

Pensions Committee

2.00 p.m., Tuesday, 15 March 2016

2016-2018 Service Plan and Budget

Item number	5.11
Report number	
Executive/routine	
Wards	All

Executive summary

The Service Plan provides details of the pension fund's key challenges over the coming years including increased external scrutiny, increasing changes in employer participation in the Fund and opportunities afforded by investment pooling. It also sets budget and performance targets for the service.

Links

Coalition pledges

Council outcomes [CO26](#)

Single Outcome Agreement

2016-2019 Service Plan and Budget

Recommendations

That Committee:

- 1.1 Invites the Pension Board to raise any relevant matters or concerns which the Committee should consider;
- 1.2 Approves the two-year Service Plan for 2016-2018;
- 1.3 Approves the budget for 2016-2017;
- 1.4 Notes the indicative budget for 2017-2018.

Background

- 2.1 The Lothian Pension Fund's Service Plan has been reviewed to ensure its key performance indicators and objectives are up-to-date, clear, challenging and achievable.

Main report

- 3.1 The draft Service Plan for 2016-2018 is provided as Appendix 1.
- 3.2 The Fund's objectives remain unchanged as follows:
 - Customer First;
 - Honest & Transparent;
 - Working Together; and
 - Forward Thinking.
- 3.3 The Service Plan provides details of the pension fund's key challenges over the coming years including increased external scrutiny, increasing changes in employer participation in the Fund and opportunities afforded by investment pooling.
- 3.4 Notable initiatives are:
 - The use of the Pension Administration Standards Association to drive further improvements in service;
 - A proactive approach to investment collaboration to explore opportunities;
 - Reviewing the approach to employer covenant monitoring and management to ensure efficient and effective working.

- 3.5 The proposed budget for 2016/17 is included in the Appendix, together with an indicative budget for 2017/18. The main points to note are summarised below at “Financial Impact”.
- 3.6 Lothian Pension Fund’s Service Plan has until now been reviewed on an annual basis. It is proposed to change this to every two years i.e. the next review of the Plan will be in March 2018. However the budget for 2017/18 would be submitted to Committee for approval in March 2017.

Measures of success

- 4.1 The funds key measures of success are:
- Meeting key performance indicators; and
 - Achieving key actions set out in the Service Plan.

Financial impact

- 5.1 The proposed budget for invoiced expenditures for 2016-2017 of £12.2m and indicative figures of £12.9m for 2017-2018 are provided in the Appendix.
- 5.2 Notable movement in the proposed budget, compared to the 2015/16 budget are as follows:

Invoiced Expenditure increased by £348K, made up of

- £980K reduction in investment fees incurred via invoiced investment management, partly due to changes in investment management arrangements and partly due to lower market values;
- £700K reduction in stock lending income;
- Increased employee costs £417K, made up of increased national insurance, salary increments and implementation of new terms and conditions of staff in LPFE. Additional investment analyst support has also been included to build capacity for potential further insourcing;
- £100K additional fees pending a review of the Fund’s management of employer covenant monitoring management;
- Note that Central Support Costs are estimated due to lack of available information.

Uninvoiced Expenditure - The Budget also includes indicative costs of un-invoiced investment fees which are deducted from capital. This increased cost transparency aligns to the best practice accounting methodology adopted in the Fund’s accounts in recent years. Committee is reminded that investment fees are difficult to predict accurately in the short term as fees are typically based on market values which can be volatile and performance fees payable in a single accounting year are difficult to forecast. Similarly, transaction costs are difficult to estimate as they are dependent on the level of trading which may be affected, for example, by changes in investment managers’ mandates or opportunities in

the market. This reinforces the need for the totality of investment costs to be considered in the context of investment performance.

Un-invoiced costs are estimated to be £18.8million for year 2016-2017.

- Transactions costs are expected to reduce over time as investment portfolios have been reorganised and the new portfolios generally trade less;
- Fees deducted from capital are expected to increase with an increasing allocation to private debt.

5.3 The proposed budget continues to include £10 million contingency to be utilised in the specific event of significant departures from the internal investment team compelling the outsourcing of the investment management function.

