

Notice of meeting and agenda

Pensions Committee

2.00 pm Wednesday, 25th September, 2019

Dunedin Room - City Chambers

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

The law allows the Council to consider some issues in private. Any items under “Private Business” will not be published, although the decisions will be recorded in the minute.

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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 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 If any

4. Minutes

- 4.1 Minute of Pensions Committee of 26 June 2019 – submitted for approval as a correct record 5 - 10

5. Reports

- 5.1 Referrals and Recommendations from Pensions Audit Sub-Committee
- 5.2 Agenda Planning – Report by Executive Director of Resources 11 - 16
- 5.3 Audited Annual Report 2019 of the Lothian Pension Fund and Scottish Homes Pensions Fund Including Annual Report by External Auditor – Report by Executive Director of Resources 17 - 276
- 5.4 Lothian Pension Fund Contract Awards (Period 1 January to 30 June 2019) – Report by Executive Director of Resources 277 - 282

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| 5.5 | Overpayment of Pension – Report by Executive Director of Resources | 283 - 286 |
| 5.6 | Service Plan Update – Report by Executive Director of Resources | 287 - 296 |
| 5.7 | Risk Management Summary – Report by Executive Director of Resources | 297 - 314 |

6. Resolution to Consider in Private

- 6.1** The Committee is requested under Section 50(A)(4) of the Local Government (Scotland) Act 1973 to exclude the public from the meeting for the following items of business on the grounds that they would involve the disclosure of exempt information as defined in Paragraphs 6 and 9 of Part 1 of Schedule 7A of the Act.

7. Reports

| | | |
|------------|---------------------------------------------------------------------------------------------|-----------|
| 7.1 | LPFE Limited and LPFI Limited Annual Report – Report by Executive Director of Resources | 315 - 338 |
| 7.2 | Employer Covenant Review 2019 – Report by Executive Director of Resources | 339 - 350 |
| 7.3 | Employers Participating in Lothian Pension Fund – Report by Executive Director of Resources | 351 - 358 |
| 7.4 | Lothian Pension Fund ICT Update – Report by Executive Director of Resources | 359 - 364 |
| 7.5 | Governance Update – Report by Executive Director of Resources | 365 - 404 |
| 7.6 | Office Relocation – Report by Executive Director of Resources | 405 - 412 |

Andrew Kerr

Chief Executive

Committee Members

Councillor Alasdair Rankin (Convener), Councillor Steve Burgess, Councillor Maureen Child, Councillor Cameron Rose and Councillor Neil Ross; John Anzani and Richard Lamont.

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 twelve 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 Lesley Birrell, Committee Services, City of Edinburgh Council, Business Centre 2:1, Waverley Court, 4 East Market Street, Edinburgh EH8 8BG, Tel 0131 529 4240, email lesley.birrell@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/meetings .

Minutes

Pensions Committee

2.00pm, Wednesday 26 June 2019

Present

Councillors Rankin (Convener), Child, Miller, Rose and Neil Ross; John Anzani.

Pension Board Members

Jim Anderson, Sharon Cowle, Darren May, Tom Howorth, Brian Robertson and Alan Williamson.

Independent Professional Observer

Andy McKinnell

1. Minutes

Decision

To approve the minute of the Pensions Committee of 27 March 2019 as a correct record.

2. Referrals/Recommendations from Pensions Audit Sub-Committee

Councillor Rose advised the Committee of the discussion and decisions taken at the Pensions Audit Sub-Committee on 25 June 2019.

Decision

To note the updates and that Councillor Rose would raise any specific issues as each agenda item was considered.

(Reference – Pensions Audit Sub-Committee 25 June 2019)

3. Agenda Planning

Details were provided of proposed potential reports for future meetings of the Pensions Committee and Pensions Audit Sub-Committee including meetings in September and December 2019.

Decision

- 1) To note the agenda planning document.
- 2) To note that additional reports on Employer Covenant Review and Specific Contribution Strategy Review would be added to the September meeting schedule.

(Reference – report by the Executive Director of Resources, submitted)

4. Lothian Pension Fund Internal Audit Opinion and Annual Report for the Year Ended 31 March 2019

The Internal Audit annual opinion for Lothian Pension Fund (LPF) for the year ended 31 March 2019 was presented. The opinion was based on the outcomes of four audits included in the LPF 2018/19 Internal Audit annual plan and the status of open and overdue Internal Audit findings as at 31 March 2019.

Members noted that the opinion had changed from “red” to “amber” this year based on the outcomes of the audits undertaken. It was noted that the key driver for this change was the significant progress made since March 2019 on the overdue internal audit findings.

A follow up process on outstanding actions had been implemented and was now firmly established together with a quality assurance framework which would be applied from the financial year 2019/20.

Decision

To note the internal audit opinion for the year ended 31 March 2019.

(Reference – report by the Chief Internal Auditor, submitted)

5. Lothian Pension Fund Unaudited Annual Report (and Financial Statements) 2019

The unaudited Annual Report and Financial Statements for the year ended 31 March 2019 for the Lothian Pension Fund was submitted.

Councillor Rose advised that members of the Pensions Audit Sub-Committee had received a presentation on the detail of the Annual Report and Financial Statements. Key areas highlighted were:

- Merger of Lothian Buses into the Lothian Pension Fund
- Effect on Fund Account
- Effect on Net Asset Statement
- Membership figures
- Scottish Homes Pension Fund Financial Statements
- Contributions from Scottish Government

Guidance was awaited from CIPFA on the standardised reporting of investment cost transparency and members discussed the work being carried out in England around PSLA new templates relating to cost transparency initiative.

Lothian Pension Fund currently provided disclosures additional to those required in the CIPFA guidance and Audit Scotland had indicated they were supportive of this.

In summary, the Chief Finance Officer reported that LPFE and LPFI company accounts were consolidated for presentation to Scott Moncrieff as external auditors.

Decision

- 1) To note the unaudited Annual Report (and Financial Statements) for the year ended 31 March 2019 for Lothian Pension Fund and Scottish Homes Pension Fund.
- 2) To refer the report to the City of Edinburgh Council meeting on 27 June 2019 for noting.

(Reference – report by the Executive Director of Resources, submitted)

6. Joint Investment Strategy Panel Activity

An update was provided on the activity of the Joint Investment Strategy Panel for the year to 31 March 2019.

The primary focus for the Panel during 2018/19 has been implementation of the existing investment strategies for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund, previously agreed by Committee as well as a new investment strategy review for Lothian Pension Fund in collaboration with the Falkirk and Fife Funds.

Decision

To note the activities of the Joint Investment Strategy Panel during the financial year 2018/19.

(References – Pensions Committee 26 March 2018 (item 7); report by the Executive Director of Resources, submitted)

7. Annual Investment Update – Lothian Pension Fund

Information was provided on the investments and funding position of the Lothian Pension Fund to 31 March 2019.

Over the twelve months to 31 March 2019, investment market returns were generally strong. Global equities returned 10.5% to sterling-based investors while index-linked gilts, a good proxy for Fund liabilities, rose by 5.7% over the year. The UK property market also provided a positive return of 5.6%, largely rental income rather than capital growth.

Decision

To note the asset allocation, investment performance and funding update of the Lothian Pension Fund.

(Reference – report by the Executive Director of Resources, submitted)

8. Annual Investment Update – Scottish Homes Pension Fund

An update was provided for the year to 31 March 2019 on the strategic allocation and invested assets of the Scottish Homes Pension Fund.

At end March 2019, the funding level was estimated to be 105.4%. The Fund's assets had increased in value by 4.6% adjusted for cash flow movements to pay pensions while a proxy of the value of liabilities had increased by 4.4%.

Over 2018/19, £6.6m was sold to pay pensions which compared with the Fund value of £163m at the end of March 2019.

Decision

To note the report.

(Reference – report by the Executive Director of Resources, submitted.)

9. Pension Administration Strategy (Revised)

A revised version of the Lothian Pensions Funds' Pensions Administration Strategy had been presented to Committee in March 2019, prior to consultation with Fund employers.

A further amendment was proposed relating to the introduction of the i-Connect portal. As required under the Local Government Pension Scheme (Scotland) Regulations, a consultation exercise would be carried out with the Fund's employers.

Decision

- 1) To note that the Fund intended to consult with employers on the revised Pensions Administration Strategy.
- 2) To approve the draft revised Pensions Administration Strategy, subject to any further amendment arising from the forthcoming employer consultation being reported to the Committee at its next meeting.

(References – Pensions Committee 27 March 2019 (item 6); report by the Executive Director of Resources, submitted)

10. Risk Management Summary

The quarterly risk overview as at 15 May 2019 was presented. Members discussed risk changes and noted that most had improved or were progressing towards improvement.

Councillor Rose advised that there had been considerable discussion around the risk overview by members of the Pensions Audit Sub-Committee.

Decision

- 1) To note the update on the quarterly risk overview.
- 2) To request that a 3-year graphic to set context be included and that cyber security risk be listed separately in future reporting.

(References – Pensions Audit Sub-Committee 25 June 2019 (item 5); report by the Executive Director of Resources, submitted)

11. Governance Update

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the following items of business on the grounds that they involved the disclosure of exempt information as defined in paragraphs 6 and 9 of Schedule 7(A) of the Act.

