that the Pensions Board may review to support its remit. The heading of this clause should therefore be amended to avoid confusion and to ensure it is clear that the remit should not extend beyond that set out in the 2013 Act and provided for in paragraph 5 of the 2014 Regulations. This is consistent with the approach taken in the English Regulations. 8(2) should be deleted and any reference to investments of the fund and investment principals etc. included in 8(1), making it clear that the Pensions Board shall be to review such activities in order to fulfil its remit set out in paragraph 5 of the 2014 Regulations and the 2013 Act. The current drafting may otherwise lead to ambiguity around the potential extension of the remit of the Pensions Board beyond what is anticipated by the 2013 Act.
8(3)	**Requisitioning reports:** the paragraph should be amended so that the Pensions Board may only requisition reports from the Scheme Manager where it (acting reasonably) determines that this would be necessary to enable it to properly carry out its functions in accordance with the 2014 Regulations.
9	**Pension Committee and Pension Board disagreements:** these provisions should be amended to ensure that a review may only be requested where the Pension Board has demonstrated valid concerns in relation to the decision being in breach of any applicable law, regulation or Code of Practice. The grounds for review set out in paragraph 9(2) are too loosely construed and should therefore be amended accordingly not being appropriately aligned to the remit of the Pensions Board itself. Greater clarity as to what does or does not constitute grounds for the review of a decision should be provided. In particular, 2(a) and (d) are so general in nature as to enable a review to be requested on virtually any decision of the Scheme Manager, at any point in time. Despite this, regulation 9(5) indicates that even where the Pension Board and Scheme Advisory Board oppose a decisions of the Committee they are ultimately powerless to force a change.
Training Programme	
10	This should include appropriate reference to the requirements and guidance issued by the Pensions Regulator from time to time.
Other drafting points	
1(4)	The definition of the fund should read "the pension fund ***or funds*** managed by the scheme manager" reflective of the fact that certain Scheme Managers administer more than one fund.

The Lothian Pension Fund

Nominations and Appointments Policy

for

External Members of the Pensions Committee

and

Members of the Pension Board

INTRODUCTION

Pensions Committee: The City of Edinburgh Council ("**CEC**" or "**Scheme Manager**") operates a Pensions Committee (the "**Pensions Committee**") for the purposes of facilitating the administration of the Lothian Pension Fund, the Lothian Buses Pension Fund, the Scottish Homes Pension Fund and any other Local Government Pension Scheme that it may administer from time to time (the "**Funds**"). The Terms of Reference of the Pensions Committee require that, in addition to the elected members, two additional members should be appointed to the Pensions Committee as follows:

A. a member drawn from the membership of the Funds ("**Member Representative**"); and
B. a member drawn from the scheduled or admitted bodies that participate in the Funds ("**Employer Representative**").

This policy sets out the means through which CEC will operate and support the nomination and appointment of the Member and Employer Representatives to the Pensions Committee.

Pension Board: CEC is also required to establish and maintain a Pension Board (the "**Pension Board**"), for the purposes of assisting with the ongoing compliance of the Funds. The Pension Board is constituted under the provisions of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014 (the "**2014 Regulations**") and the Public Service Pensions Act 2013 and will at all times consist of equal numbers of [trade union representatives (drawn from trade unions that represent the membership of the Funds)] ("**Employee Members**") and [local government] employer representatives [(drawn from local authorities and scheduled or admitted bodies that participate in the Funds) ("**Employer Members**"]. Further to the Constitution for the Pension Board (dated [ ]) (the "**Constitution**") the Pension Board will comprise:

A. [Five] Employer Members; and
B. [Five] Employee Members.

The Constitution provides for the operation of the Pension Board and this policy sets out the Scheme Manager's procedures for inviting nominations for the membership of the Pension Board and putting forward eligible candidates for appointment by the Pension Board.

1. PENSIONS COMMITTEE: NOMINATION AND ELECTION

1.1 Where required to fill a vacancy, employer bodies that participate in the Funds will be invited to nominate a suitable representative to be considered for selection as the Employer Representative on the Pensions Committee.

1.2 Where required to fill a vacancy, the members of the Funds will be invited to nominate themselves to be considered for selection as the Member Representative on the Pensions Committee.

1.3 All candidates put forward for the roles of either Employer or Member Representative will be requested to provide a brief biography, highlighting their background, any relevant experience and why they would be suitable for the role.

1.4 [No person may be appointed to the Pensions Committee under this policy where, in the Scheme Manager's sole discretion, that person has a Conflict of Interest. A **'Conflict of Interest'** being a financial or other interest which is likely to prejudice the exercise of that persons' functions as a member, but does not include a financial or other interest arising merely by virtue of that person being a member or employer body in any of the Funds.]

1.5 Once either the employer bodies and/or members of the Fund have been given a reasonable period of time to respond, CEC will draw-up a list of relevant candidates for each of the roles and send that list on to the Independent Professional Observer or such other suitable independent person or advisor (the "**Independent Professional Observer**") (the "**Review Panel"**) for review with regard to the obligations on the Scheme Manager pursuant to Regulations [7(1)] (*conflicts of interest*) [and [6(1)] and 10 (*requisite training and development*)] of the 2014 Regulations. The Review Panel will check the candidates and their respective submissions with a view to excluding any candidates that, at their discretion, would not meet the criteria set out in the 2014 Regulations or any standards, guidance or code of practice issued by the Pensions Regulator from time to time.

The Review Panel will then send the updated list of potential candidates to CEC to facilitate the election.

1.6 CEC will then facilitate the elections of the Member and Employer Representatives by the members and employers of the Fund respectively. Such election(s) may take place at a meeting called and arranged by CEC or through the form of an electronic or other remote voting system. The Employer and Member Representatives will be required to be elected through receiving a majority of the votes cast by their respective peers. In the event of a tied vote, the Independent Professional Observer will have a casting vote to determine which candidate is appointed to the role. Where only one candidate was put forward for the role, CEC will proceed to appoint that individual to the relevant role without the need for an election.

2. PENSIONS COMMITTEE: APPOINTMENT AND RATIFICATION BY COUNCIL

2.1 Once a candidate for the Member and/or Employer Representative has been selected, and has confirmed their willingness to take up the role, approval of the appointment will be sought from the Council pursuant to the Committee Terms of Reference and Delegated Functions.

2.2 Any newly appointed Member and Employer Representatives will require to have read, understood and signed the Lothian Pension Fund's Council's Code of Conduct prior to taking up their role.

2.3 Any newly appointed Member and Employer Representatives will require to have completed the necessary induction training from CEC prior to taking up their role.

2.4 The Employer and Member Representatives will serve a maximum term of [two] years and whereupon they will either stand down or require to submit themselves as a candidate for a further election.

2.5 The Employer and Member Representatives will be required to make all reasonable efforts to regularly attend the meetings of the Pensions Committee and are required to comply with the Lothian Pension Fund's Training and Attendance Policy. Failure to do so could result in their position(s) on the Pensions Committee being reviewed.

2.6 Any member of the Pension Board will not be eligible for appointment as either the Employer or Member Representative on the Pensions Committee.

3. PENSION BOARD: NOMINATION AND ELECTION

3.1 Where required to fill a vacancy or vacancies, employer bodies that participate in the Funds will be invited to nominate suitable representative(s) to be considered for selection as an Employer Body Member on the Pension Board.

3.2 The Scheme Manager will, in consultation with the Pension Board (once established), review and allocate the Employee Member(s) among the trade unions in order to ensure they are broadly representative of the proportion of members represented by each trade union. Where required to fill a vacancy or vacancies, those trade unions will be requested to invite nominations, elect and put forward suitable individuals for appointment as Employee Member(s) to the Pension Board.

3.3 All candidates put forward for the roles of an Employer Member and/or Employee Member will be requested to provide a brief biography, highlighting their background, any relevant experience and why they would be suitable for the role.

Employer Members

3.4 Once the employer bodies have been given a reasonable period of time to respond, the Scheme Manager will draw up a list of relevant candidates for the role(s) and send that list on to the Review Panel for review with regard to the obligations on the Scheme Manager pursuant to Regulations [7(1)] (*conflicts of interest*) [and [6(1)] and 10 (*requisite training and development*)] of the 2014 Regulations. The Review Panel will check the candidates and their respective submissions with a view to excluding any candidates that, at their discretion, would not meet the criteria set out in the 2014 Regulations or any standards, guidance or code of practice issued by the Pensions Regulator from time to time. The Review Panel will then allocate the Employer Member(s) among the employers in order to ensure they are broadly representative of the different types of employer body in the Fund(e.g. local authorities, education establishments, charities etc).

3.5 Where there are more candidates than vacancies, the Scheme Manager will then facilitate the election of the Employer Member(s). Such election(s) may take place at a meeting called and arranged by the Scheme Manager or through the form of an electronic or other remote voting system. The Employer Member(s) will be required to be elected by a majority of the votes cast (or if more than one member is to be appointed the individuals receiving the most votes in descending order to fill the number of vacancies). In the event of a tied vote, the Independent Professional Observer will have a casting vote to determine which candidate is appointed to the role. Where only one candidate was originally put forward for the role, the Scheme Manager will proceed to appoint that individual to the relevant role without the need for an election.

Employee Members

3.6 Once the trade unions representing members of the Funds have put forward their candidates, the Scheme Manager will send the list of prospective candidates to the Review Panel for review with regard to the obligations on the Scheme Manager pursuant to Regulations [7(1)] (*conflicts of interest*) [and [6(1)] and 10 (*requisite training and development*)] of the 2014 Regulations. The Review Panel will check the candidates and their respective submissions with a view to excluding any candidates that, at their discretion, would not meet the criteria set out in the 2014 Regulations or any standards, guidance or code of practice issued by the Pensions Regulator from time to time. The Scheme Manager will then proceed to arrange for the appointment of the appropriate candidates as Employee Member(s) of the Pension Board and liaise with the trade union bodies collectively in relation to any candidate that did not meet the criteria set out in the 2014 Regulations and/or the Pensions Regulator's guidance (with a request for a further candidate to be put forward in accordance with the procedures set out herein). In the event of there being more candidates than vacancies, the Scheme Manager will then facilitate the election of the Employee Member(s).

4. PENSION BOARD: APPOINTMENT

4.1 Candidates selected to be either Employer Member(s) and/or Employee Member(s) will then be appointed to those roles by the Scheme Manager or (following the establishment of the Pension Board) by the Pension Board itself on receiving notice of the selected individuals from the Scheme Manager.

4.2 Employer Members and Employee Members will otherwise carry out their role and be appointed and removed in accordance with the Constitution**[[1]]**.

4.3 Any individuals appointed as member of the Pension Board (including any pre-approved alternates) will require to have read, understood and signed the Lothian Pension Funds' Code of Conduct prior to taking up their role.

[1] **NOTE:** we are checking whether appointments to a body of this nature would require approval by the Council under the current internal governance arrangements/Terms of Reference.

Lothian
PENSION FUND

4.4 Members of the Pension Board (including any pre-approved alternates) will be required to have completed the necessary induction training from the Scheme Manager prior to taking up their role.

4.5 Any member of the Pensions Committee will not be eligible for appointment as a member of the Pension Board.

Approved by: **The City of Edinburgh Council** (as administering authority of the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund)

On: [ ] 201[ ]

The Lothian Pension Fund

Pension Board Constitution

Introduction

The City of Edinburgh Council (the "**Scheme Manager**") is required to establish a Pension Board for the purposes of facilitating the administration of the Lothian Pension Fund, the Lothian Buses Pension Fund, the Scottish Homes Pension Fund and any other Local Government Pension Scheme that it may administer from time to time (the "**Funds**"). The Pension Board has been established under the provisions of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014 (the "**2014 Regulations**") and the Public Service Pensions Act 2013.

Further to Regulation [6(6)] of the 2014 Regulations, this constitution (the "**Constitution**") shall supersede any model or other constitution regarding the operation and functioning of the Pension Board associated with the Funds (the "**Pension Board**").

1. Remit and exercise of functions

1.1 The Pension Board shall carry out its compliance functions ("**Functions**") strictly within the remit set out in Regulation [5] of the 2014 Regulations.

1.2 Members of the Pension Board ("**Members**") shall have access to and receive all papers provided to the Scheme Manager's Pensions Committee (the "**Pensions Committee**") (and any sub-committee) for the purpose of their carrying out the Functions. Members may requisition additional reports from the Scheme Manager in accordance with Regulation [8(3)] of the 2014 Regulations to the extent reasonably required for the proper performance of their Functions.

1.3 Members shall have a collective duty to act independently in the interests of the members and employer bodies in the Funds and also the taxpayers. [In most cases the interests of these stakeholders in the Funds will be aligned, but where they do diverge the Members shall use their reasonably exercised discretion to take a balanced and proportionate view of the interests of the respective stakeholders in the Funds in the context of the particular circumstances and having regard to any regulation or guidance issued by the UK Pensions Regulator.]

1.4 Members of the Pension Board shall not participate in the voting, decision making or other business of the Pensions Committee, or the operational activity of the Scheme Manager, other than to input to the discussion and/or consideration of matters by the Pensions Committee to the extent required and appropriate in the performance of their Functions.

2. Membership

2.1 The membership of the Pension Board will at all times consist of equal numbers of [trade union representatives (drawn from trade unions that represent the membership of the Funds)] ("**[Employee] Members**") and [local government] employer representatives [(drawn from scheduled or admitted bodies that participate in the Funds) ("**Employer Members**"] and will comprise:

a. [five] Employer Members; and
b. [five] Employee Members.

2.2 Members who are appointed to the Pension Board will at all times be required to:

a. demonstrate the relevant knowledge, skills and expertise to properly perform the Functions;
b. make all reasonable efforts to regularly attend the meetings of the Pension Board;
c. make appropriate contributions at Pension Board meetings in the performance of their Functions; and
d. comply with the Scheme Manager's Training and Attendance Policy (as amended from time to time).

2.3 To the extent that any Member does not comply with the competency criteria set out in paragraph 2.2 above, the Scheme Manager shall have the right to serve notice on the Pension Board to that effect. On receiving notice from the Scheme Manager, the Pension Board shall take action to remove the relevant Member and reappoint a suitable replacement, unless it can demonstrate to the Scheme Manager's reasonable satisfaction that such Member has or will be able to perform the Functions in compliance with such criteria.

2.4 Any Member may appoint a person to attend and act on his behalf as an alternate on the Pension Board, or any sub-committee of the Pension Board, provided always that such person has been pre-approved by a vote or written authorisation of a majority of the Pension Board and has the requisite knowledge, skill and expertise to perform the Functions. All other provisions of this Constitution shall, where appropriate, apply equally to alternate Members as if they were themselves Members.

2.5 At no time shall a Member be appointed or retained who is at that time also a member of the Pensions Committee.

2.6 Subject to paragraph 12 herein, no person may be appointed to the Pension Board that, in the Scheme Manager's sole discretion, has a Conflict of Interest. A **'Conflict of Interest'** being a financial or other interest which is likely to prejudice a person's exercise of the Functions as a Member, but does not include a financial or other interest arising merely by virtue of that person being a member of any of the Funds.

2.7 Advisors may attend meetings of the Pension Board at its direction and at its chairman's discretion as to numbers and, where the Pension Board and the Pensions Committee will meet concurrently, with the prior approval of the Convener of the Pensions Committee.

3. Meetings

3.1 Members participate in a meeting of the Pension Board where it has been called and constituted in accordance with this Constitution and the 2014 Regulations.

3.2 The Pension Board shall meet at least quarterly and, in the normal course, to coincide with the meetings of the Pensions Committee. While the statutory roles and function of the Pensions Committee and Pension Board are separate, normal practice will be that both bodies will meet at the same time to consider the same agenda, with the Convener of the Pensions Committee chairing the concurrent meeting.

3.3 A majority of the Pension Board may otherwise agree to hold meetings from time to time and will authorise [one of] the joint secretaries to issue notice of such a meeting and make the necessary arrangements.

3.4 No less than [7] days notice of a meeting of the Pension Board must be given to each Member, unless unanimously agreed by the Members, and will usually be given in writing (including in electronic form). Any papers to be considered at or in advance of a meeting of the Pension Board shall be circulated to the Members no less than [5] days before the meeting.

3.5 In determining whether a Member is participating in a meeting of the Pension Board it is irrelevant where any Member is or how they communicate with each other. If all of the Members participating in the meeting are not in the same place they may decide that a meeting is to be treated as taking place wherever any of them is.

4. Quorum for Members' meetings

4.1 At a meeting of the Pension Board, unless a quorum is participating, no proposal is to be voted on, except a proposal to call another meeting.

4.2 The quorum for a Pension Board meeting may be fixed from time to time by a decision of the Members, but it must never be less than [four] Members (comprising at least [two] Employer Members and [two] Employee Members), and unless otherwise fixed is [four] Members constituted in the manner set out herein.

4.3 If the total number of appointed Members for the time being is less than the quorum required, the Members must not take any decision other than a decision to fill any Member vacancies.

5. Chairing meetings

5.1 Members will appoint a Member to chair the meetings of the Pension Board during any meeting not held concurrently with a meeting of the Pensions Committee.

5.2 Where the Pension Board and the Pensions Committee meet concurrently the Convener of the Pensions Committee will chair the meeting and the chairman of the Pension Board may act as a spokesperson on behalf of the Pension Board.

5.3 The chairman of the Pension Board will be rotated on an annual basis so that it shall be held in alternate years by:

a. a person nominated by a majority vote of the Employer Members and subsequently appointed by the Pension Board; and

b. a person nominated by the majority vote of the Employee Members and subsequently appointed by the Pension Board.

5.4 Where the appointed chairman is not participating in a meeting of the Pension Board the participating Members must appoint one of themselves to chair it.

6. Decisions by Members

6.1 Subject to Regulation [9(1)] of the 2014 Regulations, decisions by the Members shall be made by either a majority approval at a meeting of the Pension Board or by way of a unanimous written resolution approved (through either signing of the resolution itself or agreement to it in writing by email) by all of the Members at that time.

6.2 If the number of votes for and against a proposal are equal the chairman shall have the casting vote, unless the chairman is otherwise excluded from participating in the relevant vote (e.g. should they have a conflict of interest etc.).

6.3 Where the Pension Board agree to invoke its right under Regulation [9(1)] of the 2014 Regulations to request that the Pensions Committee review a particular decision, such a request (except where the Pensions Committee and Pension Board agree that would not be appropriate) will be made within [10] days of that decision having been made by the Pensions Committee. The Pension Board will only request that a decision of the Pensions Committee be reviewed where it has reasonable grounds for such review, in accordance with Regulation [9(2)] of the 2014 Regulations [and that such grounds are within the remit of its Functions].

6.4 Where the Pension Board decides to publish any difference in views between it and the Pensions Committee pursuant to Regulation 9 of the 2014 Regulations, it shall provide the Scheme Manager with a written statement and give the Scheme Manager and the Pensions Committee [a reasonable period of time] to consider that statement and respond with any comments.

6.5 The Pension Board shall ensure, working together with the Scheme Manager, that any joint secretarial report published pursuant to Regulation [9(3)] of the 2014 Regulations does not include any:

a. incorrect, inaccurate, ambiguous or misleading statements; or
b. confidential or sensitive information, the disclosure of which may result in the Scheme Manager being in breach of contract or any applicable law or would be substantially to the financial or other detriment of the Funds and their stakeholders.

7. Delegation to individual Members and sub-committees

7.1 Members of the Pension Board may delegate Functions to a particular Member or a sub-committee of Members of the Pension Board for the purpose of attending any sub-committee of the Pensions Committee. It is anticipated that any such sub-committee of the Pension Board will contain a reduced number of Members proportionate to the relevant sub-committee being attended, but will at all times be constituted to have equal numbers of Employer Members and Employee Members. Decisions taken by any sub-committee must follow the procedures, in as far as they are applicable, of this Constitution which govern decisions by the Pension Board.

