

# Pensions Committee

**2.00 p.m., Wednesday, 28 September 2016**

## **2016 - 2018 Service Plan Update**

<b>Item number</b>	5.10
<b>Report number</b>	
<b>Executive/routine</b>	
<b>Wards</b>	All

### **Executive summary**

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The purpose of this report is to provide an update on progress against the 2016 – 2018 Service Plan, performance indicators and the key actions to enable the Fund to meet its four key objectives:

- Customer First;
- Honest & Transparent;
- Working Together; and
- Forward Thinking.

Overall progress is being made against the service plan objectives.

Whilst three of our indicators are behind target, there are currently no reasons why performance targets should not be achieved by the end of the year.

### **Links**

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**Coalition pledges**

**Council outcomes**

[CO26](#)

**Single Outcome Agreement**

## 2016 - 2018 Service Plan Update

### Recommendations

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Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider.
- 1.2 Note the progress of the Fund against the 2016 – 2018 Service Plan.

### Background

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- 2.1 The purpose of this report is to provide an update on the 2015 – 2018 Service Plan, performance indicators and the key actions to enable the Fund to meet its four key objectives:
  - Customer First;
  - Honest & Transparent;
  - Working Together; and
  - Forward Thinking

### Main report

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- 3.1 Progress is being made against the service plan and this report includes areas of particular note. The following areas are covered elsewhere on the agenda:
  - LPFE Limited and LPFI Limited Annual Report
  - Fiduciary Duty & Update on Governance
  - Funding Update and Preparation for 2017 Actuarial Valuation
  - Employers Participating in Lothian Pension Fund
  - Collaboration Update.
- 3.2 At its recent meeting, the Pensions Audit Sub- Committee also considered Pensions Administration Data Quality and Fraud Prevention.
- 3.3 **Investments and Brexit:** The Investment Strategy Panel discussed the effect of Remain and Leave votes at its meeting in early June. Panel concluded that the markets appeared to be mispricing the risk of Brexit - the downside risk of Brexit was significantly bigger than the upside reward of Remain. For Scottish Homes Pension Fund, the planned reduction in equities by 5% and increase in bonds (consistent with the existing de-risking strategy) was implemented head of the vote. To protect the Lothian Pension Fund and the Lothian Buses Pension Fund, Panel agreed to increase exposure to German government bonds by

approximately 2% and reduce investment exposure to European equities of approximately 2% of each Fund. Futures were used to implement these decisions and they were reversed on 28 June. Following the Brexit vote, sterling fell sharply against other currencies, stock markets were weak and bond markets were strong. The Funds' investments in overseas markets benefitted from the fall in sterling. These positions protected the Lothian Pension Fund and the Lothian Buses Pension Fund by approximately 0.17% (£m). Panel met in July for a special meeting where it was agreed that no further action was necessary.

- 3.4 **FCA registration:** On 24 June, LPFI, the Fund's regulated investment services vehicle, received authorisation from the Financial Conduct Authority (FCA). This authorisation allows the Fund to provide investment advisory and arranging services which will support the activities and development of the investment team in managing the portfolios of assets. It also will allow further collaboration with other pension funds and institutional investors. A update is provided elsewhere on the Committee's agenda.
- 3.5 **Potential merger of Lothian Buses Pension Fund and Lothian Pension Fund:** As agreed by Committee in March 2016, the option for Lothian Buses Pension Fund to be merged into Lothian Pension Fund is being explored. Work is being progressed and Investment Strategy Panel considered the issue in September concluding that from an investment and administration perspective, there are very clear benefits from a merger including improved diversification benefits and opportunities for Lothian Buses Pension Fund. Such a merger is made possible by the new unitisation system. Merger raises some important governance questions which need to be explored. These, together with consultation with stakeholders, will be taken forward over the coming months.
- 3.6 **Pension administration system:** The pension administration software system contract expires in October 2018. The Fund has begun the preparatory procurement stages of a tender as any change to provider will need long and careful planning. The tender stipulates the provision of an integrated administration service, including member benefit calculations and pensioner payroll, together with member self-service module and employer data portal.
- 3.7 **Pensions Administration Standards Association (PASA):** The Pensions Regulator and the Department of Work and Pensions have both identified that good administration can be demonstrated by independent accreditation. PASA Accreditation recognises pension organisations that have evidenced compliance with the standard. Given the existing accreditation with Customer Service Excellence, the Fund is well positioned relative to the 5 standards which are as follows:
1. Service Agreement
  2. Measurement and Reporting
  3. Operational Controls and Procedures
  4. Data
  5. People

However the Fund is using the framework to make further improvements, the main focus is currently on reviewing and updating procedure manuals. Other improvements include more extensive performance analysis. The Fund will consider applying for full accreditation later in the year. The accreditation involves an on-line application backed up with documentary evidence and a site visit by an Independent Assessor. PASA accreditation is valid for two years from the date it is awarded.