An update was provided on progress being made towards implementing the recommendations of the Lothian Pension Fund Governance Review 2019.

Decision

- 1) To note the update on implementing the proposals set out in the LPF Governance Review 2019.
- 2) To note the reappointment of John Anzani, (member representative) and Richard Lamont (employer representative) as members of the Committee.

(Reference – report by the Executive Director of Resources, submitted)

12. Lothian Pension Fund ICT Update

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the following items of business on the grounds that they involved the disclosure of exempt information as defined in paragraphs 6 and 9 of Schedule 7(A) of the Act.

An update was provided on Lothian Pension Fund's digital strategy and ICT pathway.

Decision

Detailed in the confidential schedule, signed by the Convener, with reference to this minute.

(References – Pensions Audit Sub-Committee 25 June 2019 (item 6); report by the Executive Director of Resources, submitted)

13. Regulatory Update – The Pensions Regulator Audit

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the following items of business on the grounds that they involved the disclosure of exempt information as defined in paragraphs 6 and 9 of Schedule 7(A) of the Act.

Information was provided on the findings of the Pension Regulator Audit which had been carried out during the preceding six months.

Decision

To note the Pension Regulator Cohort Review feedback on the Lothian Pension Fund.

(References – Pensions Audit Sub-Committee 25 June 2019 (item 7); report by the Executive Director of Resources, submitted)

14. Investment Controls and Compliance

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the following item of business on the grounds that it involved the disclosure of exempt information as defined in Paragraphs 6 and 9 of Schedule 7(A) of the Act.

A summary was provided of key matters in relation to the Lothian Pension Fund Group's systems and controls around the development of the in-house investment operations of the Lothian Pension Fund.

Decision

To note the update.

(References – Pensions Audit Sub-Committee 25 June 2019 (item 8); report by the Executive Director of Resources, submitted)

15. Investment Strategy Implementation Update – Joint Investment Strategy Panel

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the following item of business on the grounds that it involved the disclosure of exempt information as defined in Paragraphs 6 and 9 of Schedule 7(A) of the Act.

An update was provided on Lothian Pension Fund investment strategy implementation issues.

Decision

Detailed in the confidential schedule, signed by the Convener, with reference to this minute.

(Reference – report by the Executive Director of Resources, submitted)

Pensions Committee

2.00pm, Wednesday, 25 September 2019

Agenda Planning

| | |
|---------------------|-----|
| Item number | 5.2 |
| Executive/routine | |
| Wards | All |
| Council Commitments | |

1. Recommendations

The Pensions Committee is requested to:

- 1.1 note the agenda planning document; and
- 1.2 note that the Pension Board are invited to comment on agenda items during Committee meetings.

Stephen S. Moir

Executive Director of Resources

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Agenda Planning

2. Executive Summary

- 2.1 This report and the scheme of committee document (appendix 1 of this report) provides the Committee with an overview of the proposed agendas for future meetings of the Pensions Committee and Pensions Audit Sub Committee. It also provides a more general overview of the current cycle of papers for those committees.
- 2.2 There will, of course, be specific matters and papers which need to be brought to attention of the committees in addition to those set out herein.

3. Background

- 3.1 In order for the Committee and Pension Board to gain an overview of the content of future meetings, it was agreed that an agenda planning document be submitted each quarter.
- 3.2 Committee meetings are held on a quarterly basis and the Audit Sub Committee meetings are generally held three times a year.

4. Main report

- 4.1 The proposed agendas for the next two meetings are therefore set out below, based on the usual Committee cycle plus any additional and intra-cycle requests.
- 4.2 The Statement of Investment Principles paper, scheduled for June 2019, was postponed allowing for the outcome of the Joint Investment Strategy Panel meeting in June to be included. The Principles will be reviewed and revised and presented to the Pensions Committee at the December meeting of the Pension Committee.
- 4.3 In addition, three reports have been added to the scheme of committee schedule (appendix 1) these are:

- the Lothian Pension Fund Contract Awards update presented to the Pensions Committee by Procurement Services in March and September each year.
- the employer covenant review presented to the Pensions Committee annually in September each year.
- the Contribution Stability Mechanism Review (previously referred to as Funding update and preparation for the Actuarial Valuation) presented to the Pensions Committee 'as required'.

December 2019

| Pensions Committee | Audit Sub Committee |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> • Referrals / recommendations from Pensions Audit-Sub Committee • Benchmarking • Contribution Stability Mechanism Review 2019 • The Statement of Investment Principles • Stewardship and Engagement • Service Plan Update • Risk management summary • Governance Update | <ul style="list-style-type: none"> • EU Tax Claims & Income Recovery • Investment Income Review-Cross-Border withholding tax • Investment Controls & Compliance • Global Custody Services Performance • Risk Management in-depth review |

March 2020

| Pensions Committee |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> • Referrals / recommendations from Pensions Audit-Sub Committee • Audit plans and reports (internal and external) * • Policies and Strategies Update • Governance Update • Actuarial Valuation: Lothian Pension Fund/Scottish Homes Pension • Employers Participating in Lothian Pension Fund • Service Plan Update and Budget for 2020/21 • Risk management summary <p data-bbox="150 1630 1414 1693">*Draft audits and plan will be developed in consultation with the Convenor of the Audit Sub Committee and the Independent Professional Observer.</p> |

Future Pensions Committee and Audit Sub Committee dates:

| Pensions Committee | Pensions Audit Sub Committee |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none">• Wednesday, 11 December 2019, 2.00pm, Dunedin Room, City Chambers.• Wednesday, 25 March 2020, 2.00pm, Dunedin Room, City Chambers.• Wednesday, 24 June 2020, 2.00pm, Dunedin Room, City Chambers. | <ul style="list-style-type: none">• Tuesday, 10 December 2019, 2.00pm, Dunedin Room, City Chambers.• Tuesday, 23 June 2020, 2.00pm, Dunedin Room, City Chambers. |

5. Next Steps

5.1 None.

6. Financial impact

6.1 None.

7. Stakeholder/Community Impact

- 7.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the pension funds and they are invited to comment on the relevant matters at Committee meetings.
- 7.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report. The forward planning of the Committees' agendas should facilitate improved risk management and governance for the pension funds.
- 7.3 There are no adverse sustainability impacts arising from this report.

8. Background reading/external references

8.1 None.

9. Appendices

Appendix 1 – Scheme of Committee Papers

| 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 |
| | Policies and Strategies Update (including revised Pension Administration Strategy biennial from March 2016) | N/A | March |
| | Service Plan (every 2 years) | N/A | March |
| | Budget | N/A | March |
| | Governance Update (including Pension Audit Sub-Committee appointments) | N/A | March |
| | LPF Annual Report and Accounts (Unaudited) | LPF Annual Report & Accounts (Unaudited) | June |
| | Statement of Investment Principles | N/A | June |
| | Joint Investment Strategy Panel Activity | N/A | June |
| | Annual Investment Updates - Lothian Pension Fund and Scottish Homes Pension Fund | N/A | June |
| | Employer Covenant Review | N/A | September |
| | LPFE Limited and LPFI Limited Annual Reports | LPFE Limited and LPFI Limited Annual Reports | September |
| | Audited Annual Report and Accounts of the Lothian Pension Fund and Scottish Homes Pension Fund, including the Annual Report by External Auditor. | Audited Annual Report and Accounts of the Lothian Pension Fund and Scottish Homes Pension Fund, including the Annual Report by External Auditor. | September |
| | N/A | Pensions Data Quality | September |
| | N/A | Irrecoverable overpayment of pensions – decisions made under delegated authority | September |
| | N/A | Fraud Prevention | September |
| | Annual Report by External Auditor | Annual Report by External Auditor | December (or September if available) |
| | Benchmarking | N/A | December |
| | N/A | EU Tax Claims and Other Income Tax Recoveries | December |
| | N/A | Investment Income Review-Cross-Border Withholding Tax | December |
| | Stewardship and Engagement | N/A | December |
| N/A | Investment Controls and Compliance | December | |
| N/A | Global Custody Services Performance | December | |
| | Risk Management: In-depth review | December | |

| Frequency | Pensions Committee | Audit Sub Committee | Month |
|------------------|-------------------------------------------------------------|--------------------------------------------------------------------------|-------------------------------------|
| Semi Annually | Employers Participating in Lothian Pension Fund | N/A | March & September |
| | Lothian Pension Fund Contract Awards Report | 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 SHPF Funding Strategy Statement | | December or March |
| As required | Delegated authorities (provider appointments) | N/A | |
| | Discretions (death grants etc.) | N/A | |
| | N/A | Internal Audit Reports | |
| | Regulatory Update | N/A | |
| | Investment Strategy Reviews (at least every 3 years) | N/A | |
| | N/A | Particular items of risk management for greater scrutiny (as requested). | |
| | Contribution Stability Mechanism Review | N/A | |

Pensions Committee

2.00pm, Wednesday, 25 September 2019

Audited Annual Report 2019 of the Lothian Pension Fund and Scottish Homes Pension Fund, including Annual Report by External Auditor

| | |
|----------------------------|------------|
| Item number | 5.3 |
| Executive/routine | |
| Wards | All |
| Council Commitments | |

1. Recommendations

The Pensions 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 report by Scott-Moncrieff “Lothian Pension Funds 2018/19 Annual Audit Report to Members and the Controller of Audit” (at Appendix 1);
- 1.3 note the audited Annual Report for the year ended 31 March 2019 for the Lothian Pension Fund and the Scottish Homes Pension Fund (at Appendix 2); and
- 1.4 note that the audited financial statements, for the year ended 31 March 2019, of both the wholly-owned companies, LPFE Limited and LPFI Limited, were approved by the respective Board of Directors in May 2019. These statements are shown in full at Appendices 3 and 4.