8. Secretaries

8.1 The Scheme Manager and the Employee Members shall each appoint a [joint secretary] of the Pension Board.

8.2 The Scheme Manager shall provide reasonable and appropriate support in order to assist with the administration of the Pension Board, such as the preparation of minutes of meetings (including any decisions, noting conflicts, attendance etc.) of the Pension Board whether held separately or at the same time as the Pensions Committee meetings.

9 Appointment and removal of Members

9.1 Any person who is willing to act as a Member and has the requisite level of knowledge, skill and expertise may be appointed as a Member in accordance with the Scheme Manager's Appointment and Nomination Policy (as amended from time to time).

9.2 A person ceases to be a Member as soon as:

a. that person dies or resigns as a Member;
b. that person is convicted of a serious criminal or civil offence or is declared bankrupt;
c. that person has become physically or mentally incapable of acting as a Member and may remain so for more than three months; or
d. the Scheme Manager has issued a notice to the Pension Board pursuant to paragraph 2.3 of the Constitution which the Scheme Manager has confirmed is not to be withdrawn.

9.3 A Member may also be removed with the unanimous approval of all other Members of the Pension Board.

10 Amending the Constitution

10.1 This Constitution may be amended by the agreement of no less than [80]% of the Members of the Pension Board and with the written consent of the Scheme Manager. Any amendments to the Constitution must be made in compliance, and not conflict, with the 2013 Act (where appropriate) and the 2014 Regulations.

10.2 Where the Pension Board has agreed to amend the Constitution in accordance with paragraph 10.1 above, but the Scheme Manager has refused to give its consent, the matter may be referred to the National Scheme Advisory Board in Scotland for mediation and adjudication pursuant to Regulation [6(7)] of the 2014 Regulations.

11 Costs and Members' expenses

11.1 The Pension Board will liaise with the Scheme Manager to assist the Scheme Manager in budgeting for the likely costs of operating the Pension Board in the subsequent financial years. Any costs associated with the operation and administration of the Pension Board (including the costs of any advisers to be appointed by the Pension Board) will be borne by the Funds, provided that the Pension Board has sought prior approval of the Scheme Manager before incurring such costs.

11.2 The Funds also shall pay and/or reimburse the Members for any reasonable expenses properly incurred in connection with their attendance at meetings of the Pension Board, any sub-committee or training event held in accordance with the Scheme Manager's Training and Attendance Policy provided that the Scheme Manager's prior approval is sought before incurring any such expenses (other than routine costs associated with travelling to and from Pensions Committee meetings) and appropriate receipts are sent to the Scheme Manager evidencing the expenses being claimed for.

12 Conflicts of interest

12.1 Members must declare any potential conflicts of interest at the start of any meeting of the Pension Board.

12.2 If the proposed decision of the Members is particularly concerned with an actual or proposed transaction or arrangement with a person or entity in which the Member is interested, that Member is not to be counted as participating in the decision-making process for quorum of voting purposes, except where:

a. the remaining Members in attendance unanimously vote that the Member should participate;
b. the Member's interest cannot reasonably be regarded as likely to give rise to a conflict of interest; or
c. the Member's conflict of interest arises simply by virtue of its role as a representative of either a member or employer group or body.

13. Records of decisions

13.1 Minutes of each meeting of the Pension Board will be prepared, including where the Pension Board and Pensions Committee meet concurrently, which shall include a record of the time and place of the meeting, those attending, any conflicts of interest noted and all decisions made at such meetings by the Members.

13.2 The draft minutes will be approved at the next meeting of the Pension Board, signed by the chairman and copy circulated to the Pensions Committee and the Scheme Manager.

13.3 Notwithstanding the process to prepare and agree the minutes, a summary of the decisions taken at each meeting of the Pension Board will be circulated to the Members and the Pensions Committee within [10] days of that meeting taking place.

13.4 Copies of the agreed minutes of Pension Board meetings shall be retained by [the Scheme Manager] for no less than [12] years from the date of the decision.

[14 Liability of Members]

[*To be considered in due course based on final regulations and further guidance from the Pensions Regulator.***]**

Approved by: **The City of Edinburgh Council** (as administering authority of the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund)

On: [ ] 201[ ]

The Lothian Pension Fund

Pensions Committee and Pension Board

Training and Attendance Policy

INTRODUCTION

Pensions Committee: The City of Edinburgh Council ("**CEC**" or "**Scheme Manager**") operates a Pensions Committee (the "**Pensions Committee**") for the purposes of facilitating the administration of the Lothian Pension Fund, the Lothian Buses Pension Fund, the Scottish Homes Pension Fund and any other Local Government Pension Scheme that it may administer from time to time (the "**Funds**"). Members of the Pensions Committee owe an independent fiduciary duty to the members and employer bodies in the Funds and the taxpayer. Such members are therefore required to carry out appropriate levels of training to ensure they have the requisite knowledge and understanding to properly perform their role.

Pension Board: The Scheme Manager is also required to establish and maintain a Pension Board (the "**Pension Board**"), for the purposes of assisting with the ongoing compliance of the Funds. The Pension Board is constituted under the provisions of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014 (the "**2014 Regulations**") and the Public Service Pensions Act 2013. Members of the Pension Board should also receive the requisite training and development to enable them to properly perform their compliance role.

This policy sets out the requirements and practicalities for the training of members of both the Pensions Committee and the Pension Board. It also provides some further detail in relation to the attendance requirements for members of the Pension Board and in relation to the reimbursement of expenses.

1. Training of the Pensions Committee and Pension Board Members

1.1 New members of the Pensions Committee and/or Pension Board must attend an induction course by the Scheme Manager before taking up their role. This course will provide an overview of the structure and operation of the Funds and insight into the roles and responsibilities of the members on their respective body. The purpose of this training is to allow the Pensions Committee members to consider and decide on all matters relating to the Funds, involving complex investment and pension matters, and to enable Pension Board members to assist the Pensions Committee in providing input on the compliance implications associated with such matters.

1.2 Members of the Pensions Committee and Pension Board will also be required to undertake no less than [three days (21 hours)] of training in each calendar year. This training obligation will be met through the following:

- Internal training events designed specifically for this purpose and to cover a range of pension administration and investment matters.
- External events for Funds' stakeholders, such as the annual employer seminar and finance briefing.
- Seminars and conferences offered by industry wide bodies, such as the LAPFF, LGC and NAPF.
- Seminars and training events offered by the Fund's external professional advisers, investment managers and other service providers.
- Online training, including that provided by the Pensions Regulator (e.g. the Pensions Trustee and LGPS Toolkits) from time to time.
- Other training deemed appropriate by the Scheme Manager from time to time.

1.3 In designing a programme of training for the members of the Pensions Committee and the Pension Board the Scheme Manager will have regard to Regulation [10] of the 2014 Regulations, the Pensions Regulator's codes of practice and guidelines, the CIPFA Guidelines on the Principles for Investment Decision Making in the Local Government Pension Scheme, and the CIPFA Knowledge and Skills Framework issued from time to time.

1.4 Members of the Pension Board may be required to attend further specific training which will focus on any regulatory, legislative or other technical updates which they should be aware of in the performance of their compliance role.

2 Training of the Secretaries of the Pension Board

2.1 Any joint secretary of the Pension Board appointed by the trade unions pursuant to the Constitution must also attend an induction course which provides an overview of the structure and operation of the Funds by the Scheme Manager and focuses on any key matters associated with the ongoing governance and administration of the Funds.

3 Attendance of the Pension Board

3.1 Section [2.2 (b)] of the constitution of the Pension Board (the "**Constitution**") requires members of the Pension Board to make all reasonable efforts to regularly attend the meetings of the Pension Board. To provide further clarity, and pursuant to section [2.2(d)] of the Constitution, the Scheme Manager requires that members of the Pension Board must attend a minimum of [three?] out of the four quarterly meetings of the Pension Board which will be held concurrently with the quarterly meetings of the Pensions Committee. In addition, members of the Pension Board should use all reasonable efforts to attend any meetings of the Pension Board held out-with the main cycle of quarterly meetings and, in any event, shall not miss any more than two such additional meetings in any calendar year.

3.2 If a Pension Board member is unable to attend a Pension Board meeting, any named alternate should attend in their place pursuant to the Pension Board's Constitution.

3.3 For these purposes, an alternate attending on behalf of the Pension Board member pursuant to the Pension Board's Constitution, notwithstanding that for the purposes of the meeting such alternate shall be counted as attending as if the Pension Board member had attended, shall not be deemed to count towards that member's attendance record.

4 Substitute Members of the Board

4.1 Substitute or alternate members of the Pension Board that are pre-approved pursuant to section [2.4] of the Constitution ("**Alternates**") may attend meetings of the Pension Board. Regulation [6(2)] of the 2014 Regulations requires that any such Alternates should have *undergone the requisite training and development to inform their role*.

4.2 Alternates will therefore be required to attend the same induction course as Pension Board and Pensions Committee members.

4.3 Alternates will also require to attend no less than [15] hours of relevant training each year.

5. Monitoring and Reporting

5.1 Each member of the Pensions Committee and Pension Board, and any Alternates, will inform the Scheme Manager of relevant training attended from time to time.

5.2 A report will be submitted to the Pensions Committee annually highlighting the training and attendance of each member of the Pensions Committee and Pension Board and any Alternates.

5.3 Where the Scheme Manager has a concern that a member of the Pension Board (or any Alternate) is not complying with the requisite training or attendance requirements it may serve a notice on the Pension Board, pursuant to section [2.3] of the Constitution, requiring the Pension Board to remove that member and seek to appoint a replacement. The Pension Board shall be given reasonable opportunity to review the circumstances and, where appropriate, liaise with the Scheme Manager with a view to demonstrating that such member will be able to continue to properly perform the functions required of a member of the Pension Board and request that the Scheme Manager withdraw the notice. Any decision to withdraw such notice will be made by the Scheme Manager at its sole discretion.

5.4 This training policy will be reviewed on an ongoing basis by the Scheme Manager.

6. Reimbursement of expenses

6.1 All reasonable expenses properly incurred by members of the Pensions Committee, appointed pursuant to the Nominations and Appointments Policy, and the Pension Board necessary for the performance of their roles will be met by the Funds, provided that the Scheme Manager's prior approval is sought before incurring any such expenses (other than routine costs associated with travelling to and from Pensions Committee meetings) and appropriate receipts are sent to the Scheme Manager evidencing the expenses being claimed for.

Approved by: **The City of Edinburgh Council** (as administering authority of the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund)

On: [ ] 201[ ]

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Reform of the Local Government Pension Scheme in Scotland and Regulatory Update (excluding Governance)

Item number	5.6
Report number	
Executive/routine	
Wards	All

Executive summary

Good progress continues to be made towards implementation of a new Local Government Pension Scheme (LGPS) in Scotland from 1 April 2015.

Coverage of the LGPS in England and Wales and other pensions regulatory matters is included for reference.

Further regular updates will be provided to Pensions Committee.

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	

Reform of the Local Government Pension Scheme in Scotland and Regulatory Update (excluding Governance)

Recommendations

1.1 Committee is requested to:

- Note the report;

Background

Reform of the LGPS in Scotland 2015

2.1 This report is the latest in a series of regular updates on public service pension reform and specifically the implications of fundamental change to the design and governance of the Local Government Pension Scheme in Scotland.

2.2 A separate report on Governance matters is provided elsewhere on the agenda.

Main report

LGPS 2015 - Payroll and Human Resources (HR) Guidance

3.1 In September the Payroll Guide for LGPS 2015 in Scotland was published on the LGPS Regulations website. An updated version was added on 30 October 2014. This guide sets out the requirements for payrolls in respect of the Local Government Pension Scheme (Scotland) 2015 (LGPS), effective from 1st April 2015. It is intended to inform payroll providers and employers of the minimum information needed to effectively manage the 2015 Scheme (and its interaction with the 2009 Scheme). The link to this website is shown later in this report under “Background reading / external references”.

3.2 In November 2014, a “walkthrough” seminar with LGPS employers to discuss HR management requirements was convened by CoSLA, It is anticipated that the HR Guide will be released in the coming weeks. It should be noted that suitable guidance on the application of pay protection for a member is being finalised by the Scottish Local Government Pensions Advisory Group (SLOGPAG) and it is expected that this will be issued as an appendix to the HR guide. In due course, administration guides (similar to those produced in England and Wales for LGPS 2014) will also be made available on the LGPS Regulations website.

LGPS 2015 - Communications

3.3 Work on member and employer communications material continues to be progressed by the SLOGPAG Communications Sub-Group. All information currently approved by SLOGPAG for public release is available though the website www.scotlgps2015.org. Within the suite of Scotland wide-communications resources, the following are now available for all Funds which we are using to complement the fund's own bespoke communications:

- Video for members
- Modeller showing estimate of benefits from April 2015 onwards
- Presentation for employer and member events
- Five in-depth topic briefings – available on the website
- Series of e-newsletters linked to topic briefings to be issued over the period to the change (newsletters can also be for use on noticeboards), including coverage of the complicated issue of pensionable pay and other protections
- Poster highlighting the changes, what is staying the same and also protections.
- Councillor briefing (for their scheme)

Lothian Pension Fund specific communications

3.4 The Fund is using the Scotland-wide material as a basis for communications directly to members and via employers in addition to Fund specific messages and events.

3.5 The Fund has provided regular updates to employers and members during the reform of the LGPS including updates on the Fund's website, newsletters and employer briefings. A four page newsletter was also issued to members in August 2014. E-newsletters publicising the Scheme changes, modeller and briefing series have also been circulated.

3.6 Also, LPF held its Annual Seminar for employers on 4 December 2014. The Fund's actuary provided a presentation and commentary on the actuarial valuation 2014, including coverage of the impact of the new LGPS 2015 on the overall level of funding.

3.7 On 21 November 2014, LPF provided a training workshop for its employers. This session was provided by a pensions specialist from the Local Government Pensions Committee (LGPC). The purpose was to facilitate understanding by employers of their obligations for LGPS2015 and was targeted at payroll and HR officers. The workshop proved very popular with over seventy employer representatives in attendance.

3.8 The following communications methods will be used in the coming months:

- Fund e-newletters linking to briefings on the Scotland-wide site sent directly to individual member where e-mail address is held or via employer
- Video for use by employers at workplace or team meetings
- Presentation to be held at a central venue for all employers in March or April 2015
- Presentations at larger employer workplaces from January 2015
- Staff newsletter article /payroll message /team briefing presentation - for use by the employer
- Lothian Pension Fund website relaunch with updated information.

Staff training

3.9 Supplementing regular “in-house” briefings on the LGPS 2015, LPF has secured places for six staff to attend detailed workshop training for Administering Authority “pension practitioners” from January 2015. These workshops, which again are provided by specialists from LGPC, are solely aimed at administering authority staff, particularly those involved in the day-to-day administration of the LGPS. LPF staff attending these events will then provide suitable feedback and tuition to colleagues.

Software systems

3.10 An update of the Fund’s pensions administration system to reflect the changes to the scheme prior to April 2015 will be vital to ensure continued service to members.

3.11 As is customary, the supplier of the pension administration system intends to issue the updated modules in test format to selected administering authorities to provide validation prior to live implementation. Details of this programme are expected shortly. Training webinars on optimal usage of the administration system are also being provided by the supplier on a regular basis.

3.12 Similarly, the supplier of the secure data transmission portal has undertaken essential development work to ensure compliance with the requirements of the new scheme. A programme of testing is underway at present.

3.13 CoSLA initiated consultation with HR and payroll system providers some months ago in order to raise awareness of additional data demands and potential system re-configuring. It is expected that the production of detailed guidance and supplementary employer communication and engagement should prove beneficial in ensuring implementation readiness. Ultimately, however, compliance with the requirements of LGPS 2015 is a statutory responsibility of each individual employer.

Actuarial factors

3.14 The Government Actuary's Department (GAD) will be required to issue updated actuarial factors to ensure the new benefit structure of the LGPS 2015 is appropriately reflected in pension calculations by administering authorities. Examples include early and late retirements, transfer values and pension sharing. SLOGPAG has requested that this work is suitably prioritised by GAD to avoid service interruption.

Other Regulatory Updates

Automatic Enrolment Earnings Thresholds Review and Revision 2015/16

3.15 On the 25 November 2014, consultation by the Department for Work and Pensions (DWP) closed on revised proposals for the automatic enrolment thresholds for 2015/2016. "Automatic enrolment into a workplace pension scheme is designed to target moderate to low earners who are either not saving or not saving at least a minimum for their retirement. If the trigger is too high then people who should be saving, or should be saving more may lose out. Set it too low and people for whom it makes little sense to save for retirement because they probably cannot afford to save and are very likely to receive a high replacement rate from the state, may be driven to opt out."

3.16 The potential impact upon the LGPS cannot yet be determined and would obviously be influenced by the level of opting-out of membership and the uptake of the 50/50 option in the new scheme.

Taxation of Pensions Bill

3.17 Following the Government's recent consultation on "Freedom and Choice in Pensions", the Taxation of Pensions Bill, introducing the changes to tax legislation required to enable flexible access to pensions, was placed before Parliament. Some concerns were raised, including the potential that consumers would be exposed to heightened risk of pension liberation scams as a result of the new freedoms. As previously advised to Committee, the potential impact for the LGPS could result from transfers from the LGPS to defined contribution (DC) schemes.

3.18 The Department for Communities and Local Government have recently announced a series of amendments to the Pension Schemes Bill, three of which affect public service pension schemes :-

- The requirement to take independent financial advice when transferring from a defined benefit to a defined contribution scheme (as opposed to the "Guidance Guarantee" that will be offered to those in defined contribution arrangements as they approach retirement);
- A ban on transfers out of unfunded public service schemes to a defined contribution scheme as previously announced by the government, and

- A new safeguard that will give Ministers a power to reduce CETVs in funded public service pension schemes, should it prove necessary to protect the taxpayer.

State Pension Scheme Communications

3.19 On 4 October 2014, the Department for Work and Pensions (DWP) launched a new campaign called "Your future, your pension". This is aimed at ensuring that today's workers understand the new State Pension Scheme being introduced in April 2016 and what the reforms mean. As part of this campaign, advertisements will be appearing later this year. In addition a new service giving people a personalised written statement of what they can expect to receive under the new system (based on their work history and National Insurance (NI) contributions to date) has been launched. At the moment it is available to approximately 2.5 million people who will reach State Pension age in the first five years of the new scheme (currently between April 2016 and August 2021). The service will be expanded gradually over the next 18 months, eventually becoming available to all working age people.

LGPS in England and Wales – Shadow Scheme Advisory Board – Annual Report 2013

3.20 Changes to public sector pensions will result in the set up of a Scheme Advisory Board for each Scheme. For the LGPS in England and Wales, a Shadow Scheme Advisory Board has been set up ahead of the formal adoption in April 2015.

3.21 On 4 November 2014, the Shadow Scheme Advisory Board published the first Annual Report 2013 for the LGPS in England & Wales. The aim is to provide information about the LGPS in England and Wales to its members, employers and other stakeholders. The aggregate information in the Report is based on the annual reports as at 31 March 2013 supplied by the 89 individual funds.

3.22 It is worth noting that the Chair explicitly draws attention to the £47bn funding deficit in the LGPS and says that the Board is ‘actively developing proposals’ to tackle this deficit to improve the sustainability of the LGPS and its future funding levels.

3.23 The 2013 Annual Report is a pilot for a more comprehensive 2014 Annual Report to be published in 2015. In a move to more transparent disclosure in the LGPS, the Board is developing a range of financial and non-financial ‘health’ indicators so that it can assess and benchmark the ‘health’ of the LGPS as a whole (relative to other large private and public sector funds) as well as the relative ‘health’ of individual LGPS funds. The financial analysis will be based on the 2013 triennial valuation results using consistent assumptions across all funds and will look at, amongst other things, current levels of deficit repayment, actual historic returns compared with a fund's required future investment returns and deficit spread periods.