- 3.8 **Stewardship services:** As approved by Committee in March, the Hermes EOS contract has been extended until March 2017. The extension was agreed in order to allow the Fund to appoint a provider from the National LGPS Framework. Lothian Pension Fund staff, together with representatives from a range of funds, helped to set up the framework. Bids were submitted in July and the evaluated during August. It is anticipated that appointments to the framework will be finalised in September.
- 3.9 **Custodian services:** The contract with the Funds custodian, Northern Trust, was due to expire 28 February 2017. The Fund took up the option of extending its contract by 3 years (taking the contract up to 29 February 2020), after conducting a benchmarking exercise to ensure that value for money was being obtained by the Fund.

#### **Performance Indicators**

- 3.10 Performance Indicators for the first quarter are provided in the attached appendix.
- 3.11 **Annual benefit forecasts:** We issued 99.9% annual benefit statements to active and deferred members (where we held a valid address) within the Pension Regulator's statutory deadline of 31 August 2016. Work continues on statements for 159 members.
- 3.12 Three indicators are highlighted as 'amber':
- Customer satisfaction is below target (86.2% compared to 88%). Satisfaction of members with our email service is improving but remains below target. The annual survey to pensioner members has been issued and results will be reported to the Committee in December. Due to variations in the numbers of members responding to surveys and the impact on the overall satisfaction, the measure is now being calculated as the average of satisfaction of pensioners, employers (both measured by annual surveys) and members' satisfaction with specific transactions;
  - The payment of employer contributions for the quarter (98.8%) is marginally behind target of 99%, primarily due to Scottish Police Services and Scottish Futures Trust paying contributions late. In total, there were 18 late payments in the first three months of the year;
  - 62.5% of staff had completed their pro-rata training target up to 30 June 2016. The Fund is comfortable that this is a relatively short period over which training has been measured and the target should be achieved by the end of the year.

- 3.13 The Fund has won the Professional Pensions award for the best Communications in the Public Sector. The award submission covered general communications as well as those for the introduction of the new 2015 scheme.
- 3.14 At the 2016 LAPF Investment awards, Lothian Buses Pension Fund won the award for LGPS Fund of the Year of less than £1.5billion. Lothian Pension Fund won in the categories of Investment Strategy of the Year and Investment Performance of the Year. In two other categories, Lothian Pension Fund was 'Highly Commended' for the Infrastructure and Large LGPS Fund of the Year Awards.

### **Membership and Cashflow monitoring**

- 3.15 Officers of the Fund continue to monitor movements in membership numbers in order to assess potential implications upon cashflow. Early retirement initiatives could trigger significant and immediate outflows due to the payment of tax free lump sums and pensions and reductions in contributions received. However payment of strain costs by the employer help to mitigate current cashflow pressures.
- 3.16 The below summary details the cash flows as at the end of July and projections for the financial year. This has been prepared on a cash flow basis (compared to the accruals basis of the year end financial statements and budget projections).

<b>Lothian Pension Fund</b>	<b>2016/17 YTD</b>	<b>2016/17 Projected</b>
<b><u>Income</u></b>	<b>£'000</b>	<b>£'000</b>
Contributions from Employers	50,086	145,000
Contributions from Employees	12,886	39,300
Transfers from Other Schemes	2,055	4,700
	<b>65,027</b>	<b>189,000</b>
<b><u>Expenditure</u></b>		
Pension Payments	(46,245)	(141,000)
Lump Sum Retirement Payments	(15,652)	(49,000)
Refunds to Members Leaving Service	(214)	(530)
Transfers to Other Schemes	(2,081)	(5,250)
Administrative expense	(589)	(1,865)
	<b>(64,781)</b>	<b>(197,645)</b>
<b>Net Additions/(Deductions) From Dealings with Members</b>	<b>246</b>	<b>(8,645)</b>

<b>Lothian Buses Pension Fund</b>	<b>2016/17 YTD</b>	<b>2016/17 Projected</b>
<b><u>Income</u></b>	<b>£'000</b>	<b>£'000</b>
Contributions from Employers	2,496	7,235
Contributions from Employees	690	1,975
Transfers from Other Schemes	10	30
	<b>3,196</b>	<b>9,240</b>
<b><u>Expenditure</u></b>		
Pension Payments	(2,771)	(8,450)
Lump Sum Retirement Payments	(1,310)	(3,000)
Refunds to Members Leaving Service	(7)	(25)
Transfers to Other Schemes	-	(72)
Administrative expense	(37)	(112)
	<b>(4,125)</b>	<b>(11,659)</b>
<b>Net Additions/(Deductions) From Dealings with Members</b>	<b>(929)</b>	<b>(2,419)</b>

<b>Scottish Homes Pension Fund</b>	<b>2016/17 YTD</b>	<b>2016/17 Projected</b>
<b><u>Income</u></b>	<b>£'000</b>	<b>£'000</b>
Contributions from Employers	<b>675</b>	<b>675</b>
<b><u>Expenditure</u></b>		
Pension Payments	(2,281)	(6,880)
Lump Sum Retirement Payments	(192)	(512)
Transfers to Other Schemes	(56)	(100)
Administrative expense	(19)	(55)
	<b>(2,548)</b>	<b>(7,547)</b>
<b>Net Additions/(Deductions) From Dealings with Members</b>	<b>(1,873)</b>	<b>(6,872)</b>