Stephen S. Moir

Executive Director of Resources

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Audited Annual Report 2019 of the Lothian Pension Fund and Scottish Homes Pension Fund, including Annual Report by External Auditor

2. Executive Summary

- 2.1 The unaudited Annual Report for the year ended 31 March 2019 for the Lothian Pension Fund and Scottish Homes Pension Fund has now been considered by the external auditor, Scott-Moncrieff.
- 2.2 International Standard on Auditing (ISA) 260 requires the external auditor to communicate its findings to those charged with governance of the Funds. Accordingly, the Scott-Moncrieff “Lothian Pension Funds 2018/19 Annual Audit Report to Members and the Controller of Audit” is included at Appendix 1.
- 2.3 Scott-Moncrieff has provided “an unqualified opinion on the financial statements and other prescribed matters for Lothian Pension Fund and Scottish Homes Pension Fund within our independent auditor’s report” and has also stated “that there were no matters which we were required to report by exception”.

3. Background

ISA 260 annual report by External Auditor

- 3.1 Under statutory accounting guidance issued by the Scottish Government, Administering Authorities are required to issue a separate Annual Report covering the Local Government Pension Scheme (LGPS) funds that they are responsible for. These Annual Reports are subject to a separate external audit.
- 3.2 International Standard on Auditing (UK and Ireland) 260 (ISA 260) requires the External Auditor to communicate its findings to those charged with governance of the Funds. This summarises any matters arising from the audit of the financial statements prior to the formal signing of the independent auditor’s report.
- 3.3 As part of the standard, the External Auditor is required to provide its view of the following:
 - 3.3.1 Any significant qualitative aspects within the Funds’ accounting practice;
 - 3.3.2 Any significant difficulties encountered during the audit;
 - 3.3.3 Any material weakness in the design, implementation or operating effectiveness of the system of internal control;

- 3.3.4 Any significant matters arising from the audit discussed with management;
 - 3.3.5 Any representations that have been requested from management; and
 - 3.3.6 Any other matter that is significant.
- 3.4 City of Edinburgh Council noted the Unaudited Annual Report 2019 for the Lothian Pension Fund and Scottish Homes Pension Fund at its meeting on 28 June 2019.

4. Main report

Scott-Moncrieff - Lothian Pension Fund and Scottish Homes Pension Fund 2018/19 Annual Audit report to Members and the Controller of Audit

- 4.1 The report by the external auditor on the financial statements is included at Appendix 1 – “Scott-Moncrieff - Lothian Pension Funds 2018/19 Annual Audit Report to Members and the Controller of Audit. This will be presented to Committee by Nick Bennett, Partner, Scott-Moncrieff.
- 4.2 Scott-Moncrieff has stated that its “work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK and Ireland) and Ethical Standards”.
- 4.3 Scott-Moncrieff has provided “an unqualified opinion on the financial statements and other prescribed matters for Lothian Pension Fund and Scottish Homes Pension Fund (collectively referred to as “the Funds”) within our independent auditor’s report” and has also stated “that there were no matters which we were required to report by exception”.
- 4.4 The external auditor has commented that “We are pleased to report that our audit identified no material adjustments. In addition, we can confirm that there were no unadjusted errors relating to the 2018/19 financial statements. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual report and financial statements. The most significant disclosure change related to the present value of promised retirement benefits.”
- 4.5 After the Supreme Court denied the Government leave to appeal the McCloud and other associated cases on 27 June 2019, a written ministerial statement confirmed that as ‘transitional protection’ had been offered to members of all the main public service pension schemes, the difference in treatment would need to be remedied across all those schemes, including the Local Government Pension Scheme (LGPS). As the remedy will involve ‘levelling up’ member benefits, any future agreed outcome will serve to increase the cost of LGPS pensions.
- 4.6 Prior to the Supreme Court’s determination, a contingent liability had been disclosed by Lothian Pension Fund in its unaudited financial statements 2018/19 (note 32).
- 4.7 The actuary has now carried out an assessment of the impact of the McCloud judgement on the Lothian Pension Fund. The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting

Standard 19 (IAS19) assumptions, is now estimated to be £9,435m, an increase of £102m. This is disclosed at Note 23 of the Financial Statements.

- 4.8 A revised IAS19 statement for LPFE Limited to incorporate the potential implications of the McCloud judgement was also sought. The actuary has estimated an increase of £255k to LPFE's defined benefit obligation. Whilst this has been declared by supplementary note, the group financial accounts have not been adjusted so as to remain consistent with LPFE Limited's audited financial statements.
- 4.9 For the Scottish Homes Pension Fund, the actuary has stated that the McCloud judgement has no impact because this Fund has no active employees.
- 4.10 Appendix 1 ("Appendix 1: Management action plan", Pages 40 to 46 of that report) "details the control weaknesses and opportunities for improvement that we (Scott-Moncrieff) have identified during our audit". Planned management actions by Lothian Pension Fund staff in relation to the points raised by the external auditor are also stated.
- 4.11 In addition to members of the Pensions Committee and Pensions Audit Sub-Committee, Scott-Moncrieff has also sent the report to the Controller of Audit and has advised that it will be published on the Audit Scotland web-site in due course.

Audited Annual Report 2019 for Lothian Pension Fund and Scottish Homes Pension Fund

- 4.12 With the completion of the work by Scott-Moncrieff, the Audited Annual Report 2019 for the Lothian Pension Fund and Scottish Homes Pension Fund has been finalised and is included at Appendix 2.
- 4.13 As part of the completion of the audit, the auditor seeks written assurances from the Chief Finance Officer, Lothian Pension Fund, on aspects of the financial statements and judgements and estimates made. A draft letter of representation under ISA580 is attached at Appendix 5.

Audited Financial Statements for the year ended 31 March 2019; LPFE Limited and LPFI Limited

- 4.14 The consolidated financial statements (within the Annual Report 2019) combine those of the Fund (the parent entity) and its controlled entities (the investment staffing company, LPFE Limited, and the investment services company, LPFI Limited), as defined in International Accounting Standard (IAS) 27. As reported to Pensions Committee in June 2019, the financial statements of both companies have been audited by Scott-Moncrieff and were approved by the respective Boards of Directors in May 2019. In the interests of governance transparency, these statements are shown in full at Appendices 3 and 4.
- 4.15 LPFE Limited is the employment vehicle for the Fund's staff. It provides staffing services to the City of Edinburgh Council, LPFI Limited and to Falkirk Council. The company's financial objective is "to make a modest trading surplus before adjustments required under International Financial Reporting Standards (IFRS)". Such adjustments primarily relate to pension costs, as required by International Accounting Standard (IAS) 19, and the related deferred tax. For the year ended 31

March 2019, the underlying trading profit of the company was £88,926 (2018: £41,052).

- 4.16 LPFI Limited provides Financial Conduct Authority (FCA) regulated investment services, both to Lothian Pension Fund and other pension funds, but does not employ any staff directly. Its financial objective is “to make a modest trading surplus”. For the year ended 31 March 2019, the underlying trading profit of the company was £59,396 (2018: £34,619).
- 4.17 A separate report on the two companies on this agenda provides a more detailed progress update.

5. Next Steps

- 5.1 Reflecting Audit Scotland guidance, the Annual Report should be referred to full Council. It is anticipated that City of Edinburgh Council should note the audited Annual Report 2019 at its meeting on 24 October 2019.

6. Financial impact

- 6.1 There are no direct financial implications arising from this report.

7. Stakeholder/Community Impact

- 7.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the pension funds and they are invited to comment on the relevant matters at Committee meetings.
- 7.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report. The forward planning of the Committees’ agendas should facilitate improved risk management and governance for the pension funds.
- 7.3 There are no adverse sustainability impacts arising from this report.

8. Background reading/external references

- 8.1 None.

9. Appendices

Appendix 1 – Scott-Moncrieff - Lothian Pension Fund and Scottish Homes Pension Fund 2018/19 Annual Audit Report to Members and the Controller of Audit, in accordance with International Standard on Auditing (UK and Ireland) 260 (ISA 260);

Appendix 2 - Audited Annual Report 2019 for the Lothian Pension Fund and Scottish Homes Pension Fund;

Appendix 3 - LPFE Limited – Financial Statements (Audited) for the year ended 31 March 2019;

Appendix 4 – LPFI Limited – Financial Statements (Audited) for the year ended 31 March 2019;

Appendix 5 – Letter of Representation (ISA 580) by Chief Finance Officer, Lothian Pension Fund

Lothian Pension Fund and Scottish Homes Pension Fund

2018/19 Annual Audit Report to
Members and the Controller of
Audit

August 2019

Appendix 1





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1. Key messages



Annual accounts audit

Lothian Pension Funds will approve the annual report and financial statements for 2018/19 on 25 September 2019. We intend to report unqualified opinions on the financial statements and other prescribed matters for Lothian Pension Fund and Scottish Homes Pension Fund (collectively referred to as the “Funds”) within our independent auditor’s report. We also intend to report that there were no matters which we were required to report by exception.