3.24 This update on the Shadow Scheme Advisory Board is provided to Committee purely for information as the regulatory regime is entirely separate from that pertaining to the LGPS in Scotland. Nevertheless, the issues arising may similarly prevail in Scotland and may well be the focus of attention of the Scottish Scheme Advisory Board, once this is established from 1 April 2015.

Measures of success

4.1 This report is purely advisory at this stage.

Financial impact

5.1 There are no financial implications arising directly from this report. However, changes to the LGPS in Scotland will have financial consequences for Lothian Pension Fund and Lothian Buses Pension Fund, participating employers and members. These will be addressed in future reports to Pensions Committee.

Risk, policy, compliance and governance impact

6.1 This report is purely advisory at this stage. There is a risk, however, that taxation changes for defined contribution pension schemes may have an impact on the cash-flow, investment and funding of the pension funds.

Equalities impact

7.1 There are no adverse equalities impacts arising from this report. Changes to the design of the LGPS are subject to Equality Impact Assessment by the Scottish Government.

Sustainability impact

8.1 There are no adverse sustainability impacts arising from this report. The public Service Pensions Act 2013 aims to make pensions more sustainable.

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds. Lothian Pension Fund is committed, on an ongoing basis, to keeping its employers and members fully informed of all the key developments on reform of the LGPS in Scotland.

Background reading / external references

The Payroll Guide for LGPS 2015 in Scotland can be viewed at:

http://www.lgpsregs.org/index.php/scotland/scot-hr-payroll-guides/lgps2015-payroll-guide.

Scotland wide communications for the LGPS 2015 is provided at: www.scotlpgs2015.org.

The DWP consultation on Automatic Enrolment Earnings Thresholds Review and Revision 2015/16 can be found at:

www.gov.uk/government/uploads/system/uploads/attachment_data/file/363705/automatic-enrolment-earnings-thresholds-2015-2016.pdf.

The Shadow Scheme Advisory Board's Annual Report 2013 for the LGPS in England & Wales is available here.

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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	

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Pension Fund Cost Benchmarking

Item number	5.7
Report number	
Executive/routine	
Wards	All

Executive summary

The purpose of this report is to inform Committee of summary conclusions of the benchmarking of investment for Lothian Pension Fund and pensions administration costs for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.

The report on investment costs relies on data provided by CEM, an independent provider of benchmarking data. Its database is comprised of 357 global pension funds. CEM concludes that Lothian Pension Fund's costs are low compared with those of the global peer group. This is almost certainly due to the Fund's 'implementation style' – the Fund manages a relatively high percentage of assets internally compared with the universe of pension funds.

Pension administration cost per member for this Council (£24.90) has been maintained at a similar level for the last few years and appears to be within the expected range, although this is higher than the selected local authority peer group.

Qualitative assessment of performance for both investment and pension administration is difficult to ascertain given the lack of readily comparable statistics.

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	

Report

Pension Fund Cost Benchmarking

Recommendations

1.1 Committee is requested to:

- Note the report;
- Note that the CEM Investment Benchmarking Analysis and the CIPFA Pensions Administration Benchmarking 2014 comparator reports have been provided, on a confidential basis, to the Convener of the Pensions Committee, Convener of the Pensions Audit Sub-Committee and the Independent Professional Observer.

Background

2.1 The annual report 2013/14 for the pension fund identifies £31million of costs, with investment costs representing by far the largest proportion of the Fund's total expenses.

2.2 Benchmarking can be a helpful tool to help drive improvements and deliver value for money. It is intended that participation in the benchmarking of service provision should facilitate:

- Comparison between the costs and performance;
- Provision of evidence to support decisions on budget and improvement and thereby enhance customer satisfaction;
- Sharing of information and ideas with peer(s)
- Review of LPF performance trends over time.

2.3 In an effort to better understand its investment expense base, Lothian Pension Fund has contributed to CEM's database for the last two years. CEM's global database comprises 357 funds representing £5.0 trillion in assets, three fifths of which are based in North America. It includes 35 UK pension funds with aggregate assets of £196bn. The size of the funds range between £30 million and £510 billion. The median fund size was £2.9bn, which compares with Lothian Pension Fund's assets under management of £4.3bn at 31 December 2013. However, care should be taken in deriving conclusions from the headline data. CEM itself states that "being high or low cost is neither good nor bad". What matters is whether a pension fund is receiving sufficient value for the costs incurred. This is reflected in the long term returns of pension funds, net of costs.

2.4 Chartered Institute of Public Finance and Accountancy (CIPFA) pensions administration benchmarking club has been used for a number of years to assess the costs of administration of the Lothian Pension Fund, Lothian Buses Pension Fund and the Scottish Homes Pension Fund. The outputs and analyses have served to supplement internal performance management information.

Main report

CEM Investment Cost Benchmarking Analysis

3.1 CEM aims to provide comparable data but is unable to capture all investment costs from all funds. Accordingly, it excludes transaction costs and private asset performance fees from its analysis. For this reason, and also because the data is collected on a calendar year basis rather than a financial year basis, the actual costs differ from those reported in Lothian Pension Fund's annual report.

3.2 CEM calculates a benchmark cost for Lothian Pension Fund reflecting the Fund's size, asset mix and domicile. Lothian's actual cost of approximately 0.50% was below the benchmark cost of 0.59%. The 0.09% difference amounts to approximately £3.5m per year.

3.3 CEM concludes that the primary reason for costs being low compared with the benchmark is almost certainly 'implementation style' – a relatively high percentage of assets are internally managed and fund-of-fund usage is less than average. External active management tends to be much more expensive than internal management, while fund-of-funds tend to be the most expensive type of external management.

CIPFA Pensions Administration Benchmarking Club

3.4 The CIPFA Pensions Administration Benchmarking Club aims to collect the transactional volumes and processing costs for administering members' LGPS benefits (i.e. excluding investment) using standard definitions. "Employing authority work" and any work associated with the administration of non-LGPS pensions are excluded.

3.5 Each administering authority has scope to select a suitable peer group for the "comparator report" and also the submission by any individual LGPS administering authority is also available through the club database "interactive" report. The selected peer group comprises similar sized English and Welsh authorities, but also including some from Scotland. In total, nineteen Funds are included.

3.6 CIPFA has stated that, in order to protect its commercial interests, its report "Pensions Administration Benchmarking Club 2014" "cannot be put in the public domain. It is for internal uses only within the authority....and for contacting and communicating with other members of the club". Accordingly, the full comparator and interactive reports have been provided, on a confidential basis, only to the Convener of the Pensions Committee, Convener of the Pensions Audit Sub-Committee and the Independent Professional Observer.

3.7 It is emphasised that it would be incorrect to derive definitive conclusions on the basis of apportioned costs. This is an inherent issue given the scale of central support costs which are typically apportioned to the pension fund by the host Councils, the extent of co-provision of employer services and also the bases of overhead apportionment to the pension administration function, as distinct from other activities within the Fund Accounts.

3.8 Recognising this caveat, summary findings on costs and other observations on differences in the make-up of the Fund are as follows:

- LPF cost per member of £24.90 is within the range of the 18 comparable funds, £14.85 to £27.23. However LPF cost is higher than the peer group average (£20.28);
- Cost per member for LPF has been maintained at a similar level for the last few years. LPF cost and the average from a similar peer group from 2008/09, were £24.39 and £19.86 respectively;
- Staff costs (£13.34 per member for LPF) show similar results to those of total costs;
- Active members represent a higher percentage of overall membership for LPF than the peer group average, but not significantly so. The proportion of pensioners to total membership is again higher, with the consequence being that the proportion of deferred members is lower than that of the typical fund. These factors would tend to increase pension administration and payroll workload;
- Previous benchmarking reports have showed LPF as having the highest number of employers (in 2008/09, approximately 170 compared to an average of 105). Recently in England, the average number of employers has increased significantly with the inclusion of academy schools as separate entities and now LPF's number of employers is broadly comparable with the average; and
- LPF's staff turnover was low in the year to 31 March 2014 relative to other funds although it should be noted that LPF turnover has increased significantly in 2014/15.

Performance Benchmarking

3.9 Qualitative assessment of performance for both investment and pension administration is difficult to ascertain given the lack of readily comparable statistics.

3.10 CEM highlights that investment costs should be taken in the context of a fund's long term net returns. However, relevant comparisons of long-term returns are not readily available.

3.11 For pension administration, fewer than half the peer group, including LPF, have provided “industry standard performance indicators” to CIPFA. Work is being progressed to ensure that this can be provided in future.

Pensions Administration - Service Improvement Initiatives

3.12 Benchmarking reports in recent years have showed higher payroll costs for LPF compared to a peer group. This was one of the drivers behind the transfer of the payroll service in 2013 from the Council’s payroll system to the pension administration system. Payroll cost per pensioner is now broadly in line with the average.

3.13 Efficient electronic transfer of member data has also been the focus over recent years, including the recent implementation of PensionsWeb, which has helped to improve efficiency as well as customer service.

3.14 Lothian Pension Fund is actively engaged on the matter of consistency of performance indicators with the pension administration supplier in order to facilitate performance reporting on a consistent basis in future. From April 2014, Lothian Pension Fund has revised its performance management information in order to best comply with The Pensions Regulator and CIPFA’s requirements. Comparison with other funds should be available for 2014/15.

3.15 Officers of the Fund continue to learn from other pension funds on a regular basis including site visits to specific funds as well as attending regular meetings of the Scottish Pensions Liaison Group.

3.16 The need to focus on continuous improvement to the pensions administration service is recognised. The Fund intends to review its pensions administration procedures to ensure continuing alignment to best practice and also reinforce performance management where appropriate. This will include further liaison with other LGPS administering authorities. Synergies with current initiatives being undertaken by Corporate Governance Directorate with regard to the maintenance of member records and also the potential for channel-shifting to more efficient web-based self-service methods will be explored.

Measures of success

4.1 Benchmarking of costs provides management information, which serves to inform the service planning and budgetary process of the three Lothian Pension Funds.

Financial impact

5.1 There are no financial implications arising directly from this report. Out of the pension funds' total cost of £31million for 2013/14, pension administration costs included in amounted to £2.014million, with the remaining largely attributable to investment. Continuous improvement initiatives will be met from the approved budget 2014/15.

Risk, policy, compliance and governance impact

6.1 The provision of summarised conclusions of benchmarking is intended to enhance the governance of the three Lothian Pension Funds.

Equalities impact

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

Sustainability impact

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

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading / external references

Not applicable.

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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	None

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Scottish Homes Pension Fund – 2014 Actuarial Valuation & Investment Strategy

Item number	5.8
Report number	
Executive/routine	
Wards	All

Executive summary

This paper presents the results of the 2014 actuarial valuation for the Scottish Homes Pension Fund. The funding level at 31 March 2014 was 88.8%, increased from 86.3% from the 2011 actuarial valuation.

The funding level remains below the target funding level (91.5% at March 2014) as prescribed in the funding agreement with Scottish Government. Therefore, contributions of £575,000 p.a. will be payable from April 2015 from the Scottish Government, in addition to payment of administration costs of £100,000 p.a.

Committee is also asked to approve a change to the investment strategy and the equity allocation of the Fund, with corresponding change in the bond allocation, dependent on the funding level. This is pending full review of strategy in 2015.

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	

Report

Scottish Homes Pension Fund – 2014 Actuarial Valuation & Investment Strategy

Recommendations

1.1 Committee is requested to:

- Approve the 2014 actuarial valuation for the Scottish Homes Pension Fund;
- Note that the funding level of the Scottish Homes Pension Fund at 31 March 2014 was 88.8% and Scottish Government will pay contributions of £675,000 per annum to the fund for the three years starting April 2015;
- Approve the revised investment strategy for the Fund as shown in paragraph 3.12.

Background

2.1 The City of Edinburgh Council took over the administration of the deferred and pensioner liabilities of Scottish Homes in July 2005. An agreement between the Scottish Government and the City of Edinburgh Council ('the Guarantee') was put in place in June 2005. The Scottish Government acts as the 'Guarantor' for the Fund liabilities.

2.2 The Scottish Homes Pension Fund is required by law to undertake an actuarial valuation every three years. The actuarial valuation of a pension fund has 3 main purposes:

- To assess whether the funding strategy and assumptions are appropriate;
- To assess the financial health of the pension fund;
- To set the future rates of contributions payable by the employer / guarantor.

2.3 The funding strategy for the Scottish Homes Pension Fund and the valuation methodology is set out in the Guarantee. The strategy assesses the funding level using prudent financial assumptions and sets target funding levels for the Fund at each actuarial valuation. It also sets out the conditions which will trigger contributions to be payable by the Scottish Government.

Main report

2014 Actuarial Valuation

3.1 The 2014 Actuarial Valuation report is provided in Appendix 1.

3.2 The table below summarises the financial position of the Fund at 31 March 2014.

Past Service Position	**2011**	**2014**
Past Service Liabilities, £M	144.1	153.5
Market Value of Assets, £M	124.3	136.3
Surplus / (Deficit), £M	(19.8)	(17.1)
Actual Funding Level	**86.3%**	**88.8%**
Target Funding Level	**89.5%**	**91.5%**

3.3 The Target Funding Levels (TFLs), as set out in the Guarantee, are 89.5% and 91.5% at 31 March 2011 and 2014 respectively. The Actual Funding Level (AFL) is therefore lower than the TFL at both this and the previous valuation date. This triggers a contribution of £575,000 p.a. from the Scottish Government, as Guarantor, under the terms of the Guarantee payable from April 2015. In addition, the Guarantor will pay £100,000 p.a. towards the cost of administration expenses. The Scottish Government will therefore pay a minimum of £675,000 p.a. for the years 1 April 2015 to 31 March 2018.

Investment Strategy

3.4 Pensions Committee approved the Investment Strategy 2012-17 for the Scottish Homes Pension Fund in October 2012. The funding agreement with the Scottish Government and the investment strategy are designed to reduce investment risk as the Fund is closed to new members and the liabilities will mature over the time.

3.5 As reported to Committee in June 2014, over the financial year 2013/14 the actual funding level moved closer to the target funding level and so the move to the long term strategy was accelerated. The current investment strategy is in line with the long term strategy which is shown in the table below.

Asset Class	**Current & Long Term Strategy Allocation 2012-2017 %**
Equities	30
Bonds	65
Property	5
Cash	0
TOTAL	**100**

3.6 Further work to reduce the risk within the Fund's equities was put on hold pending the review of the funding agreement with the Scottish Government.

3.7 Discussions regarding potential changes to the funding agreement have been held with the Scottish Government over recent months with the assistance of the fund's investment advisers. Options to change the funding approach to one where contributions would be determined by fund cashflows, rather than funding level, have been explored.

3.8 However, the Scottish Government would prefer that the 2014 actuarial valuation and contributions for the 3 years starting April 2015 are determined in accordance with the existing Guarantee. However, they would like to explore funding options further ahead of the 2017 actuarial valuation. Updates to the Committee will be provided in due course if this work progresses.

3.9 The Guarantee provides guidance on the investment strategy for the Fund including the expectation that the allocation to equities is reduced over time and the desire of the Scottish Government to 'lock away any surpluses that may occur over time by accelerating the transfer into bonds'.

3.10 The Actuary is currently in the process of updating the funding level estimate based on investment market movements since 31 March 2014. Internal estimates indicate that the funding level has improved further.

3.11 Work now is underway with the Investment Strategy Panel to review the investment strategy for the Fund within the constraints of the existing funding Guarantee.

3.12 Pending this review, Committee is requested to approve reductions in the equity allocation of the Fund, with corresponding increases in the bond allocation, dependent on the funding level as follows:

	Equity Allocation %	**Funding level**	**Note [1]**
	35	89.5%	2011 TFL
Current	30	91.5%	2014 TFL
	25	93.0%	2017 TFL
	20	94.5%	2020 TFL
	15	95.5%	2023 TFL
	10	96.5%	2026 TFL

[1] Target Funding Level as per the Guarantee

3.13 The intention is to continue to monitor the funding level and adjust the level of equities in the Fund if target funding level(s) are achieved. For example if the funding level increased to 94.5%, the equity allocation would be reduced to 20%. If the funding level fell to 89.5%, the equity allocation would be increased to 35%.

3.14 The review of the investment strategy for the Fund will be reported to Committee in the first half of 2015.

Measures of success

4.1 The Guarantee agreement with the Scottish Government sets out the target funding levels for the Scottish Homes Pension Fund every 3 years until 2044. Actual funding levels are measured against the target funding levels on a regular basis.

Financial impact

5.1 The funding strategy, together with the Guarantee from the Scottish Government, should ensure that the Fund has sufficient assets in the long term. The results of the actuarial valuation have a financial impact on the Scottish Government as guarantor. The actuarial valuation sets the contribution rates payable by the Scottish Government over the next 3 years.

Risk, policy, compliance and governance impact

6.1 The investment strategy of the pension fund is one of the main determinants of risk, in terms of volatility of funding level and contributions payable by the Scottish Government. The proposed change to the investment strategy seeks to reduce this risk as required in the Guarantee with the Scottish Government.

Equalities impact

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

Sustainability impact

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

Consultation and engagement

9.1 The Scottish Government has been consulted during the actuarial valuation process.

Background reading / external references

None.

Alastair Maclean

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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 – 2014 Actuarial Valuation Report for Scottish Homes Pension Fund

Hymans Robertson LLP has carried out an actuarial valuation of the Scottish Homes Pension Fund ("the Fund") as at 31 March 2014, details of which are set out in the report dated 4 December 2014 ("the Report"), addressed to City of Edinburgh Council ("the Client"). The Report was prepared for the sole use and benefit of our Client and not for any other party; and Hymans Robertson LLP makes no representation or warranties to any third party as to the accuracy or completeness of the Report.

The Report was not prepared for any third party and it will not address the particular interests or concerns of any such third party. The Report is intended to advise our Client on the past service funding position of the Fund at 31 March 2014 and employer contribution rates from April 2015, and should not be considered a substitute for specific advice in relation to other individual circumstances.

As this Report has not been prepared for a third party, no reliance by any party will be placed on the Report. It follows that there is no duty or liability by Hymans Robertson LLP (or its members, partners, officers, employees and agents) to any party other than the named Client. Hymans Robertson LLP therefore disclaims all liability and responsibility arising from any reliance on or use of the Report by any person having access to the Report or by anyone who may be informed of the contents of the Report.

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Scottish Homes Pension Fund
2014 Actuarial Valuation Report

HYMANS ROBERTSON

December 2014

Contents

1 Executive summary

Richard Warden
Partner and Actuary

Steven Scott
Actuary

We have carried out an actuarial valuation of the Scottish Homes Pension Fund ("the Fund") as at 31 March 2014.

The Scottish Government (previously known as the Scottish Executive) acts as the 'Guarantor' for the Fund liabilities. The valuation of these mature liabilities uses more prudent assumptions than those applied to other employers in the Lothian Pension Fund, as set out in the agreed Scottish Executive Guarantee dated June 2005. The results are presented in this report and summarised below.

Funding position

The table below summarises the financial position of the Fund at 31 March 2011 and 31 March 2014 in respect of benefits earned by members up to this date.

Past Service Position	31 March 2011 (£m)	31 March 2014 (£m)
Past Service Liabilities	144.1	153.5
Market Value of Assets	124.3	136.3
Surplus / (Deficit)	(19.8)	(17.1)
Funding Level	**86.3%**	**88.8%**

The Actual Funding Level (AFL) has improved to 88.8% since the previous valuation at 31 March 2011. This corresponds to a deficit of £17.1m at 31 March 2014.

The Target Funding Level (TFL), as set out in the Guarantee paper, is 91.5% at 31 March 2014. The AFL is therefore lower than the TFL at both this and the previous valuation date. This triggers a contribution of £575,000 p.a. from the Scottish Government, as Guarantor, under the terms of the Guarantee payable from April 2015. In addition, the Guarantor will pay £100,000 p.a. towards the cost of administration expenses.

2 Introduction

Purpose

We have carried out an actuarial valuation of the Scottish Homes Pension Fund ("the Fund") as at 31 March 2014. This is our report to the City of Edinburgh Council ('the Administering Authority') on the results of the valuation.