Risk, policy, compliance and governance impact

6.1 The service plan includes plans in place to manage key risks to the 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 Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

9.2 Consultation and engagement via a number of sources has informed the service plan including:

- Customer insight including surveys and meetings;
- Feedback from the Fund's Customer Service Excellence assessment;
- Staff survey and staff meetings.

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

Single Outcome Agreement

Appendices Appendix 1 – Draft Lothian Pension Fund Service Plan 2016-2018



Service Plan 2016 – 2018



Introduction

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

Lothian Pension Fund is the second largest Local Government Pension Fund in Scotland with assets of approximately £5.0 billion, 100 employers with active members and over 70,000 members.

The Lothian Buses Pension Fund holds assets of £0.5 billion and 3,900 members, while Scottish Homes Pension Fund investments amount to £0.14 billion with 1,800 members.

How the Fund is run

All pension matters are delegated to the Pensions Committee of the Council and its members act as 'quasi trustees'. The day to day running of the Fund is delegated to the Investment and Pensions Division under the supervision of the Director of Resources.

A Pension Board, made up of 5 employers and 5 union members, assists the Pensions Committee in securing compliance with legislation and other requirements imposed by the Pensions Regulator.

Investment strategy guidance to the Committee is provided by the Investment Strategy Panel, which includes senior officers and specialist investment advisers.

The Fund has its own internal investment team who manage approximately 60% of assets. It also appoints external managers to invest in specific investment markets. Additionally, internal staff provide the pension administration, accounting and ICT functions.

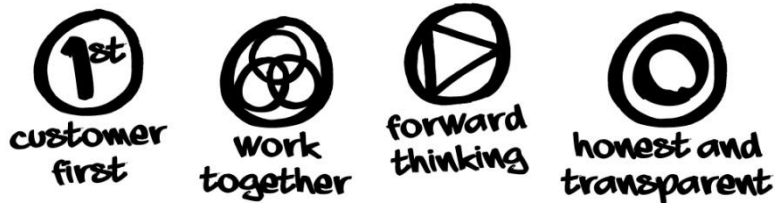
The Fund maintains a comprehensive website for easy access to all relevant pension information and this is found at www.lpf.org.uk. This includes the Annual Report & Accounts of the three pension funds.

Policies

The policies of the Fund, including the Statement of Investment Principles, Funding Strategy Statement, Pensions Administration Strategy and Pensions Discretions Policy are published on the Fund's website.

Our Service

The Fund is committed to continuously developing to provide the best possible service to our customers. To ensure we meet this aim we have set the following four objectives for our service to:



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

To enable us to achieve these objectives we must:

- meet our statutory **responsibilities**
- develop **our service** beyond our statutory responsibilities taking into account internal and external influences. This will ensure that the Fund continuously improves to deal with the potential demands of the future.

Our Responsibilities

The Fund is responsible for all aspects of the pension funds, including investment, administration and accounting. The principal responsibilities are:

- Carrying out the funding strategy aimed at ensuring the assets of the Funds are sufficient to meet pension liabilities.
- Investing fund assets, implementing investment strategy and investing responsibly.
- Administering pension services including calculating and paying benefits.
- Safe keeping and accounting of fund assets and preparing the Fund's annual report and accounts.
- Providing an excellent service to key stakeholders, including, members of the Fund and employers.
- Ensuring the Fund has committed, knowledgeable and customer-focused staff.

To ensure we meet our responsibilities, we use a range of indicators covering different aspects of the service. We set challenging targets for the performance indicators and monitor performance against the targets on a regular basis.