The annual report and financial statements and supporting schedules were of a high standard. Our thanks go to staff for their assistance with our work.

Wider scope audit

Financial sustainability

The Funds have effective arrangements in place to ensure the ongoing sustainability of the pension funds.

The focus of their investment strategy is to ensure a sufficient return over the long term to meet the funding objectives outlined by the Funding Strategy Statement. Performance over 5 years shows they are managing investment above benchmark.

There is an ongoing risk that the pension scheme is not affordable for admitted bodies and Lothian Pension Fund has reported an increase in the number of bodies leaving the Fund and an increase in the cessation liability following the 2017 triennial valuation.

Financial management

The Funds have effective arrangements in place for financial management and the use of resources

Lothian Pension Fund’s investment performance increased in 2018/19 and was above the short term benchmark and national average.

The net assets of Lothian Pension fund have risen in 2018/19 and Scottish Homes Pension Fund assets have not moved. The promised retirement benefits have increased across all three funds.

Governance and transparency

Governance arrangements at the Funds are deemed to be appropriate.

Our assessment has been informed by a review of the corporate governance arrangements in place, the information provided to the Board and Committees as well as the risk management arrangements in place.

We identified a significant risk regarding the transfer of assets from Lothian Buses Pension Fund to Lothian Pension Fund. We have confirmed appropriate governance processes were in place during 2018/19 to ensure the transfer was in line with relevant regulations.

Value for money

The Funds have appropriate arrangements in place to secure value for money through appropriate monitoring of performance of investments and the administration of the Funds.

The Funds’ investment performance is subject to regular review by the Pension Committee.

Conclusion

This report concludes our audit for 2018/19. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK) and Ethical Standards.

Scott-Moncrieff
August 2019



2. Introduction

This report is presented to those charged with governance and the Controller of Audit and concludes our audit of the Lothian Pension Funds for 2018/19.

We carry out our audit in accordance with Audit Scotland's Code of Audit Practice (May 2016). This report also fulfils the requirements of International Standards on Auditing (UK) 260: Communication with those charged with governance.

We have designated the Pensions Committee as "those charged with governance" for the purposes of audit communication.



Introduction

1. This report summarises the findings from our 2018/19 audit of Lothian Pension Funds (the Funds).
2. We outlined the scope of our audit in our External Audit Plan, which we presented to the Pensions Committee at the outset of our audit. The core elements of our work include:
 - an audit of the 2018/19 annual report and accounts and related matters;
 - a review of the Funds' arrangements for governance and transparency, financial management, financial sustainability and value for money; and
 - any other work requested by Audit Scotland.

Exhibit 1: Audit dimensions within the Code of Audit Practice



3. The Funds are responsible for preparing an annual report and accounts which show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the annual report and accounts or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.
4. The report contains an action plan with specific recommendations, responsible officers and dates for implementation. Senior management should assess these recommendations and consider their wider implications before deciding on appropriate actions. We give each recommendation a grading to help the Funds assess their significance and prioritise the actions required.
5. We discussed and agreed the content of this report with the Chief Finance Officer. We would like to thank all management and staff for their co-operation and assistance during our audit.

Confirmation of independence

6. International Standards on Auditing in the UK (ISAs (UK)) require us to communicate on a timely basis all facts and matters that may have a bearing on our independence.
7. We confirm that we have complied with the Financial Reporting Council's (FRC) Revised Ethical Standard (June 2016). In our professional judgement, the audit process is independent and our objectivity has not been compromised in any way.
8. We set out in Appendix 1 our assessment and confirmation of independence.



Adding value through the audit

9. All of our clients demand of us a positive contribution to meeting their ever-changing business needs. Our aim is to add value to the Funds through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way we aim to help the Funds promote improved standard of governance, better management and decision making and more effective use of resources.

Feedback

10. Any comments you may have on the service we provide, the quality of our work and our reports would be greatly appreciated at any time. Comments can be reported directly to the audit team or through our online survey:
www.surveymonkey.co.uk/r/S2SPZBX
11. While this report is addressed to the Funds and the Controller of Audit, it will be published on Audit Scotland's website www.audit-scotland.gov.uk

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3. Annual report and accounts

The Funds' annual report and accounts are the principal means of accounting for the stewardship of their resources and performance in the use of those resources.

In this section we summarise the findings from our audit of the 2018/19 annual report and accounts.



Annual report and accounts

An unqualified audit opinion on the annual report and accounts

The annual report and accounts for the year ended 31 March 2019 are due to be approved by the Pensions Committee on 25 September 2019. We intend to report unqualified opinions within our independent auditor's report. We did not identify any significant adjustments to the unaudited annual report and accounts.

The Funds' had good administrative processes in place to prepare the annual report and financial statements and the required supporting working papers.

Overall conclusion

An unqualified audit opinion on the annual report and accounts

12. The annual report and accounts for the year ended 31 March 2019 are due to be considered by the Pensions Committee on 25 September 2019. We intend to report within our independent auditor's report:
 - an unqualified opinion on the financial statements; and
 - an unqualified opinion on other prescribed matters.
13. We are also satisfied that there are no matters which we are required to report by exception.

Good administrative processes were in place

14. We received unaudited annual report and accounts and supporting papers of a good standard, in line with our audit timetable. Our thanks go to staff at the Funds for their assistance with our work.

Our assessment of risks of material misstatement

15. The assessed risks of material misstatement described in Exhibit 2 are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the audit team. Our audit procedures relating to these matters were designed in the context of our audit of the annual report and accounts as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the annual report and accounts is not modified with respect to any of the risks described in Exhibit 2.



Exhibit 2 – Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

1. Management override

In any organisation there exists a risk that management has the ability to process transactions or make adjustments to the financial records outside the normal financial control processes. Such issues could lead to a material misstatement in the financial statements. This is treated as a presumed risk area in accordance with ISA (UK) 240 – *The auditor's responsibilities relating to fraud in an audit of financial statements*.

Excerpt from the 2018/19 External Audit Plan

16. We have not identified any indication of management override in the year. We have reviewed the Funds' accounting records and obtained evidence to ensure that transactions outside normal processes were valid and accounted for correctly. We have also reviewed management estimates and the journal entries processed in the period and around the year end. We did not identify any areas of bias in key judgements made by management and judgements were consistent with prior years.
17. While we have not identified any instances of management override from our testing we noted in 2017/18 that City of Edinburgh Council staff, with access to Oracle, have the ability to post journals to the Funds' financial ledger. This is an ongoing issue in 2018/19, however, we did not identify any instances where journals were posted by inappropriate users.

2. Revenue recognition

Under ISA (UK) 240– *The auditors responsibilities relating to fraud in an audit of financial statements* there is a presumed risk of fraud in relation to revenue recognition. The presumption is that the Funds could adopt accounting policies or recognise revenue transactions in such a way as to lead to material misstatement in the reported financial position.

Excerpt from the 2018/19 External Audit Plan

18. While we did not suspect incidences of material fraud and error, we evaluated each type of revenue transaction and documented our conclusions. We have reviewed the controls in place over revenue accounting and found them to be sufficient.
19. We have evaluated key revenue transactions and streams to gain assurance over the completeness and occurrence of income. We are satisfied income is fairly stated in the financial statements. We also carried out testing to confirm that the Funds' revenue recognition policies are appropriate and have been applied consistently throughout the year.



3. Risk of fraud in the recognition of expenditure

In 2016, the Public Audit Forum issued Practice Note 10 “The Audit of Public Sector Financial Statements” which applies to the audit of public sector financial statements for periods commencing after June 2016. This Practice Note recognises that most public sector bodies are net spending bodies and notes that there is an increased risk of material misstatement due to improper recognition of expenditure

Excerpt from the 2018/19 External Audit Plan

20. At the planning stage of our audit cycle, we reported that we did not believe the risk of fraud in expenditure recognition was material to the financial statements and we therefore rebutted this risk. This position has been reviewed throughout this audit and this conclusion has remained appropriate.
21. We conducted our testing based on our approach to low inherent risk areas and we evaluated each type of expenditure transaction and documented our conclusions. We gained reasonable assurance over the completeness and occurrence of expenditure and are satisfied that expenditure is fairly stated in the annual accounts. To inform our conclusion we carried out testing to confirm that the Funds’ policy for recognising expenditure is appropriate and has been applied consistently throughout the year.

4. Valuation of investments

The Funds held investments of £6.628 billion as at 31 March 2018, of which 33% (£2.184 billion) were classified as level 2 or level 3 financial instruments, meaning the valuation was not based on unadjusted quoted prices in active markets. Judgements are taken by the Investment Managers to value those investments whose prices are not publically available. Investments of this nature are complex, difficult to value and include a significant degree of judgement from the investment manager. The material nature of this balance means that any error in judgement could result in a material valuation error.