The deferred pensioners and pensioners of the Scottish Homes Pension Fund were transferred to the City of Edinburgh Council prior to the wind-up of the Scottish Homes Residuary Body. The City of Edinburgh Council assumed the management of its assets and liabilities from 1 July 2005.

The Scottish Government (formerly the Scottish Executive) acts as the Guarantor for the transferred liabilities. The Guarantor's intention is that over time the transferred assets together with any additional contributions required should be sufficient to fund the former Scottish Homes Pension Fund liabilities. However, it was agreed in-principle that the investment strategy should move towards having less exposure to volatile asset classes (e.g. equities) during the liability run-off. The liability run-off is expected to take a number of decades to complete, but a substantial part of the liability should be discharged over the first decade.

This valuation report complies with all of the relevant regulations and professional standards, as set out in **section 8**.

The figures in this report are based on our understanding of the benefit structure of the LGPS as at 31 March 2014, details of which are provided in **Appendix B**.

The results of the valuation are dependent on the quality of the data provided to us by the Administering Authority for the specific purpose of this valuation. This data is summarised in **Appendix D**.

As part of the valuation, assumptions must be made which are discussed in **section 3** as well as in **Appendix E.** Details of our valuation approach is covered in **Appendix C.**

The valuation results are then covered in the **section 4** with the required Guarantor contributions outlined in **section 5**.

We look at some of the risks the Fund faces in **section 6**

The valuation is just one aspect of the operation of the Fund, and related issues are covered in **section 7.**

In **Appendix F** we then set out the future contributions payable under the terms of the Guarantee paper.

Component reports

This document is an "aggregate" report, i.e. it is the culmination of various "component" reports and discussions, in particular:

- The data report (mentioned in **section 8**);
- The Initial Results report (dated 6 August 2014 which outlined the preliminary assumption proposals and whole fund results);
- The formal agreement by the Administering Authority of the actuarial assumptions used in this document, as per the Administering Authority's email dated 24 November 2014.
- The Operation of the Scottish Executive Guarantee paper dated 29 June 2005, confirming the approach to determining contributions payable to the Fund by the Scottish Government.

Note that not all of these documents may be in the public domain.

3 Assumptions

Assumptions must be made about the factors affecting the Fund's finances in the future. Broadly speaking, our assumptions fall into two categories – financial and demographic.

Demographic assumptions typically try to forecast **when** benefits will come into payment and what form these will take. For example, when members will retire (e.g. at their normal retirement age or earlier), how long they will then survive and whether a dependant's pension will be paid.

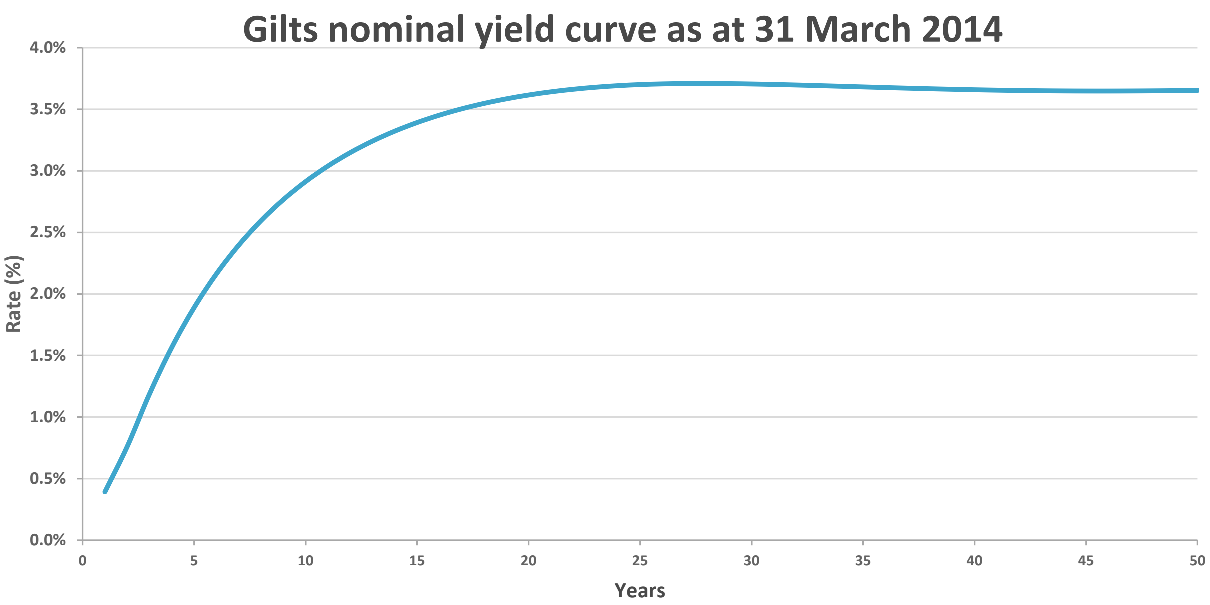
Financial assumptions typically try to anticipate the **size** of these benefits. For example, how members' pensions will increase over time. In addition, the financial assumptions also help us to estimate how much all these benefits will cost the Fund in today's money.

Financial assumptions

A summary of the main financial assumptions adopted for the valuation of members' benefits are shown below.

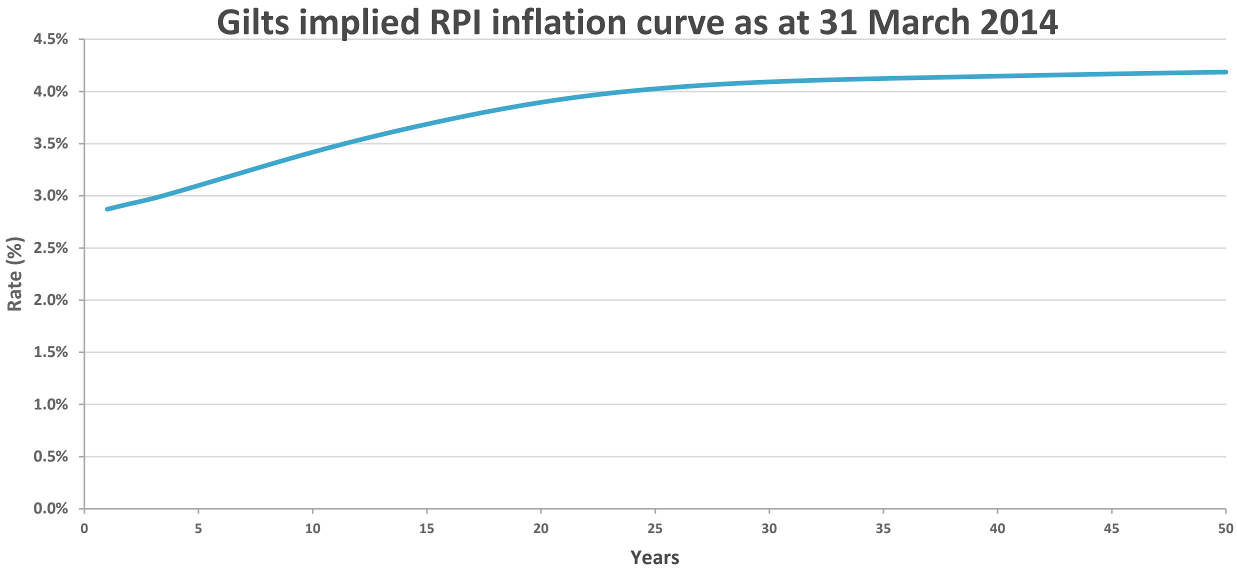
Assumption	Description
Price Inflation (CPI) (deferreds and pensioners)	Bank of England implied inflation (RPI) curve less 0.8% p.a
Discount rate (deferreds and pensioners)	Bank of England nominal yield curve

The chart below shows the nominal spot yields for a Government-backed loan (i.e. the yield to maturity of a zero coupon bond) as at 31 March 2014:



Source: Bank of England

The chart below shows the Bank of England implied inflation curve over a range of maturities at 31 March 2014. This is derived from the yields on both fixed and index linked gilts.



Source: Bank of England

Discount rate

The valuation discount rate is in line with the Bank of England nominal yield curve. This means that each future cashflow has been been discounted at an appropriate spot rate dependent on the expected timing of the cashflow. This approach differs from that taken in the previous valuation in 2011, where a single yield was chosen separately for deferred and pensioner liabilities in order to approximate the broad term of the liabilities.

As per the previous valuation in 2011, there will be no allowance for anticipated out-performance from non Government bonds, equity assets, or property.

Price inflation / pension increases

At the previous valuation, we derived a single assumption for RPI from market data as the difference between the yield on long-dated fixed interest and index-linked government bonds. At this valuation, we have adopted the Bank of England implied inflation (RPI) curve to recognise differing expected inflation assumptions as different durations. We expect the average long term difference between RPI and CPI to be 0.8% p.a.. This is in line with the assumption used in 2011.

Demographic Assumptions

Longevity

The main demographic assumption to which the valuation results are most sensitive is that relating to the longevity of the Fund's members. For this valuation, we have adopted assumptions which give the following sample average future life expectancies for members:

	Deferreds		Current Pensioners	
Assumed life expectancy at age 65	Male	Female	Male	Female
2011 valuation - baseline	19.7	22.2	19.7	22.2
2011 valuation - improvements	23.0	25.7	21.1	23.9
2014 valuation - baseline	19.8	23.2	20.3	22.2
2014 valuation - improvements	26.8	28.6	24.5	25.4

Further details of the mortality assumptions adopted for this valuation can be found in **Appendix E**. Note that the figures deferred members assume that they are aged 45 at the valuation date.

Other demographic assumptions

We are in the unique position of having a very large local authority data set from which to derive our other demographic assumptions. This year, as in previous years, we have made full use of this to analyse the trends and patterns that are present in the membership of local authority funds and tailor our assumptions to reflect LGPS experience.

Further details on these assumptions are set out in **Appendix E**.

Further comments on the assumptions

Level of prudence

As required for Local Government Pension Scheme valuations, our approach to this valuation must include a degree of prudence. This has been achieved by assuming a discount rate in line with low risk UK government bonds. No allowance has been made for the Fund's riskier assets, which would expect to yield a higher return.

For the avoidance of doubt, we believe that all other proposed assumptions represent the "best estimate" of future experience. This effectively means that there is a 50% chance that future experience will be better or worse than the chosen assumption.

Taken as a whole, we believe that our proposed assumptions are more prudent than the best estimate. The assessed liability value on a "neutral" best estimate (not prudent) basis would perhaps be 15-20% lower than the figures shown here.

4 Results

Funding level and deficit

In assessing the extent to which the past service funding objective was met at the valuation date, we have used the actuarial assumptions described in the previous section of this report and funding method described in **Appendix C**. The table below compares the value of the assets and liabilities at 31 March 2014. The 31 March 2011 results are also shown for reference.

The results are presented in the form of a "funding level", this is the ratio of the market value of assets to the assessed cost of members' past service benefits ("liabilities").

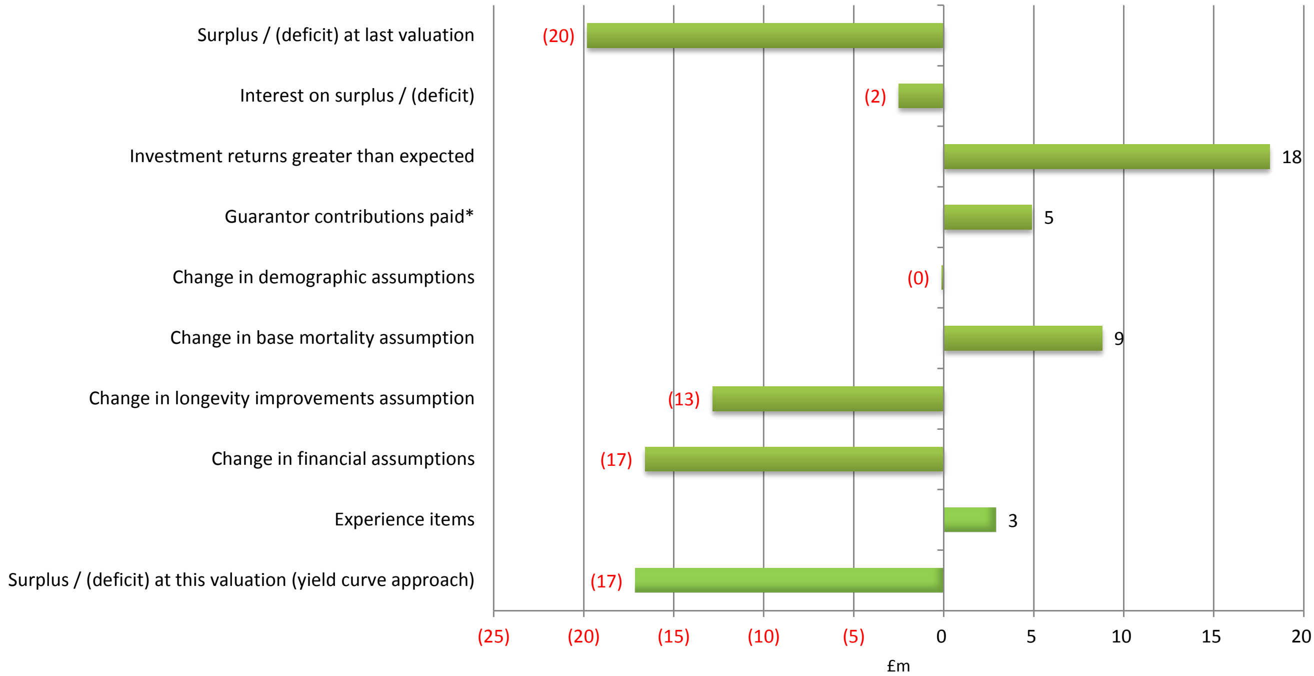
Valuation Date	31 March 2011	31 March 2014
Past Service Position	***(£m)***	**(£m)**
Past Service Liabilities		
Deferred Pensioners	36.9	39.4
Pensioners	107.2	114.1
Total Liabilities	144.1	153.5
Market Value of Assets	124.3	136.3
Surplus / (Deficit)	**(19.8)**	**(17.1)**
Funding Level	**86.3%**	**88.8%**

The Actual Funding Level (AFL) has improved to 88.8% since the previous valuation at 31 March 2011. This corresponds to a deficit of £17.1m at 31 March 2014.

The majority of members benefits increase in line with CPI. Only one element of pension, namely pre 1988 GMP, is fixed in nature (i.e. it does not increase in line with any inflation index). The liability in respect of pre 1988 GMP is equal to approximately 12% of the total liabilities.

Summary of changes to the funding position

The chart below illustrates the various factors that have led to the deficit falling between 31 March 2011 and 31 March 2014.



*includes estimated contributions paid in respect of CAY benefits

Further comments on these some of the items in this chart:

- There is an interest cost of £2m. This is broadly three years of compound interest at 4.30% p.a. (deferred liabilities) and 3.90% p.a. (pensioner liabilities) applied to the previous valuation deficit of £20m.
- Investment returns being higher than expected since 2011 led to a gain of £18m. This is roughly the difference between the actual and expected three-year return (roughly 13%) applied to the whole fund assets from the previous valuation of £124m, with a further allowance made for cashflows during the period.
- At the 2014 valuation, the Fund has adopted Club Vita baseline longevity for the first time and strengthened the future improvements assumption. The effect of this is an increase in the past service liabilities of c£4m, arising from the stronger future improvements assumption but partially offset by the effect of the Club Vita baseline assumption.
- The change in financial conditions between the previous valuation has led to a loss of £17m. This includes the effect of adopting yield curve assumptions for the first time.
- Experience items, such as changes in the membership data, have served to decrease the deficit at this valuation by around £3m.

5 Contributions payable by the Guarantor

Contribution Rate

The Guarantee paper sets out how payments from the Guarantor should be determined. The calculation below sets out the contribution due from the Guarantor based on the funding position at 31 March 2014.

Assets (£m)	136.3
Past service liabilities (£m)	153.5
Actual Funding Level (AFL)	88.8%
Target Funding Level (TFL)	91.5%
Target assets (£m)	140.4
Shortfall (TFL – AFL) (£m)	4.1
Amortisation period (years)	8
5 to 10 years fixed interest bond yield	2.35%
Annuity	7.13
Annual contribution payable from 1 April 2015	**£575,000 p.a.**

In addition, the Guarantor will pay £100,000 p.a. towards the cost of ongoing administration expenses.

6 Risk assessment

The valuation results depend critically on the actuarial assumptions that are made about the future of the Fund. If all of the assumptions made at this valuation were exactly borne out in practice then the results presented in this document would represent the true cost of the Fund as it currently stands at 31 March 2014.

However, no one can predict the future with certainty and it is unlikely that future experience will exactly match all of our assumptions. The future therefore presents a variety of risks to the Fund and these should be considered as part of the valuation process. In particular:

- The main risks to the financial health of the Fund should be **identified**.
- Where possible, the financial significance of these risks should be **quantified**.
- Consideration should be given as to how these risks can then be **controlled** or **mitigated**.
- These risks should then be **monitored** to assess whether any mitigation is actually working.

This section investigates the potential implications of the actuarial assumptions not being borne out in practice.

Set out below is a brief assessment of the main risks and their effect on the valuation results, beginning with a look at the effect of changing the main assumptions and then focusing on the two most significant risks – namely investment risk and longevity risk.

Sensitivity of valuation results to changes in assumptions

Broadly speaking, there are two particular risks that are generally of most interest to pension funds – the performance of the Fund's investments and improvements in life expectancy compared to our assumptions. A further analysis of both is given below.

Investment risk

As the assets of the Fund are taken at their market value, volatility in investment performance can have an immediate and tangible effect on the funding level and deficit. This is less relevant for the Fund because of the investment strategy in place, i.e. only 35% of the Fund's assets invested in riskier assets such as equities and equity-type investments (e.g. property). A rise or fall in the level of equity markets has a direct impact on the financial position of the Fund, which may seem obvious.

Less obvious is the effect of anticipated investment performance on the Fund's liabilities. Here it is the returns available on government bonds that are of crucial importance, as the discount rate that we use to place a value on the Fund's liabilities is based on gilt yields at the valuation date. As described earlier, the discount rate used to value the Fund's future benefit payments is based on the return on fixed interest gilts, whilst the benefits themselves are projected to increase in line with inflation. Therefore, the return available on index-linked gilts is a key factor in the valuation of the Fund's liabilities.

The table below shows how the funding level (top), deficit (middle) and total contribution rate (bottom) would vary if investment conditions at 31 March 2014 were different (based on the existing valuation approach). The level of the FTSE 100 Price index is taken as a suitable proxy for asset performance whilst the index-linked gilt yield is taken as a yardstick for the valuation of liabilities.

Index Linked Gilt Yield		6098	6598	7098
	0.20%	88% (17)	91% (14)	93% (10)
	0.00%	87% (21)	89% (17)	91% (14)
	-0.20%	85% (24)	87% (21)	89% (17)
		FTSE 100 Price Index		

The shaded box contains the results for this valuation. Note that this does not take account of the performance of all asset classes held by the Fund (e.g. property, bonds, cash) but it does serve to highlight, in broad terms, the sensitivity of the valuation results to investment conditions at the valuation date.

Note that the scenarios illustrated above are by no means exhaustive. They should not be taken as the limit of how extreme future investment experience could be.

Longevity risk

The valuation results are also very sensitive to unexpected changes in future longevity. All else being equal, if longevity improves in the future at a faster pace than allowed for in the valuation assumptions, the funding level will decline and the required Guarantor contribution will increase.

Recent medical advances, changes in lifestyle and a greater awareness of health-related matters have resulted in life expectancy amongst pension fund members improving in recent years at a faster pace than was originally foreseen. It is unknown whether and to what extent such improvements will continue in the future.

For the purposes of this valuation, we have selected assumptions that we believe make an appropriate allowance for future improvements in longevity, based on the actual experience of the Fund since the previous valuation.