Performance Indicators

	2014/ 2015	2015/ 2016	2016/ 2017	2017/ 2018
Maintain Customer Service Excellence Standard (CSE)	Retain award (Yes)	Retain award (Yes)	Retain	Retain
Overall satisfaction of employers, active members and pensioners measured by surveys	86% (89%)	87% (84.6%)*	88%	89%
Proportion of members receiving a benefit statement and by August	Over 95% (96%)	Over 96% (98%)	100%	100%
Performance and Risk of Lothian Pension Fund	Actual 9.5%pa. Benchmark 8.8%pa	*Actual 8.4%pa Benchmark 6.9%pa	Meet benchmark over rolling 5 year periods with lower risk with risk/return measures including performance in rising and falling markets	
Proportion of critical pensions administration work completed within standards	Greater than 90% (90%)	Greater than 90% (92.5%)*	Greater than 90%	Greater than 90%
Audit of annual report	Unqualified opinion (Yes)	Unqualified opinion		
Percentage by value of pension contributions received within 19 days of the end of the month to which they relate	98% (98%)	99% (98.6%)*	99%	99%
Data quality - compliance with best practice as defined by The Pensions Regulator	Fully compliant (Yes)	Fully compliant		
Monthly pension payroll paid on time	Yes (Yes)	Yes (Yes)*	Yes	Yes
Level of sickness absence	4.0% (2.1%)	4.0% (0.9%)*	4.0%	4.0%
Annual staff survey question to determine satisfaction with present job	65% (65%)	67% (73%)	75%	77%
All staff complete at least two days training per year	2 days (Yes)	Yes (on track)*	Yes	Yes

* Performance at financial year to date at the time of writing is shown in brackets against previous targets

Continuous improvement

We are committed to continuously improving our service and we take a number of factors into account when developing the service including:

<p>Political & Regulatory</p>	<p>Governance changes were introduced in April 2015 with a new Pension Board and a national Scheme Advisory Board. In addition the Pensions Regulator now has regulatory oversight of public sector pension schemes</p> <p>The Local Government Pension Scheme (LGPS) in England & Wales is reviewing options to implement investment pooling arrangements. A review of the structure of the LGPS in Scotland is expected to be undertaken.</p> <p>Members over age 55 are now able to transfer their LGPS benefits to defined contribution arrangements which allow immediate access to the cash transferred. The Fund is seeking authorisation from the Financial Conduct Authority.</p> <p>The abolishment of contracting out of the State Earnings Related Pension Scheme in April 2016 will mean increases in national insurance contributions for employers and members, as well as an onus on the Fund to reconcile members' contracting out with those of the government. The changes to benefits in the LGPS, pension taxation allowances and new pension freedoms make the administration more complex and more difficult for members to understand.</p>
<p>Economic</p>	<p>Continuing budgetary constraints across the public sector are expected to lead to further reductions in employee numbers. There is also a risk that members decide to opt-out of the Fund on grounds of affordability or lack of appreciation of the value of pension benefits. Together with the new pension freedom and pension auto-enrolment, these could impact on the Fund's membership and liabilities.</p> <p>Economic growth in most parts of the world appears to be stuttering and yields on government bonds continue to move to historic lows.</p> <p>The results of the 2014 actuarial valuation and employer covenant analysis have highlighted the need for different funding and investment options for certain employers. With increased pressure on employer contributions, there continues to be a need to improve efficiency and reduce costs.</p>
<p>Customer Insight</p>	<p>The Fund has a wide range of internal and external customers. We use a variety of engagement techniques to develop our understanding of different customer groups and our staff. Their needs, experiences of our service and their perception of the Fund help us to continually improve and become more efficient and effective.</p>
<p>Technology</p>	<p>Advances in information technology facilitating on-line self-services and data transfer for both scheme members and employers.</p>
<p>Environmental</p>	<p>The Fund continues to strive to be an active shareholder to enhance the long-term value of our investments.</p>
<p>Scrutiny & Benchmarking</p>	<p>The Fund uses feedback from scrutiny of our services to inform developments. Such scrutiny includes internal and external audit, cost benchmarking and external awards (Customer Service Excellence and Investors in People).</p>
<p>Risk Management</p>	<p>The Fund is committed to a strong control environment to ensure that risks are identified, understood, managed and monitored appropriately. The risks faced by the Fund change over time and ongoing management of risk is crucial.</p>



Customer First

The Fund has a range of customers including members of the Fund, employers, government departments and regulators. We aim to provide our customers with the very best service.

Our Customer Service Excellence award demonstrates that we consistently strive to meet our customers' needs. In 2016 we will be working with the Pension Administration Standards Association to further improve our service.