Excerpt from the 2018/19 External Audit Plan

22. In 2018/19, the value of level 2 and 3 investments rose by 13% to £2.639 billion (2017/18: £2.321 billion) increasing as a proportion of overall investments to 36% (34.7% in 2017/18). Fair values of investments of this nature are provided by fund managers and custodian using various bases selected by the investment manager or custodian. The base of investment values can include reference to similar companies or bid prices.
23. We have considered the valuation basis for a sample of investments and concluded that an appropriate base has been applied in each case. The custodian and investment managers are deemed to be management experts. In line with ISA (UK) 500 we have considered the competence, capability and objectivity of the experts used to inform the valuation. In addition we have reviewed auditor reports on the internal controls at the custodian and at each key investment manager. Our testing did not raise any issues regarding the qualifications of or work provided by the management experts employed by the Funds.
24. For a sample of hard to value investments we reviewed the assumptions and bases of the fair value. We challenged the Funds on the rationale for selecting the bases and assumptions and ensured we were satisfied they were appropriate.
25. The disclosures within the annual report and financial statements are consistent with the information provided by the custodian.



5. Lothian Buses Pension Fund Merger

In 2018/19 the assets and liabilities of Lothian Buses Pension Fund will be merged with Lothian Pension Fund. There is limited precedent for mergers of local government pension schemes and therefore, there is an increased risk of material misstatement due to the material and unusual nature of the transaction. There is a risk that the transfer of assets and liabilities from Lothian Buses Pension Fund is not accounted for in accordance with applicable accounting standards and/or statutory requirements.

Excerpt from the 2018/19 External Audit Plan

26. Lothian Buses Pension Fund was set up by way of a minute of agreement between Lothian Regional Council and Lothian Region Transport PLC dated 31 March 1987 (the Admission agreement). This agreement outlines that the Authority (Council) wishes to establish a 'further fund' in terms of regulation 3 of the Local Government Superannuation (Funds) (Scotland) Regulations 1986 in addition to the existing fund (i.e. Lothian Pension Fund).
27. Historically, Lothian Pension Fund has elected to present Lothian Pension Fund and Lothian Buses Pension Fund separately in the annual accounts. Following the decision to manage the Lothian Buses Pension Fund as part of the main Lothian Pension Fund in year, it was considered that the accounting policy of reporting the Funds separately in the accounts was no longer appropriate.
28. The accounting policy of reporting Lothian Buses Pension Fund as a separate fund was therefore changed in 2018/19. From 2018/19 Lothian Buses Pension Fund was included in the Lothian Pension Fund accounts. As this is a change in accounting policy, there is a requirement to retrospectively restate the 2017/18 figures in line with accounting standards. Consequently Lothian Pension Fund adjusted the prior year figures for comparative purposes.
29. We have considered the basis for the change in accounting policy and concluded that the judgements made by the Funds' management were appropriate. In addition we have reviewed the restated figures and confirmed that they are appropriate and accurately reflect the transactions which took place in 2017/18.



6. Governance statement

In 2017/18 Internal Audit provided a red¹ rated audit opinion meaning significant enhancements were required to the Funds' control environment.

The Funds' internal audit service is provided through the administering authority, City of Edinburgh Council. The 2018/19 internal audit plan was presented to the Pensions Committee and Pensions Audit Sub-Committee in March 2018. Within the plan, a total of 3 reviews were scheduled to take place during 2018/19 totalling 60 days.

All of the 2018/19 internal audit work is scheduled to take place between January and March 2019. Internal audit is a key source of assurance for the governance statement and there is pressure to ensure appropriate assurance is achieved prior to the year-end.

Excerpt from the 2018/19 External Audit Plan

30. The internal audit opinion was presented to the June Pensions Committee and provided an amber rating². This opinion was based on the findings from three reports in year and the follow up of prior year recommendations.
31. All internal audit reports issued within 2018/19 gave adequate assurance over the control environment. The amber rating related to overdue 'high risk' items from 2017/18 audit work.
32. The issues in 2017/18 related to IT Business Resilience and disaster recovery, pensions tax and third party suppliers. Internal audit confirmed that three of four high risk items had been appropriately addressed by June 2019. The outstanding item relates to the methodology used by Aquila Heywood in the calculation of pension tax. The Funds are currently engaged with Aquila Heywood to update the methodology.
33. The City of Edinburgh Council has considered the internal audit findings and its Chief Executive and Head of Finance are satisfied that reasonable assurance can be placed upon the adequacy and effectiveness of Funds' systems of internal control.
34. We noted that in the draft accounts the Governance Statement still refers to a red rating which is out of line with the findings of internal audit. We have requested this be updated in the revised accounts.

Our application of materiality

35. The assessment of what is material is a matter of professional judgement and involves considering both the amount and the nature of the misstatement. This means that different materiality levels will be applied to different elements of the financial statements.
36. Our initial assessment of materiality for the financial statements is set out in the table below. On receipt of the 2018/19 draft financial statements, we reassessed materiality as outlined in the table

below. We consider that our updated assessment has remained appropriate throughout our audit.

¹ Significant enhancements to the control environment required

² Generally acceptable but with enhancements required



| | Lothian Pension Fund ³ Group ⁴ materiality £million | Lothian Pension Fund ¹ Parent materiality £million | Scottish Homes materiality £million |
|--------------------------------|---------------------------------------------------------------------------|---------------------------------------------------------------|-------------------------------------|
| Overall-planning | 108 | 108 | 2.5 |
| Overall-final | 117 | 117 | 2.5 |
| Dealings with members-planning | 11.3 | 11.3 | 0.4 |
| Dealings with members-final | 12.0 | 11.9 | 0.4 |

37. Our assessment of materiality is set with reference to the Funds' net investment assets. We consider this to be one of the principal considerations for the users of the financial statements when assessing the financial performance.
38. As outlined in our External Audit Plan we considered transactions when dealing with members (i.e. contributions and expenditure incurred providing payments to pensioners) to also be of key interest to the users. This is reported in the first section of the Fund Account and contains information about the day to day operation of the Funds.
39. ISA 320 states that in certain circumstances it is appropriate to set a materiality amount for particular classes of transactions for which lesser amounts than the overall materiality could influence the decision of the users of the accounts. We have therefore set a separate materiality for transactions relating to dealings with members, based on the expenditure incurred for providing payments to pensioners.

Performance materiality

40. Performance materiality is the amount set by the auditor for each financial statement area, to reduce to an appropriately low level the probability that collectively any uncorrected and undetected

misstatements are less than materiality for the financial statements as a whole.

41. We set a performance (testing) materiality for each area of work which was based on a risk assessment for the area. We perform audit procedures on all transactions and balances that exceed our performance materiality. This means that we are performing a greater level of testing on the areas deemed to be of significant risk of material misstatement. Performance testing thresholds used are set out in the table below:

| | Area risk assessment £million | | |
|------------------------------------------------------------------------------------------|-------------------------------|--------|-------|
| | High | Medium | Low |
| Lothian Pension Fund ¹ (Group ² and parent)- overall | 58.50 | 70.20 | 87.75 |
| Lothian Pension Fund ¹ (Group ² and parent)- dealings with members | 5.95 | 7.14 | 8.93 |
| Scottish Homes Pension Fund- overall | 1.25 | 1.50 | 1.88 |
| Scottish Homes Pension Fund- dealings with members | 0.18 | 0.21 | 0.27 |

42. We agreed with the Pensions Committee that we would report on all material corrected misstatements, uncorrected misstatements with a value in excess of 5% of overall materiality, as well as other misstatements below that threshold which, in our view, warranted reporting on qualitative grounds.

Group accounts

43. The Funds' annual report includes accounts for Lothian Pension Fund and Scottish Homes Pension Fund.
44. Lothian Pension Fund accounts are prepared on a group basis following the creation of two special purpose vehicles, LPFE Ltd and LPFI Ltd in October 2014. The companies are wholly owned and controlled by the City of Edinburgh Council.
45. We reviewed the consolidation process in 2018/19 and concluded the subsidiary companies had been

³ From 2018/19 Lothian Pension Fund has merged with Lothian Buses Pension Fund and the materiality is based on the combined assets of the Funds.

⁴ Lothian Pension Fund group comprises Lothian Pension Fund (incorporating Lothian Buses Pension Fund transactions and balances), LPFE Ltd and LPFI Ltd



correctly included in the group accounts of Lothian Pension Fund.