The table below shows how the valuation results at 31 March 2014 are affected by adopting different longevity assumptions. See page 8 for further details.

	Impact	
Longevity assumption	**Funding level**	**Deficit (£m)**
2014 valuation assumption	89%	(17)
1 year extra	86%	(22)

Note that the table shows the effect of changes to each assumption in isolation. In reality, it is perfectly possible for the experience of the Fund to deviate from many of these assumptions between valuations and so the precise effect on the funding position is therefore more complex.

Other risks to consider

The table below summarises the effect that changes in some of the other valuation assumptions and risk factors would have on the funding position. Note that these are probably unlikely to change in such a way that would rank them as amongst the highest risks facing the Fund and therefore the analysis is qualitative rather than quantitative.

Risk	Funding level impact
Price inflation higher than anticipated	Decreases
Members convert less pension to cash at retirement than assumed	Decreases
Changes to Regulations that make benefit package more favourable to members	Decreases (if changes affect past service)

Managing the risks

Whilst there are certain things, such as the performance of investment markets or the life expectancy of members, that are not directly within the control of the pension fund, that does not mean that nothing can be done to understand them further and to mitigate their effect. Although these risks are difficult (or impossible) to eliminate, steps can be taken to manage them.

Ways in which some of these risks can be managed could be:

- Set aside a specific reserve to act as a cushion against adverse future experience by taking advantage of any surpluses against the TFL that arise (possibly by selecting a set of actuarial assumptions that are deliberately more prudent). For example, investment mismatch risk could be reduced over time through a gradual reduction in the percentage held in riskier assets. The Administering Authority actively monitors the AFL against the TFL on a regular basis to ensure that this happens.
- Carry out a bespoke analysis of the longevity of Fund members and monitor how this changes over time, so that the longevity assumptions at the valuation provide as close a fit as possible to the particular experience of the Fund. This is effectively what Club Vita does.

We would be delighted to set out in more detail the risks that affect the Fund and discuss with you possible strategies for managing them.

7 Related issues

The Fund's valuation operates within a broader framework, and this document should therefore be considered alongside the following:

- Operation of Scottish Executive Guarantee paper, confirming the approach to determining contributions payable to the Fund by the Scottish Government
- the Statement of Investment Principles (e.g. the discount rate must be consistent with the Fund's asset strategy);
- the general governance of the Fund, such as meetings of the Pensions Committee, decisions delegated to officers, the Fund's business plan, etc; and
- the Fund's risk register.

Further recommendations

Valuation frequency

Under the provisions of the LGPS regulations, the next formal valuation of the Fund is due to be carried out as at 31 March 2017. In light of the uncertainty of future financial conditions, we recommend that the financial position of the Fund is monitored by means of interim funding reviews in the period up to this next formal valuation. This will give early warning of changes to funding positions and possible contribution rate changes.

Investment strategy and risk management

We recommend that the Administering Authority continues to regularly review its investment strategy and ongoing risk management programme.

8 Reliances and limitations

Scope

This document has been requested by and is provided to the City of Edinburgh Council in its capacity as Administering Authority to the Scottish Homes Pension Fund. It has been prepared by Hymans Robertson LLP to fulfil the statutory obligations in accordance with regulation 32 of the Local Government Pension Scheme (Scotland) Regulations (2008). None of the figures should be used for accounting purposes (e.g. under FRS17 or IAS19) or for any other purpose.

This document should not be released or otherwise disclosed to any third party without our prior written consent, in which case it should be released in its entirety. Hymans Robertson LLP accepts no liability to any other party unless we have expressly accepted such liability.

The results of the valuation are dependent on the quality of the data provided to us by the Administering Authority for the specific purpose of this valuation. We have previously issued a separate report confirming that the data provided is fit for the purposes of this valuation and have commented on the quality of the data provided. The data used in our calculations is as per our report of 23 July 2014.

Actuarial Standards

The following Technical Actuarial Standards[1] are applicable in relation to this report and have been complied with where material:

- TAS R – Reporting;
- TAS D – Data;
- TAS M – Modelling; and
- Pensions TAS.

Richard Warden

Fellow of the Institute and Faculty of Actuaries

4 December 2014

Steven Scott

Fellow of the Institute and Faculty of Actuaries

4 December 2014

[1] Technical Actuarial Standards (TASs) are issued by the Financial Reporting Council (FRC) and set standards for certain items of actuarial work, including the information and advice contained in this report.

Appendix A: About the pension fund

The purpose of the Fund is to provide retirement benefits to its members. It is part of the Local Government Pension Scheme (LGPS) and is a defined benefit pension scheme.

Defined benefit pension scheme

In a defined benefit scheme such as this, the nature of retirement benefits that members are entitled to is known in advance. For example, it is known that members will receive a pension on retirement that is linked to their salary and pensionable service according to a pre-determined formula.

However, the precise cost to the Fund of providing these benefits is **not** known in advance. The estimated cost of these benefits represents a liability to the Fund and assets must be set aside to meet this. The relationship between the value of the liabilities and the value of the assets must be regularly assessed and monitored to ensure that the Fund can fulfil its core objective of providing its members with the retirement benefits that they have been promised.

Liabilities

The Fund's liabilities are the benefits that will be paid in the future to its members (and their dependants).

The precise timing and amount of these benefit payments will depend on future experience, such as when members will retire, how long they will live for in retirement and what economic conditions will be like both before and after retirement. Because these factors are not known in advance, assumptions must be made about future experience. The valuation of these liabilities must be regularly updated to reflect the degree to which actual experience has been in line with these assumptions.

Assets

The Fund's assets arise from the contributions paid and the investment returns that they generate. The way these assets are invested is of fundamental importance to the Fund. The selection, monitoring and evolution of the Fund's investment strategy are key responsibilities of the Administering Authority.

As the estimated cost of the Fund's liabilities is regularly re-assessed, this effectively means that the amount of assets required to meet them is a moving target. As a result, at any given time the Fund may be technically in surplus or in deficit.

A contribution strategy must be put in place which ensures that the Guarantor pays money into the Fund at a rate which will target the cost of the liabilities in respect of benefits already earned by members.

The long-term nature of the Fund

The pension fund is a long-term commitment. Even though there are no active members, it will still be paying out benefits to existing members and dependants for many decades to come. It is therefore essential that the various funding and investment decisions that are taken now recognise this and come together to form a coherent long-term strategy.

In order to assist with these decisions, the Regulations require the Administering Authority to obtain a formal valuation of the Fund every three years. Along with the Funding Strategy Statement, this valuation will help determine the funding objectives that will apply from 1 April 2015.

Appendix B: Summary of the Fund's benefits

The non-discretionary Fund benefits that we have taken into account in this valuation for the members are summarised below.

Provision	Benefit Structure To 31 March 2009
Normal retirement age (NRA)	Age 65
Earliest retirement age (ERA) on which immediate unreduced benefits can be paid on voluntary retirement	As per NRA (age 65). Protections apply to active members in the scheme immediately prior to 1 December 2006 who would have been entitled to immediate payment of unreduced benefits prior to 65, due to: (a) having previously had an NRA of age 60 (or after age 60 on attaining 25 years of scheme membership), due to being a member of the scheme immediately prior to 1 April 1998; or (b) having the potential to satisfy the rule of 85 prior to age 65 (if the sum of age (whole years) and membership (whole years) is 85 or more). The benefits relating to various segments of scheme membership are protected as follows, which means their benefits are calculated based on the above definitions of earliest retirement age in relation to these protected periods of scheme membership. (a) A member born on 31 March 1960 or earlier – membership up to 31 March 2020 protected; (b) All other members in the scheme immediately prior to 1 December 2006 – membership up to 31 March 2008 protected.
Pensionable pay	All salary, wages, fees and other payments in respect of the employment, excluding non-contractual overtime and some other specified amounts. Some scheme members may be covered by special agreements.
Final pay	The pensionable pay in the year up to the date of leaving the scheme. Alternative methods used in some cases, e.g. where there has been a break in service or a drop in pensionable pay.
Period of scheme membership	Total years and days of service during which a member contributes to the Fund. Additional periods may be granted (e.g. transfers from other pension arrangements, augmentation, or from April 2009 the award of additional pension). For part time members, the membership is proportionate with regard to their contractual hours and a full time equivalent.
Normal retirement benefits at NRA	Annual Retirement Pension - 1/80th of final pay for each year of scheme membership. Lump Sum Retirement Grant - 3/80th of final pay for each year of scheme membership. Additional lump sum can be provided by commutation of pension (within overriding limits) on a basis of £12 additional lump sum for each £1 of pension surrendered.
Option to increase retirement lump sum benefit	At the time that benefits come into payment, members have the option to exchange ('commute') some of the retirement pension into additional lump sum. The terms for the conversion of pension in to lump sum is £12 of lump sum for every £1 of annual pension surrendered.
Voluntary early retirement benefits (non ill-health)	On retirement after age 60 a pension and lump sum based on actual scheme membership completed may be paid, subject to reduction on account of early payment in some circumstances (in accordance with ERA protections).

Provision	Benefit Structure To 31 March 2009
Pension increases	All pensions in payment, deferred pensions and dependant's pensions other than benefits arising from the payment of additional voluntary contributions are increased annually. Pensions are increased partially under the Pensions (Increases) Act and partially in accordance with statutory requirements (depending on the proportions relating to pre 88 GMP, post 88 GMP and excess over GMP).
Death after retirement	A spouse's or civil partner's pension of one half of the member's pension (generally post 1 April 1972 service for widowers' pension and post 6 April 1988 for civil partners) is payable; plus If the member dies within five years of retiring and before age 75 the balance of five years' pension payments will be paid in the form of a lump sum; plus Children's pensions may also be payable.
State pension scheme	The Fund is contracted-out of the State Second Pension and the benefits payable to each member are guaranteed to be not less than those required to enable the Fund to be contracted-out.

Note: Certain categories of members of the Fund are entitled to benefits that differ from those summarised above.

Discretionary benefits

The LGPS Regulations give employers a number of discretionary powers. The effect on benefits or contributions as a result of the use of these provisions as currently contained within the Local Government Pension Scheme Regulations has been allowed for in this valuation to the extent that this is reflected in the membership data provided. No allowance has been made for future use of discretionary powers.

Appendix C: About the valuation

It is important to realise that the actual cost of the pension fund (i.e. how much money it will ultimately have to pay out to its members in the form of benefits) is currently unknown. This cost will not be known with certainty until the last benefit is paid to the last pensioner. The core purpose of this valuation is to estimate what this cost will be, so that the Fund can then develop a strategy to meet it.

Such a valuation can only ever be an estimate – as the future cannot be predicted with certainty. However, as actuaries, we can use our understanding of the Fund and the factors that affect it to determine an anticipated cost which is as sensible and realistic as possible. A decision can then be made as to how much is set aside now to meet this anticipated cost. The pace of this funding can vary according to the level of prudence that is built into the valuation method and assumptions.

Past service

The principal measurement here is the comparison at the valuation date of the assets (taken at market value) and the value placed on the Fund's liabilities (calculated using a market-based approach). By maintaining a link to the market in both cases, this helps ensure that the assets and liabilities are valued in a consistent manner. Our calculation of the Fund's liabilities also explicitly allows for expected future pay and pension increases.

The funding level is the ratio of assets to liabilities at the valuation date. A funding level of less/more than 100% implies that there is a deficit/surplus in the Fund at the valuation date.

The funding target is to eliminate any deficit (or surplus) over a specified period and therefore get back to a funding level of 100%. To do so, additional contributions may be required to be paid into the Fund.

The sensitivity of valuation results

The aim of this valuation is not only to determine these important figures but also to demonstrate their sensitivity to a number of key influences. This will promote an understanding of how the expected cost of the Fund may change in response to uncertain future events (e.g. changes in life expectancy or investment returns).

Appendix D: Data

This section contains a summary of the membership, investment and accounting data provided by the Administering Authority for the purposes of this valuation (the corresponding membership and investment data from the previous valuation is also shown for reference). For further details of the data, and the checks and amendments performed in the course of this valuation, please refer to our separate report.

Membership data

Deferred pensioners

	31 March 2011		31 March 2014	
	Number	Deferred pension (£000)	Number	Deferred pension (£000)
Total deferred membership	690	1,615	598	1,353

The deferred pension shown includes revaluation up to and including the 2014 Pension Increase Order.

Current pensioners, spouses and children

	31 March 2011		31 March 2014	
	Number	Pension (£000)	Number	Pension (£000)
Members	991	6,104	953	6,225
Dependants	302	704	314	805
Children	4	5	3	3
Total pensioner members	**1,297**	**6,813**	**1,270**	**7,033**

Note that the membership numbers in the table above refer to the number of records provided to us and so will include an element of double-counting in respect of any members who are in receipt (or potentially in receipt of) more than one benefit.

Membership Profile	Average Age (years)	
	2011	2014
Deferred Pensioners	52.4	53.5
Pensioners	69.7	71.6

The average ages are weighted by liability.

Assets at 31 March 2014

A summary of the Fund's assets as at 31 March 2011 and 31 March 2014 is as follows:

Asset class	Market Value at 31 March 2011 (£000)	Allocation %	Market Value at 31 March 2014 (£000)	Allocation %
UK equities	10,774	9%	8,777	6%
UK fixed interest gilts	11,909	10%	17,336	13%
UK index-linked gilts	49,049	39%	69,498	51%
Overseas equities	38,670	31%	31,189	23%
Property	12,193	10%	6,960	5%
Cash and net current assets	1,713	1%	2,544	2%
Total	**124,308**	**100%**	**136,305**	**100%**

Accounting data – revenue account for the three years to 31 March 2014

Consolidated accounts (£000)	Year to			Total
	31 March 2012	31 March 2013	31 March 2014	
Income				
Employer - normal contributions	100	771	771	1,642
Employer - additional contributions	0	0	0	0
Employer - early retirement and augmentation strain contributions	0	23	20	44
Employee - normal contributions	0	0	0	0
Employee - additional contributions	0	0	0	0
Transfers In Received (including group and individual)	0	0	0	0
Other Income	0	0	0	0
Total Income	**100**	**794**	**791**	**1,686**
Expenditure				
Gross Retirement Pensions	6,912	7,070	7,082	21,065
Lump Sum Retirement Benefits	683	488	329	1,501
Death in Service Lump sum	9	2	15	26
Death in Deferment Lump Sum	0	0	0	0
Death in Retirement Lump Sum	0	0	0	0
Gross Refund of Contributions	0	0	0	0
Transfers out (including bulk and individual)	209	82	9	300
Fees and Expenses	98	61	57	216
Total Expenditure	**7,912**	**7,703**	**7,493**	**23,107**
Net Cashflow	**-7,812**	**-6,909**	**-6,701**	**-21,422**
Assets at start of year	**124,308**	**131,418**	**140,116**	**124,308**
Net cashflow	-7,812	-6,909	-6,701	-21,422
Change in value	14,922	15,606	2,890	33,419
Assets at end of year	**131,418**	**140,116**	**136,305**	**136,305**
Approximate rate of return on assets	**12.4%**	**12.2%**	**2.1%**	**28.7%**

Note that the figures above are based on the Fund accounts provided to us for the purposes of this valuation, which were fully audited at the time of our valuation calculations.

Appendix E: Assumptions

Financial assumptions

Assumption	Description
Price Inflation (CPI) (deferreds and pensioners)	Bank of England implied inflation (RPI) curve less 0.8% p.a
Discount rate (deferreds and pensioners)	Bank of England nominal yield curve

Mortality assumptions

Longevity assumptions	31 March 2014
Longevity - baseline	Vita curves
Longevity - improvements	
CMI Model version used	CMI_2012
Starting rates	CMI calibration based on data from Club Vita using the latest available data as at December 2012.
Long term rate of improvement	Period effects: 1.25% p.a. for men and women. Cohort effects: 0% p.a. for men and for women.
Period of convergence	Period effects: 10 years for ages 45 and below with linear transition to 40 years for those aged 75 and over. Cohort effects: 40 years for those born in 1949 or later declining linearly to 5 years for those born in 1914 or earlier.
Proportion of convergence remaining at mid point	75%

We have suggested a longevity improvement assumption based on the industry standard model and combined information from our longevity experts in Club Vita. The start point for the improvements has been based on observed death rates in the Club Vita data bank.

In the short term we have assumed that improvements in life expectancy will continue to strengthen for a few more years before tailing off. We describe this as ‘not peaked’, as opposed to the alternative assumption that improvements have ‘peaked’ and will immediately tail off.

In the long term (for ages up to age 90) we have assumed that increases in life expectancy will stabilise at a rate of increase of 1 year per decade for men and women. This is equivalent to assuming that longer term mortality rates will fall at a rate of 1.25% p.a. for men and women.

However, we have assumed that post age 90 improvements in mortality will be hard to achieve, and so have assumed that the long term rate of improvement will decline between ages 90 and 120 so that no improvements are seen at ages 120 and over.

Other demographic valuation assumptions

Family details	A varying proportion of members are assumed to be married (or have an adult dependant) at retirement or on earlier death. For example, at age 60 this is assumed to be 90% for males and 85% for females. Husbands are assumed to be 3 years older than wives.
Commutation	Future pensioners are assumed to elect to exchange pension for additional tax-free cash up to 50% of HMRC limits.

Sample rates of the incidence of death from deferred status are shown in the table below.

Age	Death in Deferment Rates Incidence per 1000 members per annum All Males	 All Females
30	0.36	0.24
35	0.42	0.40
40	0.72	0.64
45	1.20	1.04
50	1.92	1.52
55	3.00	2.00
60	5.40	2.56

Appendix F: Rates and adjustments certificate

In accordance with regulation 32(1) of the Administration Regulations we have made an assessment of the contributions that should be paid into the Fund by the Guarantor for the period 1 April 2015 to 31 March 2018 in order to maintain the solvency of the Fund.

The required minimum contribution rates are set out in the attached table.

Richard Warden

Fellow of the Institute and Faculty of Actuaries

4 December 2014

Steven Scott

Fellow of the Institute and Faculty of Actuaries

4 December 2014

Statement to the Rates and Adjustments Certificate

The Minimum Total Contribution Rate payable by the Guarantor is set out below.

Period	Guarantor's Minimum Contribution Rate
1 April 2015 to 31 March 2016	£675,000
1 April 2016 to 31 March 2017	£675,000
1 April 2017 to 31 March 2018	£675,000

Notes

Contributions should be paid into the Scottish Homes Pension Fund ('the Fund') at a frequency in accordance with the requirements of the Regulations.

The certified contribution rates represent the minimum level of contributions to be paid. Further amounts may be paid at any time.

Pensions Committee

2.30pm, Wednesday, 17 December 2014

EU Tax Claims

Item number	5.9
Report number	
Executive/routine	
Wards	All

Executive summary

This report summarises activity on EU tax claims made on behalf of the Lothian Pension Fund. During the period since the last report, the amount of settled claims has increased by £207.2k to a total of £1,262.1k. Progress continues on the various outstanding claims.

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	

Report

EU Tax Claims

Recommendations

1.1 Committee is requested to:

- Note the progress made in reclaiming EU taxes suffered on dividends.

Background

2.1 EU tax claims relate to the recovery of tax deducted from dividend payments prior to receipt. They relate to a fundamental principle of EU law, that all member states should not discriminate in the application of national taxes between home tax payers and those in other member states.

2.2 The claims can be divided into three main types – Manninen, Fokus and Manufactured Dividends.

Main report

Claims for EU Tax Credits – Manninen

3.1 This claim is against the UK tax authorities and is based on HMRC permitting the repayment of tax credits deducted from UK dividends but not on Foreign Income Dividends paid by UK companies.

3.2 The European Court of Justice's ruling in the Manninen tax case in September 2004 opened an avenue for claims for tax credits on EU dividends. Pensions and Trusts Committee has previously agreed to pursue potential claims.