We also need to continue to strive improve our partnership working with our employers to deliver the service our customers expect.

The general lack of awareness of our members of the value of their pension benefits, and the contributions made by their employer, remains a concern. With increases in national insurance contributions in April 2016 it is important to ensure the scheme is appreciated as a valuable part of an employee's remuneration.

Developments in technology mean we have are able to give customers greater access to information regarding their pension.

Action	Description
Develop and improve customer insight	<ul style="list-style-type: none"> – Develop and refresh our insight of our customers to ensure we capture changing needs. – Develop our understanding of the ways customers contact us. 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.
Develop and improve customer awareness	<ul style="list-style-type: none"> – Develop communications for members on the value of the scheme. – Develop communications with employers on funding and investment ahead of the 2017 actuarial valuation. – Improve external communications and understanding of investment strategy.
Improve timeliness and quality of customer service	<ul style="list-style-type: none"> – Complete roll-out of “employer on-line” system. – Partnership accountability – continue to monitor and publish performance against service standards to ensure we have an effective and accountable partnership with employers. – Enhance members' first point of contact with the Fund. – Review resourcing of changes in employer admission status.
Develop and improve our information and access	<ul style="list-style-type: none"> – Improved access to services via member on-line system. – Monitor the Fund's trail of social media for communicating with stakeholders. – Review and update the Fund's new website based on feedback from employers and members. – Retender pension administration software services.



Forward Thinking

With the changes to the Local Government Pension Scheme, reducing pension taxation relief and new pensions freedom, pension administration is becoming more complex for both the Fund and employers. By striving to continually improve our performance, the Fund will be position to meet these challenges.

The results of the 2014 actuarial valuation and employer covenant analysis have highlighted the need for different funding and investment options for certain employers.

The Local Government Pension Scheme (LGPS) in England & Wales is expected to implement investment pooling arrangements. The Fund will continue to take a proactive approach to investment collaboration, building on its exoerience of working with Falkirk Pension Fund, and work with other LGPS funds to explore collaborative/pooled arrangements.

Action	Description
Monitor financial and economic pressures and scheme maturity	<ul style="list-style-type: none"> – Manage the risks of the participating employers including updates of admission agreements. – Implement different funding and investment options for certain employers in Lothian Pension Fund with new unitisation approach. – Continue to monitor membership and cash flow.
Provide an efficient, accurate and effective service	<ul style="list-style-type: none"> – Improve systems skills and data analysis, particularly performance statistics and data quality measures. – Reconcile members’ contracting out records (GMPs) with those of the government. – Put in place Service Level Agreements for key services provided by City of Edinburgh Council. – Continue to explore further efficiencies.
Shared services	<ul style="list-style-type: none"> – Explore opportunities for further investment collaboration and pooling.



Honest & Transparent

The Fund is committed to supporting a culture of openness, honesty and transparency, both internally and externally. Members and employers are an integral part of the Fund’s governance.

All public sector pension schemes are now subject to greater scrutiny by the Pensions Regulator and a Scheme Advisory Board. The Fund also has a Pension Board, made up of employers and members.

By adopting an open culture, the Fund encourages staff to contribute to the continuous improvement of the service. This includes learning from mistakes in a positive way.

The risks faced by the Fund change over time and ongoing management of risk is crucial. The Fund is committed to a strong control environment to ensure that risks are identified, understood, managed and monitored appropriately. Management of risks are reported on a regular basis to the Pensions Committee and Pension Board.

Action	Description
<p>Ensure effective Governance</p>	<ul style="list-style-type: none"> – Continue to embed the new Pension Board in to the Fund’s governance. – Continue to improve the Fund’s approach to training for the Pensions Committee and Pension Board. – Monitor and respond to the requirements of the Scheme Advsiory Board. – Participate in the review of the structure of the LGPS in Scotland.
<p>Risk is managed effectively</p>	<ul style="list-style-type: none"> – Progress with application for authorisation from Financial Conduct Authority to improve investment controls. – Continue to review and update procedure manuals. – Continue to develop integration of environmental, social and governance research into investment decision making. – Progress with updates of employer admission agreements.