Audit differences

46. We are pleased to report that our audit identified no material adjustments. In addition, we can confirm there were no unadjusted errors relating to the 2018/19 financial statements.
47. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual report and financial statements.
48. The most significant disclosure change related to the present value of promised retirement benefits.
49. In 2018/19 there were 2 significant legal cases in relation to pension scheme's which we considered to have a potential financial impact on the Funds' present value of promised retirement benefits:
- **McCloud Judgement:** This case related to an employment tribunal ruling that transitional provisions impacting on a public sector final salary scheme were unlawfully age discriminatory. This was upheld in the Courts in December 2018 although the Government at that stage sought leave to appeal this judgement. The ruling has implications for all public service schemes including the LGPS funds. In June 2019, the Supreme Court has rejected the Government's request for a further appeal.
 - **Guaranteed minimum pension (GMP)** was accrued by members of the Local Government Pension Scheme (LGPS) between 6 April 1978 and 5 April 1997. The value of GMP is inherently unequal between males and females for a number of reasons, including a higher retirement age for men and GMP accruing at a faster rate for women. However overall equality of benefits was achieved for public service schemes through the interaction between scheme pensions and the Second State Pension. The introduction of the new Single State Pension in April 2016 disrupted this arrangement and brought uncertainty over the ongoing indexation of GMPs, which could lead to inequalities between men's and women's benefits. As an interim solution to avoid this problem, GMP rules were changed so that the responsibility for ensuring GMPs kept pace with inflation passed in full to pension schemes themselves for members reaching state pension age between 6 April 2016 and 5 April 2021. This new responsibility leads to increased costs for schemes (including the LGPS) and hence scheme employers.
50. We requested the Funds' consider the likely implications for their financial statements and consult with their actuary on whether a revised estimate was required. The advice from the actuary was that the GMP impact was likely to be immaterial and that McCloud may have more significant consequences. This was in line with our understanding of the sector and therefore revised figures were only requested to show the impact of the McCloud judgement. The disclosures in note 23 in the accounts have been updated to show a present value of promised retirement benefits of £9,435 million, an increase of £102 million against the amount disclosed in the draft accounts.
51. Lothian Pension Fund group accounts disclose the actuarial valuation of the pension liability for LPFE Ltd. The actuary provided revised figures taking into consideration the McCloud judgement. The impact on the liability is £0.282 million. Management has considered the movement and elected not to adjust the accounts on the basis of materiality and to reflect that the figures used are from LPFE's audited accounts. Full details of the adjustment are included in appendix 3.

An overview of the scope of our audit

52. The scope of our audit was detailed in our External Audit Plan, which was presented to the Pensions Committee in March 2019. The plan explained that we follow a risk-based approach to audit planning that reflects our overall assessment of the relevant risks that apply to the Funds. This ensures that our audit focuses on the areas of highest risk. Planning is a continuous process and our audit plan is subject to review during the course of the audit to take account of developments that arise.
53. At the planning stage we identified the significant risks that had the greatest effect on our audit. Audit procedures were then designed to mitigate these risks.
54. Our standard audit approach is based on performing a review of the key financial systems in place, substantive tests and detailed analytical procedures. Tailored audit procedures, including those designed to address significant risks, were completed by the audit fieldwork team and the results were reviewed by the audit manager and audit partner. In performing our work we have applied the concept of materiality, which is explained earlier in this report.

Other matters identified during our audit

55. During the course of our audit we noted the following:



Other information in the annual report and accounts

56. “Other information” in the annual report and accounts comprises any information other than the financial statements and our independent auditor’s report. We do not express any form of assurance conclusion on the “other information” except as specifically stated below.

Management Commentary

57. The management commentary is a requirement of the Local Authority Accounts (Scotland) Regulations 2014 and is intended to assist readers in understanding the financial statements and provide an overview of the organisation and its performance.

58. Guidance issued by the Scottish Government (Local Government Finance Circular 5/2015 also provides a guide as to the minimum required disclosures in the management commentary including:

- The context of the annual report and financial statements;
- Insight into the priorities of the Funds’ and strategies adopted to achieve these priorities and objectives;
- Information on future plans;
- KPIs which measure the investment performance of the Funds’; and
- Information on the principal risks and uncertainties facing the authority.

59. We have concluded that the management commentary has been prepared in line with the regulations and Scottish Government guidance and is consistent with the financial statements.

Annual governance statement

60. We have reviewed the Funds’ annual governance statement against the relevant guidance: Delivering Good Governance in Local Government.

61. We consider the coverage of the annual governance statement to be broadly in line with expectations.

62. We highlighted a minor disclosure issue within the governance statement at paragraph 34 in relation to the internal audit opinion. This will be updated in the revised accounts.

63. Subject to this adjustment we have concluded that the annual governance statement is in line with the required guidance and is consistent with the accounts and assurances provided in year.

Governance compliance statement

64. The Local Government Pension Scheme (Scotland) Regulations 2014 require all pension funds to prepare a Governance Compliance Statement. The purpose of this statement is to compare the Funds’ governance arrangements with those standards set out in guidance from the Scottish Ministers.

65. We have reviewed the Governance Compliance Statement and we are satisfied the disclosures comply with guidance issued by Scottish Ministers and are not inconsistent with our knowledge of the arrangements in place at the Funds.

Remuneration and staff report

66. In February 2018 staff previously employed by the City of Edinburgh Council with responsibility for the Funds’ were transferred to LPFE Ltd. From this point all new staff employed for roles with the Funds were employed by LPFE Ltd.

67. The Local Authority Accounts (Scotland) Regulations 2014 (the 2014 Regulations) require that where a local government body has a subsidiary the details of the Chief Executive’s salary and any employee with remuneration over £0.150 million is included in a remuneration report.

68. The Funds’ therefore produced a remuneration report for the first time in 2018/19. The Funds’ met all statutory reporting requirements, however, the Funds’ expressed concern that the revised disclosure has decreased the transparency of reporting with regards to senior manager pay costs. This is an area we will revisit in 2019/20 to establish if clarity and transparency can be improved while meeting the statutory disclosure requirements.

69. We have concluded that the audited part of the remuneration and staff report has been prepared in accordance with directions from Scottish Ministers and is consistent with the financial statements.

Legality

70. We have planned and performed our audit recognising that non-compliance with statute or regulations may materially impact on the annual report and accounts.

The Local Authority Accounts (Scotland) Regulations

71. As part of our audit we reviewed the Funds’ compliance with the 2014 Regulations, in particular



with respect to regulations 8 to 105 as they relate to the annual report and financial statements.

72. In 2018/19 we received an objection to the notice of the public right to inspect. Upon review there was found to be a delay in displaying the hard copy of the public inspection notice which is required to be published prior to 17 June as outlined by the 2014 Regulations. The notice was published in the local newspaper and on the City of Edinburgh Council website by 17 June 2019, however, was not available at Council offices until 26 June 2019.
73. We highlighted issues with regards to the public inspection in 2017/18 and we would recommend the Funds make arrangements to ensure full compliance in 2019/20. We have noted that prior period issues in this area are ongoing in appendix 2.
74. Other than the above issue we concluded that appropriate arrangements are in place to comply with these Regulations.

Banking arrangements

75. It was highlighted during the course of our audit that the Pension Fund had not been operating its bank account in line with the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010. There is a requirement for administering authorities to hold a separate bank account for funds and this should be used to hold pension fund money.
76. The Funds use the Council bank account to ensure that no unfunded payments are taken from a pension fund bank account.
77. In 2018/19 the Funds have requested that “unfunded discretionary payments” be transferred to the Scottish Public Pensions Agency which would mitigate the requirement for the Funds’ to use the Council’s bank account. However, this had not been agreed by the year end.
78. If the transfer of unfunded discretionary payments is not possible the resolution of this issue would depend on the procurement of a new ledger system which did not progress in 2018/19.

Qualitative aspects of accounting practices and financial reporting

79. During the course of our audit, we consider the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided by the annual accounts. The following observations have been made:

⁵ Regulations 8 to 10 relates to the preparation and publication of unaudited accounts, notice of public right to inspect and object to

the accounts and consideration and signing of the audited accounts.



| Qualitative aspect considered | Audit conclusion |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>The appropriateness of the accounting policies used.</p> | <p>We have reviewed the significant accounting policies which are disclosed in the annual report and financial statements of the Funds. We consider the policies to be appropriate to the Funds, however, we have noted that the Funds have departed from CIPFA Guidance in relation to investment management expenses.</p> <p>During 2015/16 CIPFA issued guidance stating that pension funds should only report the direct costs of using investment managers. The impact of this is that investment management costs associated with fund of funds transactions would not be reported. The Funds feel this would detract from the transparency of the accounts and have reported indirect costs of £5.062 million for Lothian Pension Fund (2017/18: £5.912 million). There were no indirect costs for Scottish Homes in either 2017/18 or 2018/19.</p> <p>The impact of this accounting treatment is to increase the investment management expense which is offset by an increase in the change in market value of investments. The net impact on the fund account is therefore zero.</p> |
| <p>The timing of the transactions and the period in which they are recorded.</p> | <p>We did not identify any concerns over the timing of transactions or the period in which they were recognised.</p> |
| <p>The appropriateness of the accounting estimates and judgements used.</p> | <p>The Funds have significant levels of accounting estimates and judgements used by management in preparing the financial statements. The principal areas of estimation concern the valuation of unquoted private equity and infrastructure investments and the actuarial valuation of promised retirement benefits. These estimates have been informed by advice from qualified, independent experts. We evaluated the competence, objectivity and capability of management experts in line with the requirements of ISA (UK) 500 and concluded that use of the expert is appropriate.</p> <p>We are satisfied with the appropriateness of the accounting estimates and judgements used in the preparation of the annual report and financial statements. We have considered the disclosures around the estimates, including sensitivity analysis and concluded that they are appropriate.</p> |
| <p>The appropriateness of the going concern assumption</p> | <p>We have reviewed the detailed financial forecasts for 2019/20. Our understanding of the legislative framework and activities undertaken provides us with sufficient assurance that the Funds will continue to operate for at least 12 months from the signing date.</p> |
| <p>The potential effect on the annual accounts of any uncertainties, including significant risks and related disclosures that are required.</p> | <p>We have not identified any uncertainties, including any significant risk or required disclosures, which should be included in the annual accounts beyond those already made.</p> |
| <p>The extent to which the annual accounts have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed.</p> | <p>From the testing performed, we identified no significant unusual transactions in the period.</p> |



| Qualitative aspect considered | Audit conclusion |
|--------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Apparent misstatements in the annual report or material inconsistencies with the financial statements. | The annual report contains no material misstatements or inconsistencies with the financial statements. |
| Any significant annual accounts disclosures to bring to your attention. | There are no significant annual accounts disclosures that we consider should be brought to your attention. All the disclosures required by relevant legislation and applicable accounting standards have been made appropriately. |
| Disagreement over any accounting treatment or annual accounts disclosure. | While disclosure and presentational adjustments were made during the audit, there was no material disagreement during the course of the audit over any accounting treatment or disclosure. |
| Difficulties encountered in the audit. | There were no significant difficulties encountered during the audit. |