3.3 Based on the decision in the Manninen case, KPMG's EU Tax Group is undertaking claims on behalf of UK pension funds to claim a repayment of tax credits on dividend income for the period 6 April 1992 to 1 July 1997.

3.4 The claims are based on 20% of the gross dividends received. While the UK tax authorities are disputing the validity of such claims, the estimates show that the Lothian Pension Funds could benefit by up to £2.6m from a successful claim. A cost benefit analysis concluded that a claim should be lodged, and this was done on 9 February 2006.

3.5 HMRC has rejected all claims of this nature. As a result, KPMG has appointed a firm of solicitors (Pinsent Masons) to pursue recovery.

3.6 A brief chronology of events to date is provided in the table below:

Date	Event
March 2011	First-tier Tribunal (FTT) published its judgement on the test case: • Withholding of tax credits on foreign income dividends was a breach of EU law. • Claims were out of time because they were made more than six years after the end of the tax year in which the relevant dividends were received. The FTT rejected legal arguments that the statutory time limits should be extended.
July 2012	Appeal against the FTT judgement was heard by the Upper Tribunal.
February 2013	Upper Tribunal published its judgement on the appeal and supports judgement of the FTT.
May 2013	Upper Tribunal refuses HMRC's request for leave to appeal on the substantive issue and claimants' request on the out of time issue.
July 2013	Court of Appeal approves direct requests to appeal from HMRC and claimants.
September 2013	Court of Appeal advises that a preliminary hearing will be held in December 2013 to decide if any questions related to the case should be referred to the Court of Justice of the European Union.
December 2013	Court of Appeal rejects our appeal on one specific time limit argument (based on the domestic law). A further hearing by the Court of Appeal has been set for February 2015 to consider HMRC's appeal on the substantive issues and our time limit arguments (based on European law). It is possible that the Court of Appeal will refer certain issues to the CJEU at this hearing.

3.7 Fees incurred to date, by Lothian Pension Fund, on these claims amount to £54.5k (£49.5k as at the last update to Committee in December 2013). Assuming that the case is pursued to a final conclusion, total costs for the Fund are capped at £90k. This compares with the claim for £2.6m.

Claims for EU Tax Credits – Fokus Bank

3.8 These claims are against the tax authorities of the EU member states (and Norway) in which the Fund has invested. The basis of the claims is that the tax authorities have applied favourable tax treatment to domestic pension funds that they have denied to pension funds in other member states.

3.9 The Pensions and Trusts Committee of October 2007 approved making claims under the principle established in the Fokus Bank case. Claims currently estimated at around £3.5m have been made. Progress on the claims is summarised in the table below.

Country	Claim Period From / To	Estimated Amount Claimed £'000	Amount Received £'000	Notes
Completed Claims				
Austria	2006 2010	83.0	83.0	Claim paid in September 2012.
Netherlands	2003 2006	440.0	440.0	Claim paid in 2009.
Norway	2004 2010	273.0	273.0	All claims paid - final instalment received in February 2013 (£73k)
Active Claims				
France	2005 2009	658.0	-	15% tax imposed on all pension funds from 1 January 2009 – so no further claims can be made after that date. In May 2012, the EU Court ruled in the Santander test case that refunds must be paid to investment funds. Legal action started in the Court of Appeal of Montreuil in 2013. Further legal arguments are due to be filed with the Court during the last quarter of 2014. KPMG are still positive about the ultimate payment of the claims but there is still uncertainty as to when.

Country	Claim Period From / To	Estimated Amount Claimed £'000	Amount Received £'000	Notes
Germany	2003 2010	911.6	-	While the principles behind the claims seem to have been accepted by the German tax authorities, they are currently refusing to clarify the procedure that has to be followed to obtain payment of the claims. With the continuing lack of clarity from the German tax authorities, KPMG are in the final stages of filing a complaint in the German Courts.
Italy	2004 2010	508.7	-	There have been few recent developments for pension funds in Italy. Furthermore, some Italian Court decisions announced recently have even shown reluctance on the part of the Italian Courts to recognise EU law jurisprudence over Italian law. It seems that litigation will be required in order to progress with claims in this territory. There are fewer claimants in Italy to fund litigation. KPMG feel that it is better to focus on France and Germany before considering to Italy.
Spain	2004 2009	661.4	466.1	The principle of paying the refunds was approved by the Spanish Courts in May 2013. By November 2013 we had received refunds for periods up to the first quarter of 2004. In May and July of 2014 we received refunds for quarters two to four of 2006, quarter four of 2008 and all four quarters of 2009. An additional £207.2k compared to the Committee report of December 2013. Quarter three of 2007 to quarter three of 2008 remain outstanding.
TOTAL		**3,535.7**	**1,262.1**	

3.10 Exchange rate movements change the potential value of the claims in sterling terms.

3.11 Fees incurred to date on these claims amount to £367.7k (£351.7k as at the meeting of December 2013). Costs are higher for the Fokus Bank type claims because of the need to file claims separately in individual EU countries.

Claims for EU Tax Credits – Manufactured Dividends

3.12 This claim is against the UK tax authorities. It is based on the fact that manufactured dividend receipts relating to UK shares were not subject to any UK withholding tax but receipts relating to overseas dividends suffered a UK withholding tax of 15%.

3.13 Note that manufactured dividends are dividends created when a security is out on loan at the time the company pays a dividend.

3.14 Claims in respect of manufactured dividends totalling £3.9m on behalf of Lothian Pension Fund has been lodged with HMRC.

3.15 KPMG has appointed a firm of solicitors (Pinsent Masons) to pursue recovery. An initial hearing of the First-tier Tribunal (FTT) took place in March 2013.

3.16 Due to continuing inaction, other than issuance of information requests from HMRC, Pinsent Masons made an application for the test case to proceed and the FTT granted this request. It is likely that the hearing will take place during the first quarter of 2015. Pinsent Masons have been in correspondence with HMRC through the course of 2014 and have now agreed a statement of facts in order to minimise the fact-finding undertaken by the Tax Tribunal at the hearing itself.

3.17 Fees incurred to date on these claims amount to £100.4k (£92.0k as at the meeting of December 2013). Potential subsequent referrals are estimated to cost £20k for each legal stage.

Measures of success

4.1 Success is measured by the amount of tax recovered exceeding the cost of pursuing the claims.

Financial impact

5.1 EU tax claims totalling in excess of £10m have now been lodged with the relevant tax authorities. Professional fees amounting to £522.6k have been incurred to date. As previously agreed by Pensions Committee, it is likely that further legal costs will be incurred in pursuing the claims. However, any legal costs are shared across a pool of fellow claimants and Lothian Pension Fund has the right to cease participation without incurring further costs.

5.2 Currently, claims paid to date exceed the costs incurred by £739.5k. The financial position can be summarised as follows:

	Total Claims £'000	Claims Settled £'000	Claims Outstanding £'000	Costs to Date £'000
Claim Type				
Manninen	2,626.7	Nil	2,626.7	54.5
Fokus Bank	3,535.7	1,262.1	2,273.6	367.7
Manufactured Dividends	3,928.6	Nil	3,928.6	100.4
	10,091.0	**1,262.1**	**8,828.9**	**522.6**

Risk, policy, compliance and governance impact

6.1 There are no risk, policy, compliance and governance impacts arising from this report.

Equalities impact

7.1 There are no equalities impacts arising from this report.

Sustainability impact

8.1 There are no sustainability impacts arising from this report.

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to governance.

Background reading/external references

None

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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	

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Environmental Social and Governance Activity Update

Item number	5.10
Report number	
Executive/routine	
Wards	All

Executive summary

This report provides the annual update on Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund's, (the Funds), activity on environmental, social and governance (ESG) issues. The Funds pursue a policy of constructive engagement on issues, which is consistent with fiduciary duties.

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	

Report

Environmental Social and Governance Activity Update

Recommendations

1.1 Committee is requested to:

- Note the contents of this report.
- Endorse Councillor Cameron Rose's nomination to stand for re-election to the Local Authority Pension Fund Forum (LAPFF) Executive and for the position of Vice Chair, at the January 2015 AGM.

Background

2.1 The Funds pursue a policy of constructive engagement on issues, which is consistent with fiduciary duties.

Main report

Voting and Engagement

3.1 The voting and engagement arrangements on the Funds' equity holdings are shown in the tables below.

Mandate	**Voting and Engagement Arrangement**
UBS (Emerging markets)	UBS
State Street Pooled Funds (for Scottish Homes Pension Fund)	State Street
All other listed equities	Hermes Equity Ownership Services (EOS)

3.2 The busiest voting season is the quarter ending 30 June (Q2). In Q2 2014 Hermes EOS voted on the Funds' behalf at 413 meetings (5,876) resolutions. Hermes opposed 351 resolutions and supported management on 5,525.

3.3 Hermes EOS' recent engagement activity is detailed in Hermes quarterly report, which is available on the LPF website. Activity includes promotion of integrated sustainability and financial reporting by companies. As well as engaging with companies on this issue Hermes EOS is part of several initiatives to promote integrated reporting, such as the Sustainable Stock exchange initiative.

3.4 Hermes EOS has also engaged with food companies on the paradox that both obesity and malnutrition are problems.

3.5 Recent work on governance has included increased focus on issues with boards in Asia, where engagement with companies on stewardship issues is starting to gain momentum.

Local Authority Pension Fund Forum (LAPFF)

3.6 Lothian Pension Fund was a founding member of the LAPFF when it was established in 1990. It promotes the long-term investment interests of local authority pension funds and aims to maximise their influence as shareholders to promote corporate social responsibility and high standards of corporate governance amongst the companies in which they invest, commensurate with statutory regulations. Its membership has increased over recent years (currently 60 of the 110 UK local government pension schemes).

3.7 LAPFF has continued its work on accounting standards for the banking industry and has made significant progress. Other recent activity includes corporate governance, carbon risk and executive pay. Further information such as Quarterly Engagement Reports and Newsletters is available on the LAPFF website. LAPFF also uses Twitter to update on activity.

3.8 Councillor Cameron Rose is currently Vice Chair of the Executive Committee of the LAPFF. Committee is asked to endorse Councillor Rose's nomination to stand for re-election to the Executive and for the position of Vice Chair at the AGM in January 2015. If successful, Council's endorsement of the appointment will be sought. Councillor Rose will provide a verbal update to Committee on his role on the Executive.

Principles for Responsible Investment (PRI)

3.9 Lothian Pension Fund signed the PRI in 2008. The PRI is a global network for investors to publicly demonstrate their commitment to responsible investment, to collaborate and learn with their peers about the financial and investment implications of ESG issues, and to incorporate these factors into their investment decision making and ownership practices. Through membership of PRI we have been able to join various working groups on specific responsible investment issues. We also participate in an informal group of PRI signatories, which has been very useful. For example, through this group we have collaborated in an initiative to encourage external investment managers to produce meaningful information on ESG activity in their regular client reporting.

3.10 Signatories complete a self assessment each year to measure progress against the PRI principles and also to allow comparison with peers.

3.11 Previous assessments of the Funds' activities have generally been very good. The feedback on our submission for 2013 included a suggestion for improvement in ESG integration in investment decision making. The Fund is reviewing options in this area for the internally managed funds. One possibility is the use of quantitative ESG data in the decision making process. As the 2013 assessment process was still at the pilot stage, PRI stipulates that feedback reports are only made available to stakeholders, and are not to be made public.

3.12 In the past the Fund has found that the self assessment process was time consuming and complex and the value of the resulting report questionable. However we have worked with PRI on their efforts to improve the process and we have now received the assessment request for year ending 31 Dec 2014, which is to be completed by March 2015. The PRI will provide our results by July 2015. This is quicker than previously and the new assessment also seems more relevant and useful. Further updates on the assessment will be provided to Committee.

Measures of success

4.1 Success of engagement with companies is very difficult to measure. The Funds' approach is essentially qualitative and is wide ranging. The impact is very difficult to quantify, especially in the short term. The Funds are signatories to PRI and complete the annual self assessment process which compares ESG activity with peers.

Financial impact

5.1 There is no financial impact as a result of this report. The costs of the Funds' ESG activity are included in the pension funds' budget.

Risk, policy, compliance and governance impact

6.1 The Environmental Social and Governance (ESG) activity of the Fund, that is being responsible informed and involved investors, is expected to reduce risk.

Equalities impact

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

Sustainability impact

8.1 As much of the engagement activity is on sustainability issues, it is expected to contribute to the sustainability of the funds' investments.

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading / external references

None.

Alastair Maclean

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Links

Lothian Pension Fund:

Responsible Investment http://www.lpf.org.uk/info/68/responsible_investment

http://www.lpf.org.uk/lpf1/info/76/unpri

United Nations Principles for Responsible Investment http://www.unpri.org/

Local Authority Pension Fund Forum http://www.lapfforum.org/

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	None

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Class Actions

Item number	5.11
Report number	
Executive/routine	
Wards	All

Executive summary

This report provides an annual update on the Funds' class action activity. A class action is where a group (a class) sues another party. Typically, these actions happen in the US. The type of class action relevant to the Funds is when a group of shareholders collectively sue a company in order to recover a loss in share value, or to exert influence on the company. Since 2006 the fund has received US$3.0 million in class action compensation. US$139k has been received since the last update to Committee in December 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	

Report

Class Actions

Recommendations

1.1 Committee is requested to note the update on class actions.

Background

2.1 In shareholder class actions one or more investors agree to act as lead plaintiff(s). A law firm acts on behalf of the class with the lead plaintiffs being treated as the representatives of the class. The cases can take several years to be heard by the courts and can be settled out of court. In the United States, cases are typically taken on a no win, no fee basis.

2.2 If a class action case is won, the compensation fund, net of legal fees approved by the court, is distributed to eligible shareholders who make a claim within the relevant time limit. Any shareholder that held shares during the class period is entitled to make a claim. The shareholders who lodge a claim share the compensation in proportion to the loss suffered. As shareholder, the Lothian Pension Fund claims for compensation on all relevant class action settlements.

2.3 In addition, the Lothian Pension Fund may act as lead plaintiff on a number of class actions, holding company management to account and aiming to deter future fraud and/or loss of shareholder value. This is consistent with its approach to environment, social and governance issues. Also, by acting as a lead plaintiff, the Fund may be in a position to influence the terms of the settlement.

2.4 A court ruling in the case of Morrison vs. National Australia Bank (NAB) in 2010 has narrowed the ability of investors to seek redress under the laws of the US, particularly where shares are purchased on non–US stock exchanges.

Main report

Compensation

3.1 Compensation received by the Fund from class actions is shown in the table below.

Financial Year	US$ (000's)
Prior to 31/03/11	1,823
2011/12	317
2012/13	483
2013/14	287
2014/15 **[1]**	59
TOTAL [1]	**2,969**
[1] To 31 October 2014	

3.2 The last Committee report in December 2013 contained figures to 31 October 2013. In the remainder of that financial year a further $80k was received. There have been 11 settlements so far this financial year, with a total value of $59k. Included in this figure are two payments from Citigroup totalling $37k.

Lead Plaintiff Cases

3.3 All cases where the Fund was acting as lead plaintiff have now concluded. Summaries of the most recent cases are included Appendix 1. Compensation has been received from one of these cases but was minimal, $4.7k.

Impact of the Morrison ruling

3.4 The Morrison vs. NAB ruling continues to impacts on the Fund's ability to claim for compensation in the US. As a result of the ruling investors are increasingly looking to obtain compensation through other jurisdictions where the legal process may require investors to "opt-in" to the case prior to the trial if they wish to participate.

3.5 Officers have reviewed a small number of such cases. Considerations have included the estimated financial loss, potential for recovery, the resource needed to monitor the case and the risk of further detriment to the Fund.

3.6 Lothian Pension Fund will consider the potential benefits and risks on a case by case basis.

Measures of success

4.1 Success will be measured by the number of actions successfully pursued and the compensation received.

Financial impact

5.1 US class actions are conducted on a no win no fee basis. In the event of a case being won, the courts approve the legal costs which are deducted from the compensation fund. The Fund has recovered $3.0m in compensation from class actions.

Risk, policy, compliance and governance impact

6.1 The class action activity detailed in this report is undertaken as part of the Environmental Social and Governance (ESG) activity of the Fund which is expected to reduce risk. Class action activity is contributes to Fund stewardship and governance responsibilities.

Equalities impact

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

Sustainability impact

8.1 Class action activity is undertaken as part of the ESG activity of the Fund which is expected to contribute to the sustainability of the Fund's investments.

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds. Regular updates on class actions have been provided to stakeholders.

Background reading / external references

None

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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 – Class Actions

Summaries of the cases where Lothian Pension Fund has been a lead plaintiff are outlined below:

- The case against **Lehman Brothers** was in relation to false financial statements and mismanagement at the company prior to the collapse of the bank. The case consisted of separate claims against certain officers, the directors, underwriters and auditors. The case was filed in 2008 and the estimated loss to the Fund was $4.7m. Shares were purchased in the US. In August 2011, the case against the company officers and directors agreed to a settlement of $90m and the case against the Underwriters settled for $426m. In May 2012 the court gave final approval to the $90m settlement with Lehman directors and officers and $426m with the underwriters. Subsequently, the case against Lehman's accountants Ernst & Young (E&Y) settled for $90m. Although Lothian was lead plaintiff in the overall case it was not named as a class representative for the E&Y case because of the court's ruling severely limiting the class period against E&Y. Whilst the settlements achieved are sizeable in monetary terms, they are a relatively small proportion of the overall shareholders' losses. This, together with the fact that the Fund's trading in stock (and not any of the offering underwritten by the Underwriters) meant that it qualified for recovery in only the claim against the directors and officers. This resulted in a recovery for the Fund of $4.7k, which was received in December 2013.

- The Fund had an estimated loss of $2.0m due to holdings in the company **Wyeth**. The case was premised on Wyeth's (now Pfizer, as a result of a merger) misrepresentations of clinical trial results for the investigational Alzheimer's drug, bapineuzumab. The Fund was appointed co-lead plaintiff (along with Italian investment fund, Arca) in September 2010. In the summer of 2011, defendants moved to dismiss the case and were successful. An amended complaint was lodged but this was dismissed. An appeal brief was then lodged with the US Court of Appeals in Boston, and argument took place on September 9, 2013. In June 2014 the court decided against the appeal. This was not unexpected as misrepresentation is difficult to prove. The case is now closed.

- The case against **Genzyme** was filed in 2009 and the Fund's losses are estimated to be $3.1m. The case relates to its failure to disclose issues at one of its manufacturing facilities that caused the company to halt production of two of its top selling drugs due to contamination. The case was dismissed. However an appeal was lodged, as new information became available. In June 2014 the Court of Appeal denied the appeal against dismissal and denied leave to amend the complaint. The case is now closed.

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Service Plan Update 2014 - 2017

Item number	5.12
Report number	
Executive/routine	
Wards	All

Executive summary

The purpose of this report is to provide an update on the first quarter and second quarter of the 2014 – 2017 Service Plan, performance indicators and the key actions to enable the Fund to meet its three key objectives:

- To continue to be a top performing pension fund;
- To provide excellent customer care;
- To support and develop staff.

Overall progress is being made against the service plan objectives and it is expected that performance targets will be achieved by the end of the year.

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	

Report

Service Plan Update 2014 - 2017

Recommendations

1.1 It is recommended that the Committee should note the progress of the Fund against the 2014 – 2017 Service Plan.

Background

2.1 The purpose of this report is to provide an update on the 2014 – 2017 Service Plan, performance indicators and the key actions to enable the Fund to meet its three key objectives:

- To continue to be a top performing pension fund;
- To provide excellent customer care;
- To support and develop staff.

Main report

3.1 Progress against indicators and key actions agreed in the 2014-2017 Service Plan is set out in the appendix. The following areas are of particular note:

Implementation of the new LGPS Scotland 2015

3.2 The Fund continues to assist in the development of the Scotland-wide communications for the new LGPS. New material has been added to the Scotland-wide website www.scotlgps2015.org.

3.3 The Fund organised for the Local Government Association to deliver a training session for employers on 21 November. The event was attended by over 70 employer representatives.