- 3.17 Due to the City of Edinburgh Council ongoing transformation project, there continues to be a significant number of leavers during 2016. It is expected that Lothian Pension Fund will have a negative cash flow position at the end of the year, whereby pension payments exceed total contributions received. Increased investment income has been targeted in recent years for this scenario. Investment income is expected to exceed net cashflow for the foreseeable future.
- 3.18 It is expected that the number of active members for Lothian and Lothian Buses Pension Funds will continue to decrease during the year, causing a fall in contributions and increase in pension and lump sum payments. Year to date the increase in pensioner payments for Lothian Pension Fund has been offset by one off employer contributions for strain costs.
- 3.19 In Lothian Buses and Scottish Homes Pension Funds, expenditure is anticipated to continue to exceed income.

## 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 year-to-date financial outturn compared to the approved budget for 2015/16 is shown in the table below:

Category	Approved Budget £'000	Projected Outturn £'000	Projected Variance £'000	Budget to date £'000	Actual to date £'000	Variance to date £'000
Employees	2,906	2,643	(263)	969	809	(160)
Transport & Premises	236	236	-	79	73	(6)
Supplies & Services	1,195	1,180	(15)	398	361	(37)
Investment Managers Fees	7,120	5,250	(1,870)	2,373	1,650	(723)
Other Third Party Payments	1,375	1,095	(280)	458	253	(205)
Central Support Costs	300	300	-	100	100	-
Depreciation	87	88	1	29	29	-
<b>Direct Expenditure (Invoiced)</b>	<b>13,219</b>	<b>10,792</b>	<b>(2,427)</b>	<b>4,406</b>	<b>3,275</b>	<b>(1,131)</b>
Income	(977)	(982)	(5)	(326)	(501)	(175)
<b>Net Expenditure (Invoiced)</b>	<b>12,242</b>	<b>9,810</b>	<b>(2,432)</b>	<b>4,080</b>	<b>2,774</b>	<b>(1,306)</b>
<b>Indicative Expenditure (Uninvoiced)</b>	<b>18,800</b>	<b>18,800</b>	<b>-</b>	<b>6,267</b>	<b>6,267</b>	<b>-</b>
<b>Total Cost to the Funds</b>	<b>31,042</b>	<b>28,610</b>	<b>(2,432)</b>	<b>10,347</b>	<b>9,041</b>	<b>(1,306)</b>

- 5.2 The financial outturn includes year to date budget, actual expenditure and variance as at the end of July 2015. Year to date actual expenditure includes provision for services incurred but for which no invoice has yet been received. Uninvoiced expenditure (i.e. investment management costs deducted from capital) is assumed to be in-line with the budget.
- 5.3 The projection shows an underspend of approximately £2,433k. The key variances against budget are:
- **Employees - £263k underspend.** This is mainly due to unfilled posts across the division during the period from April to July 2015. Various recruitment processes are underway.
  - **Investment management fees - £1,870k underspend.** The budget for 2016/17 was set prior to the in-sourcing of a global equity portfolio in March 2016.
  - **Other Third Party Payments - £280k underspend.** This is primarily due to delays in the splitting out research costs from broker's fees.

## Risk, policy, compliance and governance impact

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- 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

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- 7.1 None.

## Sustainability impact

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- 8.1 None.

## Consultation and engagement

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

## Background reading/external references

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None

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## Links

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### 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 – Performance Indicators



## Appendix 1

### Service Plan Performance Indicators – Targets & Actual Performance

	Q1 April to June	Q2 July to Sept	Q3 Oct to Dec	Target	Status
Customer First					
Maintain Customer Service Excellence Standard	Annual assessment will be carried out early in 2017			Retain CSE Award	Not yet known
Overall satisfaction of employers, active members and pensions measured by surveys	Rolling 12 month performance is 86.2%			88%	⚠
Proportion of active members receiving a benefit statement and time of year statement is issued	99.9% issued by 31 August 2016			100%	✅
Forward Thinking					
Performance and Risk of Lothian Pension Fund	Actual 10.4%pa, Benchmark 8.4%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.	✅
Proportion of critical pensions administration work completed within standards	92.4%			Greater than 90%	✅
Honest & Transparent					
Audit of annual report	Achieved			Unqualified opinion	✅
Percentage of employer contributions paid within 19 days of month end	98.8%			99%	⚠
Data quality – compliance with best practice as defined by the Pensions Regulator	Assessment will be made at year-end			Fully compliant	Not yet known
Monthly Pension Payroll paid on time	Yes			Yes	✅
Working Together					
Level of sickness absence	0.72%			4%	✅
Annual staff survey question to determine satisfaction with present job	-			75%	Not yet known
Percentage of staff that have completed two days training per year.	62.5%			100%	⚠