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4. Financial sustainability

Financial sustainability looks forward to the medium and longer term to consider whether the Funds' planning processes support the future delivery of services.



The Funds have effective arrangements in place to ensure the ongoing sustainability of the pension funds.

The focus of their investment strategy is to ensure a sufficient return over the long term to meet the funding objectives outlined by the Funding Strategy Statement. Performance over 5 years shows they are managing investment above benchmark.

There is an ongoing risk that the pension scheme is not affordable for admitted bodies and Lothian Pension Fund has reported an increase in the number of bodies leaving the Fund and an increase in the cessation liability following the 2017 triennial valuation.

There is an ongoing review of the structure of Local Government Pension Schemes in Scotland. This could have a significant impact on the Funds and will be monitored in 2019/20.



Significant audit risk

Our audit plan identified a significant risk in relation to financial sustainability under our wider scope responsibilities.

Financial sustainability: Market volatility

The Funds held investments of £6.628 billion as at 31 March 2018. Investment strategies are in place for each of the funds which outline the Funds approach to ensure that all members and their dependents receive their benefits when they become payable. The investment strategy was recently updated and approved by the Pensions Committee in December 2018.

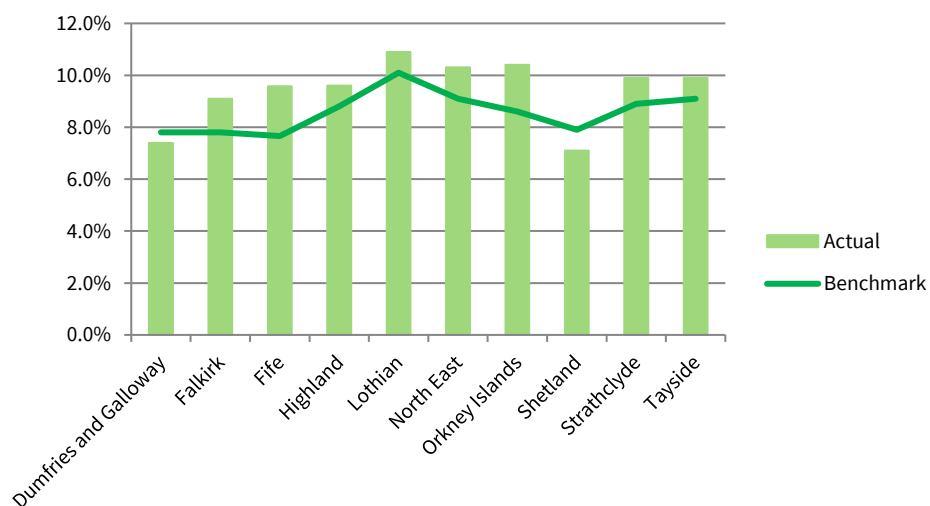
The objective of the Funds is that over the short term the fund should perform better than its strategic allocation if markets fall significantly. The Investment Strategy Panel and the internal investment team monitor investment risks on a regular basis.

While it is noted that the Funds investment strategy is designed in such a way to withstand market volatility in the long term, we have noted that worldwide political events had a significant impact on the market in 2018 and volatility is expected to continue in 2019. There is a risk that the value of investments is significantly impacted by events within the wider political environment.

Excerpt from the 2018/19 External Audit Plan

- 80. Financial sustainability of the Funds relates to the performance over the longer term. The investment objective of the Funds is to achieve a return on the fund assets which is sufficient over the long term to meet the funding objectives outlined in the funding statement strategy.
- 81. When considering the risk over market volatility we have considered the performance over the longer term.

Exhibit 3: Annualised 5 year returns across LGPS Scotland Funds against benchmark



Source: Unaudited Pension Fund Annual Report and Accounts⁶

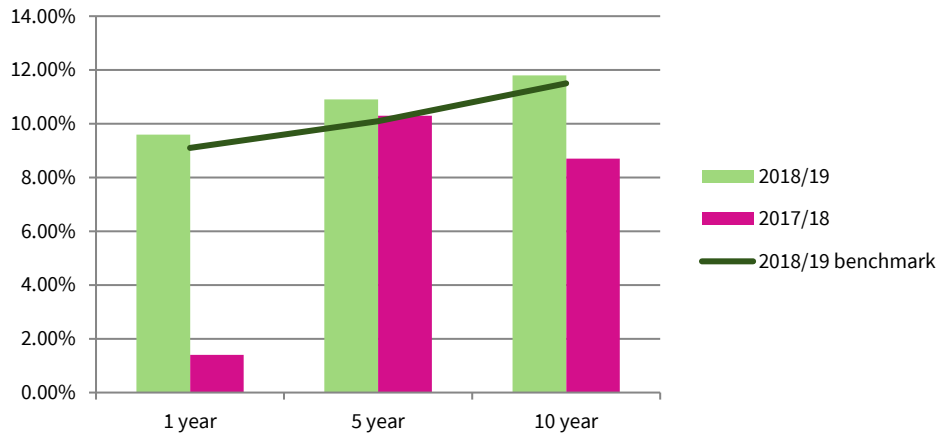
- 82. Lothian Pension Fund is reporting the highest annualised 5 year return and is one of eight funds reporting returns above the longer term benchmark.

⁶ Scottish Borders Pension Fund do not publish their 5 year annualised return



83. Lothian Pension Fund performance in 2018/19 was consistently above benchmark across short, medium and long term and has improved since 2017/18. No benchmark was set for Scottish Homes Pension Fund as investments are mandated by the Scottish Government to be held in gilts.

Exhibit 4: Performance against benchmark and compared to prior year



Source: Unaudited Lothian Pension Fund Annual Report and Accounts

84. We have concluded that the Funds have an appropriate approach to managing investments; however, within the current political climate market volatility will continue to be a risk.

85. The Funds’ have this as a risk on the risk register and it is currently rated green due to the predicted low impact on service delivery and likelihood of occurrence.

Employers within the scheme

86. A full actuarial valuation in 2017 highlighted that Lothian Pension Fund was behind the target level for funding (98% against a target of 100%). Both Lothian Buses Pension Fund and Scottish Homes Pension Fund were ahead of target.

87. Contribution rates across employers within Lothian Pension Fund generally increased leading to affordability issues.

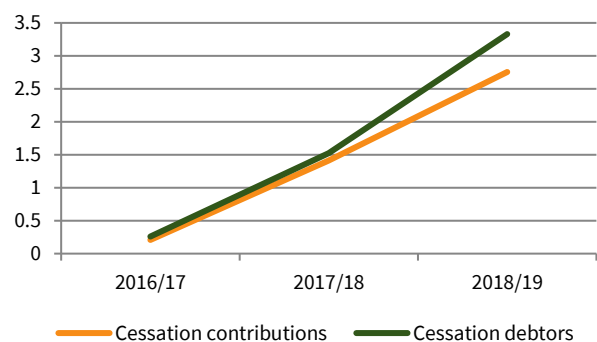
88. In recognition of this Lothian Pension Fund updated their Funding Strategy Statement with a requirement for employing bodies to confirm their commitment to meet the minimum contributions.

89. In 2018/19 three employers elected to leave the Fund and a further admitted body was wound up and left the Fund.

90. At the end of 2018/19 there were 13 ceased employees which have set up or are setting up funding agreements with Lothian Pension Fund.

91. The level of cessation contributions has increased by 1225% since 2016/17, with the long term debtors relating to ceased employers rising by a similar level.

Exhibit 5: Cessation contributions and debtors (£m)



Source: Lothian Pension Fund annual accounts

92. There is therefore an ongoing risk that an employer fails to pay contributions leading to increased contributions and pressure on other scheduled and admitted bodies.