3.4 The governance impact of the new scheme is addressed elsewhere on the Committee's agenda.

2014 Actuarial Valuation & Funding

3.5 Progress is being made with the 2014 actuarial valuations. The results for Scottish Homes Pension Fund are covered elsewhere on the Committee's agenda. Consultation with Lothian Buses plc continues on the results for the Lothian Buses Pension Fund.

3.6 The draft results for the Lothian Pension Fund have been shared with employers at the annual seminar on 4 December 2014. Individual employer results are expected to be issued in December. The Funding Strategy Statement has been revisited and a draft has been issued to employers for consultation.

Investment

3.7 The Fund continues to implement the 2012-17 investment strategy of the pension funds, with oversight and advice from the Investment Strategy Panel.

3.8 Committee will recall that since August the internal team have been monitoring the Asia Pacific equity portfolio previously managed by Baillie Gifford. In September, the Investment Strategy Panel considered the longer-term future of this portfolio alongside the Fund's efforts to reduce the volatility of the overall equity allocation. At the time of writing, plans are being made to make changes to the portfolio and a verbal update will be provided to Committee.

3.9 During recent months, the Fund has been in discussion with an employer within the Lothian Pension Fund regarding its exit from the Fund and the potential requirement for a lower-risk investment strategy, compared to the overall Fund. Discussions are ongoing and an update will be provided to Committee in due course.

3.10 The Scottish Homes Pension Fund actuarial valuation and investment strategy is covered elsewhere on the agenda. While the review of the funding approach for the Fund was not taken forward, the review of liability cashflow highlighted significant differences between the term/duration of Fund's investments (particularly the index linked gilts) compared to the liabilities. This has been partly due to the fact that the investments have tracked a standard market index of gilts and issuance of new government bonds over recent years has tended to be of longer duration. During September, the duration of the Fund's investments were reduced accordingly and part of the Fund's holdings are now being managed internally. This change in duration should result in the investments providing a closer match to the liabilities in the future. It also took advantage of recent outperformance of long-dated, compared to medium-dated, bonds.

Staffing

3.11 Since the last meeting of the Committee, the City of Edinburgh Council approved the creation of one or, if appropriate following legal and tax advice, two special purpose vehicles wholly owned and controlled by City of Edinburgh Council for the purposes of (1) seeking Financial Conduct Authority (FCA) registration for the activities of this team and (2) to directly employ certain key internal investment staff. Implementation work is ongoing with the initial focus on the work on the legal structure.

Performance Indicators

3.12 Performance for the key performance indicators against targets are shown in the Appendix.

3.13 One indicator is highlighted as ‘amber’ and one as ‘red’.

- The proportion of pensions administration critical work completed on time increased in the second quarter but the overall performance for the year so far remains below the target of 90%. Efforts to address historic queries on members’ records and to improve the quality and timeliness of data provision from the employer to the Fund continue.

- Less than half of staff have completed less than one day of training (one half of the target for the year). The Fund is comfortable that these issues reflect the relatively short period over which performance has been measured and initiatives are in place to address weaknesses. It is anticipated that performance indicators are expected to improve to achieve respective targets over the rest of the year.

3.14 Customer satisfaction over the 12 months to 30 September has increased from the previous quarter and is now marginally ahead of target (86.2% compared to target of 86%). Over the quarter, the annual surveys of pensioners and employers were undertaken. Pensioner satisfaction is broadly unchanged at 89% and employer satisfaction reduced from 91% to 84% over the year. The satisfaction of new members has continued to increase (79% from 67%). This is reassuring given the Fund’s efforts to improve service to these members who have been significantly less satisfied compared to other customer groups.

3.15 The 2014 staff survey has been undertaken and 37 members of staff responded to the survey. Overall satisfaction increased marginally to 65% meeting the target. The equivalent satisfaction figures for 2012 and 2013 were 53% and 63% respectively. The following table provides more detail:

	% who agree or strongly agree		
	2012	2013	2014
My manager listens to and is open to suggestions	56	79	70
My manager motivates me to achieve my full potential	53	61	59
My line manager delegates responsibility effectively	49	64	54
The reasons for change are well communicated	53	58	57
Have a say on changes that affect me before they are made	37	41	46
Feel that change affecting our service area is well managed	30	56	49
Have confidence in the decision made by the senior management team	53	69	62

	% who agree or strongly agree		
Feel involved in decision that affect your work	51	52	59
Feel that you have a sense of personal achievement	56	59	70
Feel that you have a say about the way you work	59	64	56
Believe their teams work together to find new ways to improve the service we provide	53	59	62
Learning & Development activities have helped to improve performance	49	59	62
Learning & Development activities will help to develop my career	42	57	57
Overall Satisfaction	**53**	**63**	**65**

3.16 Individual teams within the Fund have discussed the results and proposed actions for improvement and a plan has been agreed by the management team and the staff forum, a representative group of staff. The plan includes a review of the home-working pilot, greater discussion of staff suggestions within teams and an ongoing focus on communications. It includes specific actions for different teams reflecting the different types of work across the Fund.

Measures of success

4.1 Measures of success include meeting targets for performance indicators and progressing the actions set out in the Service Plan.

Financial impact

5.1 A summary of the projected and YTD administrative financial outturn compared to the approved budget for 2014/15 is shown in the table below:

	Approved Budget	Projected Outturn	Projected Variance	Budget to date	Actual to date	Variance to date
Category	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Employees	2,253	2,118	(135)	1,314	1,199	(115)
Transport & Premises	104	101	(3)	59	68	9
Supplies & Services	952	1,047	95	595	557	(38)
Investment Managers Fees	9,453	7,950	(1,503)	4,717	3,955	(762)
Other Third Party Payments	522	522	-	306	237	(69)
Depreciation	80	80	-	-	-	-
Direct Expenditure	**13,364**	**11,818**	**(1,546)**	**6,991**	**6,016**	**(975)**
Allocated Central Support Costs	**281**	**281**	**-**	**-**	**-**	**-**
Income	(772)	(1,937)	(1,165)	(429)	(1,375)	(946)
Total Cost to the Funds	**12,873**	**10,162**	**(2,711)**	**6,562**	**4,641**	**(1,921)**

5.2 The financial outturn includes year to date budget, actual expenditure and variance as at the end of October 2014. Year to date actual expenditure includes provision for services provided for which no invoice has been received.

5.3 The projection shows an underspend of approximately £2,711k. The key variances against budget are:

- Employees - £135k underspend. This is mainly due to unfilled posts across the division during the period from April to October 2014, partly offset by temporary agency costs, and transferring FCA authorisation projected costs (£50K) to Supplies & Services.
- Supplies & Services - £95k overspend. This is mainly due to FCA authorisation costs (£50K) which were budgeted under Employees. Other reasons for overspend are: system licence for the new scheme higher than expected (£25K), additional office move costs and higher than expected postage costs relating to pension payroll slips.
- Investment management fees - £1,503k underspend. This is due to termination of Rogge and Baillie Gifford mandates, with assets transferred in-house, and planned changes to portfolio structure, which will take place later in the year.
- Income: Securities lending income is significantly higher (projected to be over £1million) than for the previous year. Northern Trust commented on this: "This is due to increased levels of 'specials' activity in the US market, together with changes to the portfolio composition following recent transition activity and also there have been recent changes to UK relevant withholding tax. Prior to 1st January 2014, Northern Trust was required to either account for or collect UK tax on overseas manufactured dividend payments paid to

UK investors. It is anticipated that removal of relevant withholding tax is likely to significantly increase lending revenue for yield enhancement trading."

5.4 Committee is reminded that the investment management fees included in the budget are for mandates managed on a segregated basis (i.e. where the Fund assets are not comingled with those of other investors).

Risk, policy, compliance and governance impact

6.1 The pension funds' service plan aims to manage risk, improve compliance and governance. There are no direct implications on these issues as a result of this report.

Equalities impact

7.1 None.

Sustainability impact

8.1 None.

Consultation and engagement

9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading / external references

None.

Alastair Maclean

Director of Corporate Governance

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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	Service Plan Update

17 December 2014
Service Plan Update 2014 - 2017

Lothian Pension Fund
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Service Plan Performance Indicators – Targets & Actual Performance

	Q1 April to June	Q2 July to Sept	Target	Status
Performance				
Performance and Risk of Lothian Pension Fund	Actual 9.5%pa, Benchmark 9.0%pa. Exceeding benchmark. Risk/return measures will take some time to demonstrate the success or otherwise of the investment strategy.		Meet benchmark over rolling 5 year periods with lower risk with risk/return measures including performance in rising and falling markets.	
Audit of annual report	Complete		Unqualified opinion	
Proportion of critical pensions administration work completed within standards	87.23%	90.74%	Greater than 90%	
Percentage of employer contributions paid within 19 days of month end	96.97%	99.78%	98%	
Data quality – compliance with best practice as defined by the Pensions Regulator	Assessment will be made at year-end		Fully compliant	Not yet known
Pension Payroll complete on due dates	100%	99.97%	Yes	
Customer Indicators and targets				
Maintain Customer Service Excellence Standard	Annual assessment expected early 2015		Retain CSE Award	Not yet known
Overall satisfaction of employers, active members and pensions measured by surveys (rolling 12 month performance)	84.7%	86.2%	86%	
Proportion of active members receiving a benefit statement and time of year when statement is issued	96% By August		Over 95% by August	
Staff				
Level of sickness absence	2.98%	2.3%	4%	
Annual staff survey question to determine satisfaction with present job	65%		65%	
Percentage of staff that have completed two days training per year.	38%	47%	100%	

Our Performance - *To be a top performing pension fund*

Project	Status	Overall Progress	Project Summary
Successful implementation of the Scheme changes	✔	- The Fund's Communications Officer continues to work with the other funds to develop clear communications for employers and scheme members. A new website, http://scotlgps2015.org/ has been created to provide guidance to those affected by the LGPS changes. A newsletter which included details of the changes was issued to all active scheme members. - An internal project team will aim to ensure effective co-ordination of all aspects of the implementation of the scheme changes, including system updates and staff training.	- Communicate changes to scheme benefits to employers and members - Review internal processes and procedures Provide training for staff on new arrangements
Ensure effective Governance of the Fund	✔	- Briefing for the Pensions Committee and Consultative Panel include a meeting in October regarding the consultation of the LGPS Draft Regulations (Governance) changes and a Pensions Regulator presentation by Sarah Smart. - The Funds' response to the draft governance changes were issued to SPPA on 11 November. - In preparation for the Fund's new governance arrangements, draft constitution for the Pension Board and an updated training policy has been drafted for consideration by Committee in December.	- Engage in debate on governance changes for the Fund - Participate in the review of the structure of the LGPS in Scotland - Reinforce the separation of the Fund from the City of Edinburgh Council and review dependencies on its services - Continue to improve the Fund's approach to 'trustee' training
Monitor financial and economic pressures and scheme maturity.	✔	- Implementation of investment strategies is ongoing and is a regular agenda item at Investment Strategy Panel meetings. - Progress is being made on the 2014 Actuarial valuation. Initial results for Lothian Buses Pension Fund and Scottish Homes Pension Fund have been received. - Draft results for Lothian Pension Fund will be shared with employers in December. Draft Funding Strategy Statement will also be issued for consultation in December. - Employer covenant work has progressed and is covered elsewhere on the Committee's agenda. - Cashflow continues to be monitored monthly. Unitisation options are under review.	- Continue to implement new investment strategies - Undertake the Fund's 2014 actuarial valuation - Review Funding Strategy Statement - Improve membership and cash flow monitoring and forecasting - Review the risk profile of the participating employers and manage the pension implications of organisational and staffing changes - Explore potential options for unitisation of the Fund

Our Performance - *To be a top performing pension fund continued*

Project	Status	Overall Progress	Project Summary
Provide an efficient accurate and effective service.	✔	- Underlying investment costs have been included in the 2013/14 accounts. Information on benchmarking of investment costs and pensions administration is being presented to Committee in December. - The last part of the Payroll is the 'Immediate Payments Payroll'. This is progressing well and at final stages of testing before creating the procedures manual. Once this has been completed the Fund can make one off payments and Lump Sums from Vendors. This should be implemented by 31 December 2014. Payroll continues to run smoothly each month and preparations to transfer Fire Pensioners to SPPA are well on the way. - New finance Manager is now in post.	- Explore ways to improve transparency of investment costs. - Improve use of systems and data analysis skills. - Complete full implementation of payroll
Risk is managed effectively	✔	- Progress is being made in FCA authorisation and progress is being made in implementing the recommendations for improvements in the internal investment controls. - Risk register continues to be updated regularly.	- Investigate gaining of authorisation from Financial Conduct Authority to improve investment controls. - Ensure up-to-date and stream-lined procedure manuals for all key responsibilities are maintained
Shared services /governance	✔	- Joint working with Falkirk is progressing to implementing joint infrastructure investments via relevant staff being seconded on a part-time basis to Falkirk Council. - Progress is being made in the transfer of the Fire Fighters to the Scottish Government. This is expected to be completed by March 2015.	- Developed shared-services with Falkirk Pension Fund. - Transfer administration of the Fire Fighters pensions schemes to the Scottish Public Pensions Agency

Our Customers - *To provide excellent customer care*

Project	Status	Overall Progress	Project Summary
Develop and improve customer insight.		- Mystery shopping exercises are ongoing to check how customers who contact us by telephone and e-mail experience the service. - Recent annual pensioner and employer surveys are being analysed.	- Continue to regularly engage with all customer groups using a variety of techniques including mystery shopping and transactional surveys. - Improve analysis of consultations to ensure it remains integral to our service.
Improve timeliness and quality of customer service.		- Efforts continue to assist employers to submit member contribution details to the Fund on a monthly basis to improve data quality and member service. - Employer performance reports for 14/15 have been issued and meetings with employers are ongoing. - We have appointed Tracesmart to conduct a tracing exercise on members that we have lost touch with. - Pensions Administration workflow has been set up to distribute both urgent and non urgent cases. The volume of historic cases is reducing. - Customers' first point of contact with the Fund continues to be reviewed. Improvements have been implemented but effectiveness continues to be monitored.	- Extend usage of "employer on-line" system. - Partnership accountability – monitor and publish performance against service standards to ensure we have an effective and accountable partnership with employers. - Review the way we deal with members' first point of contact with the Fund. - Attempt to trace members who we've lost touch with. - Focus efforts on non-urgent member cases. - Re-assess our service standards and targets for members.
Develop and improve our information and access.		- As part of trainee pensions administrator project, the fund has begun to monitor customer satisfaction in regards to the service we provide via e-mail. - We are developing different ways of communicating to employers, staff and customer for example developing short training films for employers, staff and providing guidance for the 'Member online' process. - Strategy for social media program is currently being developed. It is hoped that this channel will be very helpful for specific messaging regarding the LGPS 2015 changes.	- Promote, and improve usability of, member on-line system. - Improve Frequently Asked Questions on website - Undertake trial of social media for communicating with stakeholders. - Provide more on-line training facilities for employers and members. - Develop way to monitor the ways customers contact us.

Our Staff - *To support and develop staff*

Project	Status	Overall Progress	Project Summary
Develop trust between line managers and staff and promote an open culture.		- Regular 1-1 meetings with staff take place regularly. - Efforts to improve engagement in team meetings are ongoing.	- Continue to have regular and engaging team meetings and 1-to-1s with all staff, to discuss progress, achievements and changes.
Communicate effectively, especially around change.		- Senior management team continues to communicate in a regular monthly e-update, face to face and via e-mail. In addition to this senior managers meet with small groups of staff. - The results of the staff survey have been reviewed and an action plan has been put in place.	- Continue to communicate regularly via face-to-face briefings and via email on issues affecting the division. - Review the success of major changes and learn lessons in how we manage change.
Ensure development and training for all staff.		- Training and development continues to be encouraged via 1:1 and staff meetings. The achievement of training and development is being assessed regularly. - Regular briefing sessions are held internally to inform staff about current issues and developments. - Compulsory data protection training was held during the first quarter and thereafter new members of staff are trained on key policies as part of their induction. - Project management tools are promoted internally.	- Continue to promote learning and development opportunities for all staff, including those who have already achieved qualifications - Develop ICT and project management skills.
Support staff well-being		- Staff forum continues to provide feedback from staff as do the regular 1-1s. - Flexible working trial is progressing well. Feedback from some pension administration staff about the flexible working arrangements have highlighted issues with printing and telephone cover. Managers are assessing solutions for these issues.	- Empower staff to make changes to the way they work to improve the service and efficiency, particularly around work-flow management. - Implementation of flexible working options.
Ensure team is robust and sustainable		- For the internal investment team, a special purpose vehicle is being put in place for specific terms and conditions. - Career development coaching for certain staff.	- Explore options and review plans for a sustainable team.

Pensions Committee

2.30pm, Wednesday, 17 December 2014

Risk Management

Item number	5.13
Report number	
Executive/routine	
Wards	All

Executive summary

The pension funds' risk management procedures require us to:

(i) maintain a detailed operational risk register which sets out all the risks identified and assessed by the officers on an ongoing basis, the degree of risk associated in each case and our action to mitigate these risks (the "**Operational Risk Register**"); and

(ii) produce a summary report of the risk register for the Pensions Committee and the Pensions Audit Sub-Committee which highlights the material risks facing the pension funds and identifies any new risks/concerns and the progress being made over time by the officers in mitigating the relevant risks (the "**Quarterly Risk Overview**").

The Operational Risk Register has been issued to the conveners of the Pensions Committee and the Pensions Audit-Sub-Committee.

The Quarterly Risk Overview, as at November 2014, is set out in the appendix to this report.

Links

Coalition pledges	
Council outcomes	CO26 –The Council engages with stakeholders and works in partnership to improve services and deliver on agreed objectives.
Single Outcome Agreement	

Report

Risk Management

Recommendations

1.1 Committee is requested to note the Quarterly Risk Overview.

Measures of success

2.1 Improved visibility of the risks facing the pension funds and progress in analysing/mitigating these risks. Regular, focused and relevant risk updates to the Pensions Committee and Pensions Audit Sub-Committee should increase general awareness and allow productive analysis/feedback by the Pensions Committee/Audit Sub-Committee members on these fundamental issues.

2.2 Ultimately, risk management should lead to less third party exposure, an improved financial position and have a positive impact on the reputation of the pension funds.

Financial impact

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

Risk, policy, compliance and governance impact

4.1 Please see the Quarterly Risk Overview appended to this report.

Equalities impact

5.1 None.

Sustainability impact

6.1 None.

Consultation and engagement

7.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading / external references

None.