Working Together



Our people are at the very heart of our business and key to delivering our responsibilities and objectives. We work hard to equip our staff with the right skills and support to drive the service forward. Staff receive support in studying for professional qualifications related to the service.

As a relatively small team of 55, there are risks associated if the Fund were to experience high staff turnover, particularly in key positions requiring specialist knowledge. Specialist investment staff are now employed via a special purpose vehicle to facilitate relevant and appropriate terms and conditions. Consideration will be given to a phase two where all the pension fund staff would be transferred to the special purpose vehicle.

Feedback from the 2015 staff survey highlighted that staff could be more involved in changes that affect their work and that more regular feedback on performance would be beneficial.

Action	Description
Develop trust between line managers and staff	<ul style="list-style-type: none"> – Continue to have regular team meetings and 1-to-1s with all staff to discuss progress, achievements and changes – Ensure all team meetings are engaging, encourage suggestions and provide feedback on suggestions
Communicate , and engage effectively especially around change	<ul style="list-style-type: none"> – Continue to communicate regularly via face-to-face briefings and via email on issues affecting the division – Increase involvement of staff in changes which affect their work – Provide more regular feedback on individual performance
Ensure team is robust and sustainable	<ul style="list-style-type: none"> – Monitor and manage potential change in team dynamics and morale following the transfer of the investment team to the special purpose vehicle – Consider potential for further transfer of pension fund staff – Review ways of working in other areas where specialist knowledge exists
Celebrate Success	<ul style="list-style-type: none"> – More proactive approach to celebrating successes of key milestones – Put in place annual achievement newsletter – Improve communication of performance indicators
Ensure development and training for all staff	<ul style="list-style-type: none"> – Continue to promote learning and development opportunities for all – Continue to deliver programme of internal Continuous Professional Development sessions – Develop ICT and project management skills

Our Budget

The budget for 2016-17 and indicative figures for 2017-2018 are as follows:

	Projected 2015/16 £000	Budget 2015/16 £000	Movement £000	Budget 2016/17 £000	Movement £000	Indicative Budget 2017/18 £000
Employees	2,253	2,489	417	2,906	89	2,995
Property Costs	190	188	7	195	2	197
Plant and Transport	35	37	4	41	0	41
Supplies and Services	1,037	1,095	100	1,195	-1	1,194
Third Party Payments	751	1,286	89	1,375	3	1,378
Investment Managers Fees	7,800	8,100	-980	7,120	552	7,672
Support Costs	315	276	24	300	0	300
Capital Funding	91	80	7	87	0	87
Gross Expenditure (Invoiced)	12,472	13,551	-332	13,219	645	13,864
Receipts	-153	-157	-20	-177	-5	-182
Income - Other	-1,050	-1,500	700	-800	0	-800
Total Income	-1,203	-1,657	680	-977	-5	-982
Net Expenditure (Invoiced)	11,269	11,894	348	12,242	640	12,882
Property Operational Costs	1,000	1,000	0	1,000	0	1,000
Investment fees deducted from Capital	15,224	15,624	976	16,600	0	16,600
Transaction Costs	2,800	2,300	-1,100	1,200	0	1,200
Indicative Net Expenditure (Uninvoiced)	19,024	18,924	-124	18,800	0	18,800
Total Indicative Expenditure	30,293	30,818	224	31,042	640	31,682
Pension Administration	1,855	2,041	20	2,061	22	2,083
Investment Management	28,438	28,777	204	28,981	618	29,599
Investment Managers Fee Contingency	0	10,000	0	10,000	0	10,000

Our Budget continued

The budget for 2016-17 and indicative figures for 2017-2018 and are as follows:

Capital Expenditure

	Projected	Budget		Budget		Indicative
	2015/16	2015/16	Movement	2016/17	Movement	Budget
	£000	£000	£000	£000	£000	2017/18
						£000
Loan Facility - LPFE	n/a	250	-250	0	0	0
- LPFI	n/a	75	0	75	-75	0
LPFI Share Capital	n/a	36	0	36	-36	0
Total Capital Expenditure	34	361	-250	111	-36	0