

Pensions Committee

2.00 p.m., Monday, 20 March 2017

Budget for 2017/18

Item number	5.11
Report number	
Executive/routine	
Wards	All

Executive summary

The budget for 2017/18 sets out the Pension Fund's expected expenditure for 2017/18 and also an indicative budget for 2018/19 is provided. Please note that the budget reflects the totality of the three funds, Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.

Links

Coalition pledges	
Council outcomes	CO26
Single Outcome Agreement	

Budget for 2017/18

Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider;
- 1.2 Approve the budget 2017/2018; and
- 1.3 Note the indicative budget 2018/2019.

Background

- 2.1 For many years, Lothian Pension Fund has prepared its budget separately to the City of Edinburgh Council. The Fund's 2016/17 budget was prepared in conjunction with its Service Plan. The Council's policy on Service Plans has changed from these being prepared annually to biennially. Accordingly, this is the first occasion where the Pension Fund's budget has been reported for approval separately from its Service Plan.
- 2.2 The budget 2017/18 has been prepared after reviewing the 2016/17 budget and adjusting for changes in the Funds expenditure and income.

Main report

- 3.1 The proposed budget 2017/18 and indicative budget 2018/19 are included in Appendix 1. The main points to note are summarised below at "Financial Impact".
- 3.2 The budget does not include costs considered in the staffing and collaboration business cases, which are reported separately on this agenda.

Measures of success

- 4.1 The Fund's key measure of success is to control and monitor costs to ensure expenditure remains within the confines of the budget approved by Committee.

Financial impact

- 5.1 The budget proposed for net invoiced expenditures for 2017-2018 totals £10.7m, with an indicative net invoiced outlay for 2018-2019 of £11.5m. A breakdown is provided in Appendix 1.
- 5.2 The proposed budget for invoiced costs represents a £1.5m saving to the comparable 2016/17 budget. The key changes comprise the following:

	Increase/ (Decrease) £'000
<u>Investment Management fees</u> – Reduction in external fund management fees owing to increased internal management of funds (LPFE staff).	(1,900)
<u>Securities Lending</u> – Reduction in income due to increasing regulatory constraints in European markets impacting the scale of lending activity.	250
<u>Employee Costs</u> – Increase in costs reflecting salary increments.	103
<u>Actuarial Fees</u> – Increase in costs due to triennial Actuarial Valuation as at 31 March 2017	40

Please note that Central Support Costs for services provided to the Fund by the City of Edinburgh Council are provisional estimates. The Fund is seeking to establish Service Level Agreements with the Council for specified services.

- 5.3 The indicative 2018/19 budget estimates a £621k increase in costs from that anticipated for 2017/19. Primarily, these relate to investment manager fees, reflecting increased market values, but also include the impact of salary increments and minor strengthening of pension administration staff resources.
- 5.4 **Uninvoiced Expenditure** – Provision has also been made for indicative costs of uninvoiced investment fees which are deducted from capital asset valuations.

Uninvoiced costs are forecasted to be in the region of £17.1million for both 2017/18 and 2018/19. The key changes from 2016/17 are summarised as follows:

	Increase/ (Decrease) £'000
<u>Investment Management Fees deducted from Capital</u> – An increase in such fees is expected owing to increased strategic exposure to infrastructure and private debt markets, offset by reducing private equity investments.	2,000
<u>Transactions costs</u> – Reduction in costs owing to re-aligning portfolios to internal management with inherent lower frequency trading	(100)

Please note that in this budget 2017/18 and 2018/19, intentionally, the Fund has not included investment performance fees. Performance fees are driven by fluctuations in market values and the timing of assets being sold which are very difficult to anticipate. This coupled by inconsistencies in the level accounting treatment by investment managers (some reporting performance on an accruals basis, others on a cash basis) make it extremely difficult to accurately forecast costs.

2015/16's accounts highlight the issues faced. The total value of uninvoiced costs was £26m, £12.1m of this in relation to performance fees. A majority of these performance fees were in relation to the Funds private equity investments which are now in the realisation stage of their life cycle. The value of performance element was also inflated by a change in accounting treatment by a manager to change performance being recognised on a cash basis to an accruals basis.

- 5.5 The 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.
- 5.6 There is no capital expenditure budgeted for 2017-2019. Please note that depending upon competitive tenders to be received, there may be capital expenditure in 2018/19 in relation to a new pension administration system. At this time, prior to the start of the tender, it is not considered appropriate to make specific anticipatory provision. Implications of the contract award will be reported to Committee in due course.

Risk, policy, compliance and governance impact

- 6.1 The budget contains contingencies to manage the key risks faced by the Pension Fund.

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.

Background reading/external references

Hugh Dunn

Acting Executive Director of Resources

Contact: John Burns, Pensions & Accounting Manager

E-mail: john.burns@edinburgh.gov.uk | Tel: 0131 469 3711

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 Budget 2017-2019

Appendix 1 Lothian Pension Fund Budget

The budget for 2017-18 and indicative figures for 2018-2019 are as follows:

	Projected 2016/17 £000	Budget 2016/17 £000	Movement £000	Budget 2017/18 £000	Movement £000	Indicative Budget 2018/19 £000
Employees	2,500	2,906	103	3,009	206	3,215
Property Costs	212	195	6	201	1	202
Plant and Transport	39	41	0	41	0	41
Supplies and Services	1,137	1,195	37	1,232	-12	1,220
Third Party Payments	875	1,375	17	1,392	-34	1,358
Investment Managers Fees	5,100	7,120	-1,920	5,200	450	5,650
Support Costs	300	300	-14	286	0	286
Capital Funding	88	87	-5	82	15	97
Gross Expenditure (Invoiced)	10,251	13,219	-1,776	11,443	626	12,069
Receipts	-166	-177	0	-177	-5	-182
Income - Other	-660	-800	250	-550	0	-550
Total Income	-826	-977	250	-727	-5	-732
Net Expenditure (Invoiced)	9,425	12,242	-1,526	10,716	621	11,337
Property Operational Costs	1,000	1,000	0	1,000	0	1,000
Investment fees deducted from Capital*	13,000	13,000	2,000	15,000	0	15,000
Transaction Costs	1,700	1,200	-100	1,100	0	1,100
Indicative Net Expenditure (Uninvoiced)	15,700	15,200	1,900	17,100	0	17,100
*Note 2016/17 figures have been adjusted to remove performance element						
Total Indicative Expenditure	25,125	27,442	374	27,816	621	28,437
Pension Administration	1,980	2,061	160	2,221	39	2,260
Investment Management	23,145	25,381	214	25,595	582	26,177
Investment Managers Fee Contingency	0	10,000	0	10,000	0	10,000

Lothian Pension Fund Budget continued

The budget for 2017-18 and indicative figures for 2018-2019 are as follows:

Capital Expenditure

	Projected 2016/17 £000	Budget 2016/17 £000	Movement £000	Budget 2017/18 £000	Movement £000	Indicative Budget 2018/19 £000
Loan Facility - LPFI	16	75	-75	0	0	0
LPFI Share Capital	50	36	-36	0	0	0
Total Capital Expenditure	66	111	-111	0	0	0