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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 - Quarterly Risk Overview, as at November 2014

Lothian
PENSION FUND

QUARTERLY RISK OVERVIEW

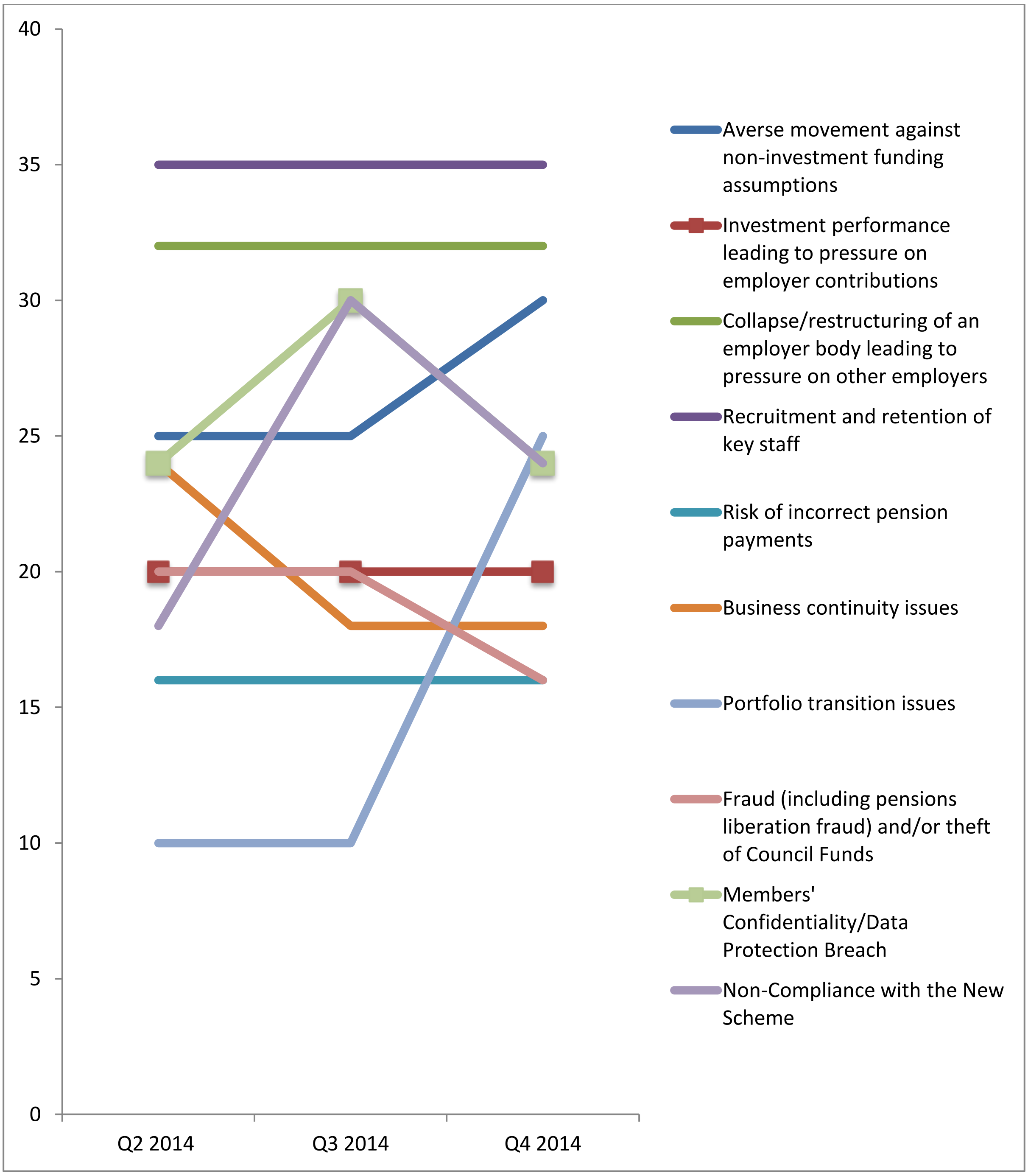
November 2014

UPDATE ON MOST NOTABLE RISKS

Risk	Update
Investment performance leading to pressure on employer contribution	The new lower volitility investment strategy continues to be implemented to mitigate this risk and more detailed reporting on the Investment Strategy has been produced for the Pensions Committee.
Adverse movement against non-investment funding assumptions leading to pressure on employer contributions	Progress continues to be made on the 2014 actuarial valuation and experience against funding assumptions and employer contributions are being assessed as part of this process.
Collapse/restructuring of an employer body leading to pressure on other employers	We have concluded our covenant analysis and will look to prioritise the actions arising from this and implement them accordingly. The employers are being made aware of their results as part of the 2014 valuation and we will look to build on this analysis and continue to monitor employer covenant on an ongoing basis.
Recruitment and retention of key staff	This risk remains high as the agreed steps to mitigate the risk associated with the Investment function continue to be implemented and, separately, there have been a number of key departures from the Pensions Administration and Employer Relations teams. In the meantime, contingency plans have been considered for the internal investment portfolios in the event of significant staff turnover. We are also looking to recruit a newly qualified solicitor to provide appropriate cover and continuity for the Legal & Risk function in anticipation of our having to meet increased compliance requirements in advance of FCA authorisation.
Risk of incorrect pension payments	Progress to achieve full integration/automation to reduce reliance on manual intervention in some processes is ongoing and is expected to complete in Q1 2015. The risk therefore remains static for now, but once appropriate solutions are implemented and internal audit have reviewed the processes, we would anticipate this risk being further reduced to the extent that it would not be worthwhile highlighting to the Committee.
Members' Confidential Data is lost or made public / breach of Data Protection Act	We are continuing to liaise with the Council's ICT and Data Protection teams regarding our systems and processes and initial feedback has been that our systems and processes are robust and fit for purpose. This risk has been reduced to reflect the work that has been done in reviewing our systems and controls and recognising that there have been no subsequent Data Protection breaches.

Fraud (including pensions liberation fraud) and/or theft of pension fund monies	We have received several responses from Action Fraud confirming that a number of the potentially fraudulent schemes we have highlighted concerns about are now under formal investigation. We have also been provided with the details of a direct contact at Action Fraud, which will greatly assist our ability to deal with these matters more quickly and provide our members with greater certainty in transfer-out processes that are reviewed with such concerns in mind. The risk of our being approached by fraudulent schemes continues, but we have lowered the overall risk here to reflect the fact that schemes are now being prosecuted/closed-down by Action Fraud and that we are better placed to make informed decisions in relation to cases that do arise.
Adverse assumptions leading to pressure on employer contributions; Fraud.	We continue to closely monitor the levels of transfers-out to determine whether there will be an increase in light of increased flexibility in Defined Contribution (DC) pensions and the decision to allow transfers from the LGPS to Defined Contribution schemes. This could have implications for funding and cash-flow and investigations on the potential implications will be taken forward.
Breach of Contract	The initial contract review has been completed and has not identified any material concerns. However, we are in the process of refining our review and so this risk should remain static until that process has been completed. We anticipate that this risk should be significantly reduced once this review has been completed.
Business continuity	Heywood Limited has outsourced the provision of the disaster recovery services to Blue Chip Limited and we await the results of the annual disaster recovery test, due to take place in November 2014 and Heywoods confirmation of their own assessment of Blue-chips systems. This risk should therefore remain static until this information has been received.
Non-compliance with the new LGPS Scheme in Scotland / Public Service Pensions Act 2013	Benefit regulations have been finalised. Implementation of the systems required to administer the new scheme remain challenging but manageable. The timetable for producing the regulations for the governance of the new scheme is challenging. We and the other Scottish administering authorities have raised concerns around the competency of the current draft regulations regarding the governance of the new scheme and await feedback from the consultation process. Progress to implement the required changes will be made in the coming months.
Portfolio Transition	Plans are being put in place to transition two investment portfolios to further implement the new investment strategy. The risk on the register has been increased reflecting the additional workload and issues involved. Following successful implementation, the risk will be reduced.

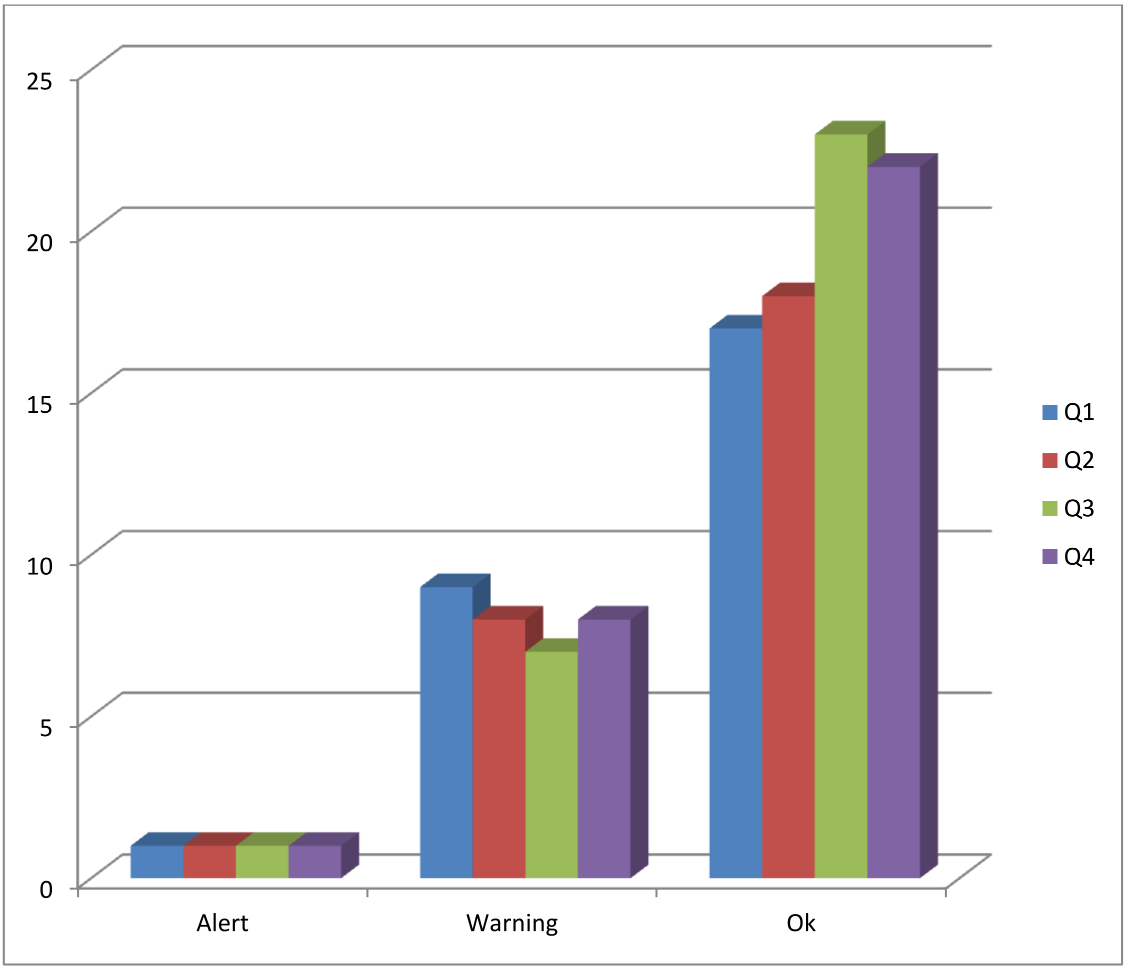
NOTABLE RISKS: PROGRESSION OF CURRENT RISK (ACCOUNTING FOR CONTROLS) IN LAST THREE QUARTERS



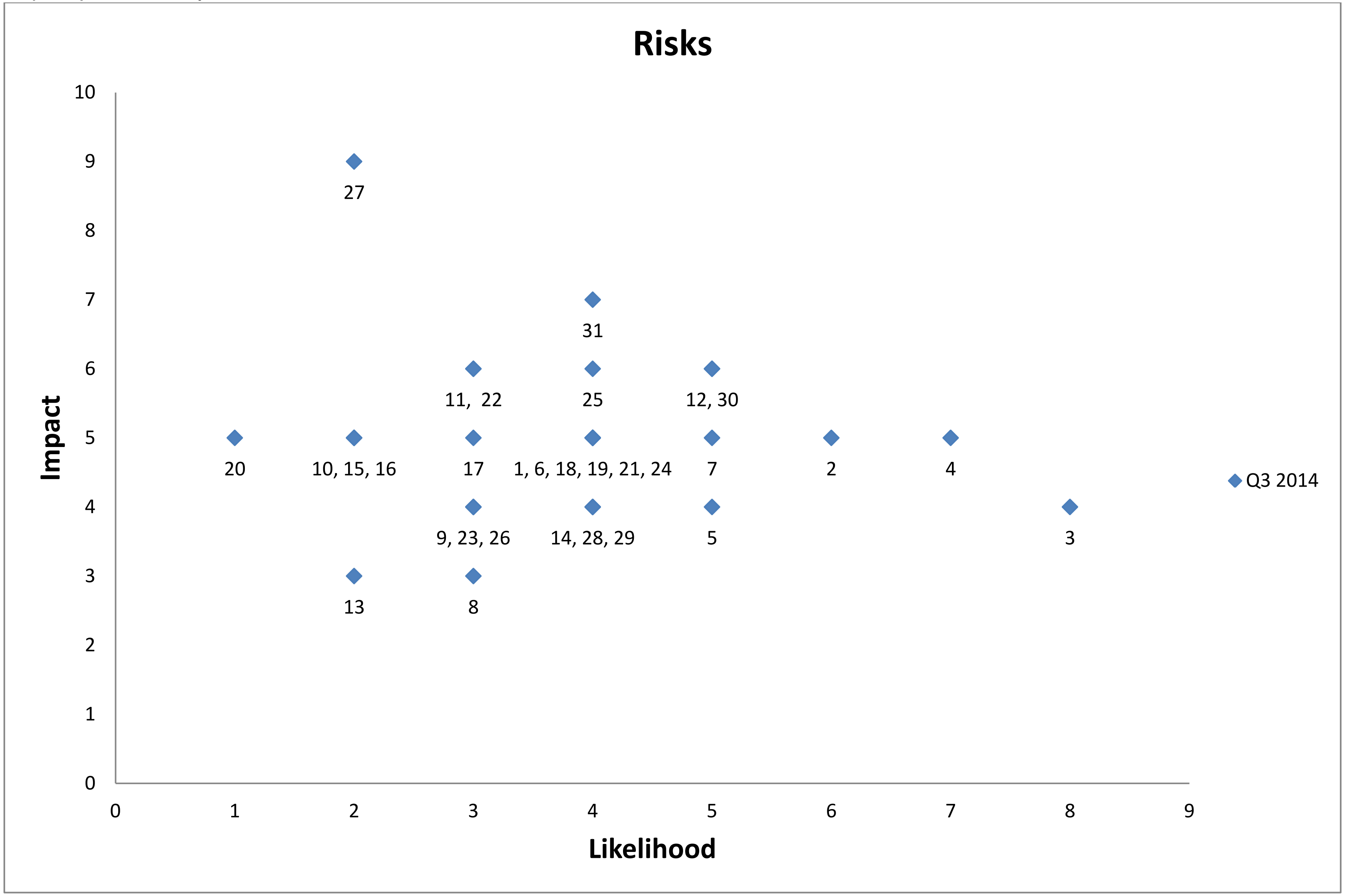
Other Key Points

	Comments
New significant risks	None
Other new risks	We are currently monitoring the resource within the division to ensure that key project receive sufficient and dedicated time.
New controls	Additional HR resource is in place for FCA and Staffing project.
Eliminated risks	None
Notable initiatives / actions	Following Council approval on 23 October 2014, progressing continues with the establishment of a Council controlled structure for the purposes of facilitating FCA authorisation and to mitigate the identified staffing risk. The arrangement with Falkirk Council will shift from a services arrangement to a pooled secondment arrangement in December 2014 which will reduce the risk to Lothian Pension Fund, subject to Council approval. Initial outcomes of the employer covenant review are being shared with guarantors and used as part of the 2014 actuarial valuation. The National Framework for Legal Services has now been completed, providing LPF with enhanced and more streamlined access to specialist legal firms in the pensions and investment sectors.
Material Litigation	None.

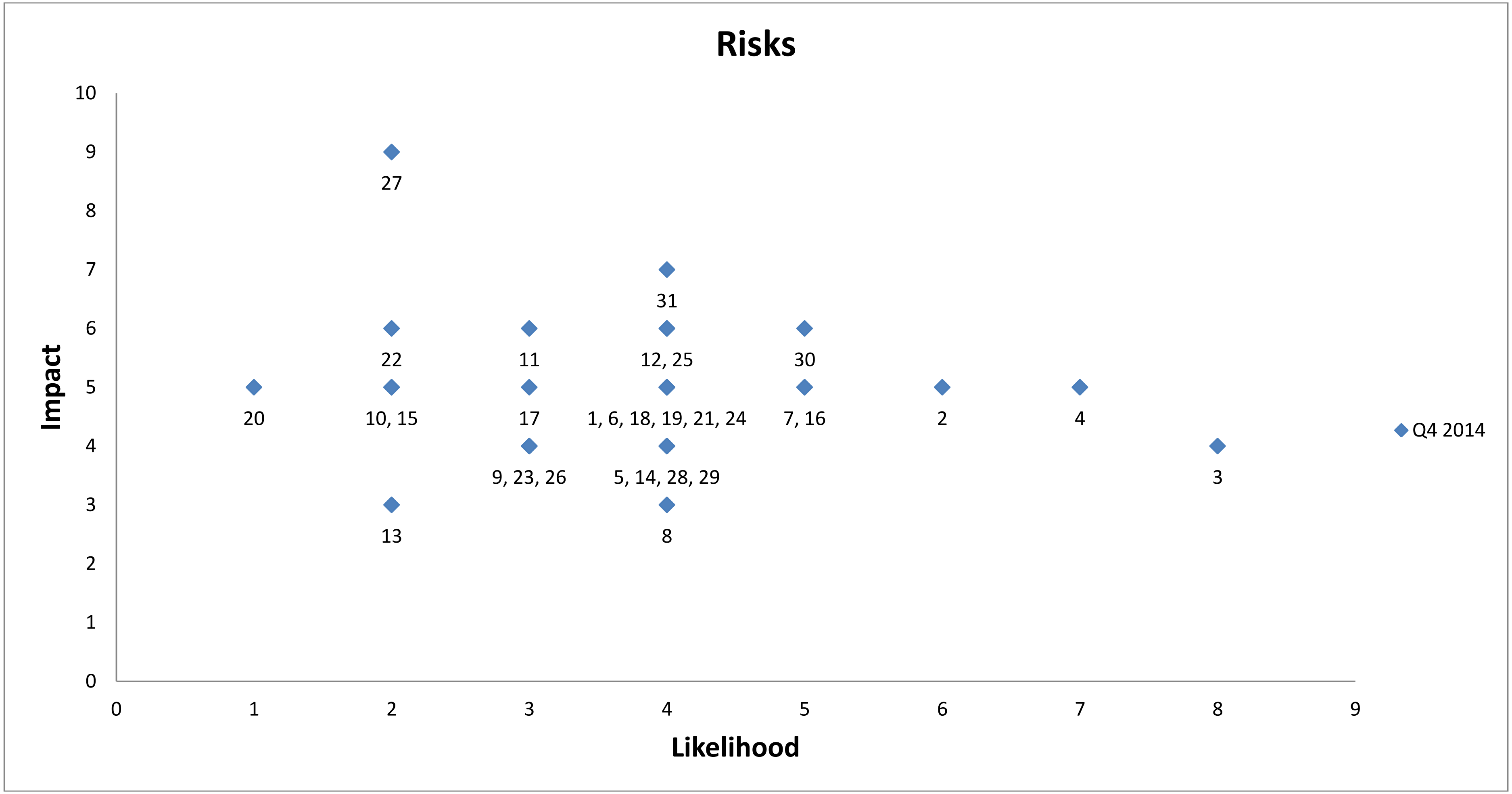
All Risks: Status Overview



Q3 (2014) All Risks: Impact and Likelihood Overview



Q4 (2014) All Risks: Impact and Likelihood Overview



Key: Risks by Number

1	Investment Performance pressure on employer contributions	15	Market abuse by investment team
2	Adverse Movement - pressure on employer contributions	16	Portfolio transition issues
3	Collapse of an employer	17	Disclosure of confidential information
4	Retention of key staff	18	Material breach of contract
5	Fraud or theft of Council/Pension Fund assets	19	Regulatory breach
6	Staff negligence	20	FOI process in accordance with law
7	Failure of IT systems	21	Incorrect communication with members
8	Employers HR decisions without consideration of fund	22	Not acting in accordance with proper authority/delegations
9	Elected members take decisions against sound advice	23	Inappropriate use of pension fund monies
10	Failure to complete annual accounts	24	Procurement/framework breach
11	Business continuity issues	25	Non-compliance with the new LGPS
12	Members' confidential data is breached	26	Claim or liability arising from shared services
13	Loss due to stock lending default	27	Late Payment of Pensions
14	Risk of incorrect pension payments	28	Unauthorised access to PensionsWEB
29	Limited or incorrect data from Employers	30	Receiving services without adequate contractual protection
31	Over-reliance on single service provider		