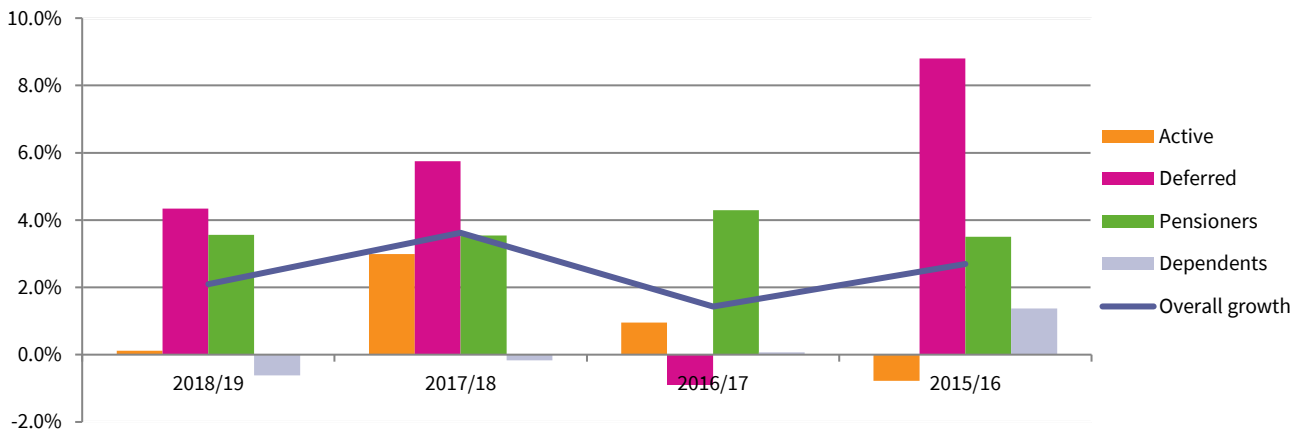
Membership

93. Lothian Pension Fund is a multi-employer fund with 15 scheduled bodies, including 4 Councils, and 68 admitted bodies. The scheme has a significant membership profile with active members being the majority. This differs from Scottish Homes Pension Funds which is a single employer scheme and have a

majority of inactive members (deferred, pensioners and dependents).

94. Analysis shows that although there is an overall increase in membership at Lothian Pension Fund, active members have been growing at a slower rate than deferred members and pensioners.

Exhibit 6: % year on year growth in members across categories



Source: Lothian Pension Funds Annual Report and Accounts

95. The fund relies on active members to meet the payments to pensioners and there is a risk that if growth in pensioners, increases at a faster rate than active members additional affordability pressures will be faced by Lothian Pension Fund.

- Pool investments between the 11 funds; and
- Merge the 11 funds into one or more new funds.

96. It is, however, noted that active members have only decreased by 1.3% as a proportion of total members moving from 42.3% of members in 2015/16 to 41% of members in 2018/19. Pensioners have increased by 1.2% as a proportion of the total members and in 2018/19 make up 30% of the membership of Lothian Pension Fund. The movement is therefore slow and this is likely to be a low risk area with regards to financial sustainability.

99. The consultation period opened in June 2018 and closed in December 2018. Responses were received from 56 bodies ranging from pension funds to professional bodies to individuals.

100. The results of the review to date are that there is general support for some change to the structure with the majority considering some form of co-operation as the best option

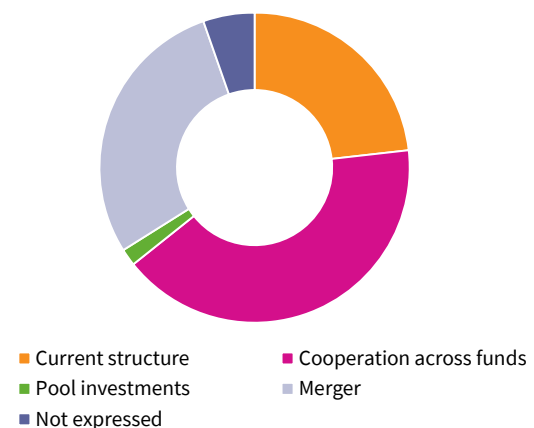
LGPS Consultation

97. A review of the structure of the Scottish Local Government Pension Schemes was agreed with stakeholders and Scottish Government in 2015 when changes to the scheme and Scheme Advisory Board ('SAB') were introduced.

98. In February 2017, SAB produced a review report which highlighted 4 options for the future structure of the local government pension scheme in Scotland:

- Retain the current structure with 11 funds;
- Promote cooperation in investing and administration between the 11 funds;

Exhibit 7: Responses to LGPS Scotland consultation



Source: Scheme Advisory Board



101. Lothian Pension Fund responded in favour of reform, specifically the creation of conditions in which like-minded schemes could seek to merge.
102. The draft report went to the Scheme Advisory Board on 24 April 2019 and further work on how to proceed is scheduled. We will continue to monitor the position in 2019/20.

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5. Financial management

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.



The Funds have effective arrangements in place for financial management and the use of resources

Lothian Pension Fund's investment performance increased in 2018/19 and was above the short term benchmark and national average.

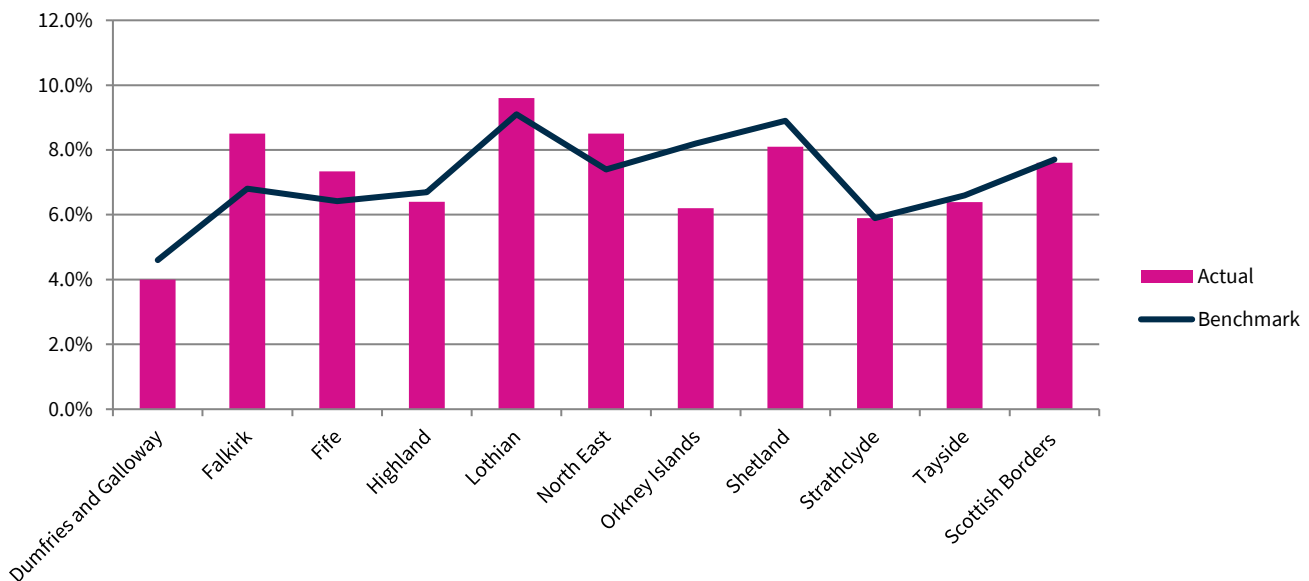
The net assets of Lothian Pension fund have risen in 2018/19 and Scottish Homes Pension Fund assets have not moved. The promised retirement benefits have increased across all three funds.



Investment performance

- 103. The Funds report their performance with regards to returns on investments as part of the annual report and financial statements. As shown in Exhibit 8 below Lothian Pension Fund, reported performance above the 1 year benchmark. This is an improvement from 2017/18 where performance was significantly behind benchmark.
- 104. Investment performance across LGPS in Scotland was generally stronger in 2018/19 than in 2017/18. The average return on investments in 2018/19 was 7.1% a small increase from 6.12% in 2017/18.

Exhibit 8: One year investment performance across LGPS Funds



Source: Unaudited LGPS Scotland Annual Report and Accounts

- 105. In contrast to 2017/18 Lothian Pension fund was above the national average in 2018/19 and was one of only four funds to outperform the benchmark.
- 106. We have highlighted in the past that the focus of the funds is long term stability and we have noted in the Financial Sustainability section that the longer term performance is also above benchmark.
- 107. The short and long term results indicate that the investment portfolio is being managed appropriately.

Financial position

- 108. The movement in net assets of the funds varied across each fund as shown in Exhibit 9. Both funds have reported a net withdrawal position from dealings with members, which is consistent with prior year. In 2018/19 the net return on investments at Lothian Pension Fund exceeded the withdrawals position leading to an overall increase in net assets. Scottish Homes Pension Fund return on investments met the net withdrawal meaning the level of net assets was maintained from 2017/18.

Exhibit 9: Lothian Pension Funds' Financial Position

| | Net assets | | | Present value of retirement benefits | | |
|----------------------|------------|---------|------------|--------------------------------------|---------|------------|
| | 2018/19 | 2017/18 | % Movement | 2018/19 | 2017/18 | % Movement |
| Lothian Pension Fund | 7,819 | 7,174 | 8.99% | 9,333 | 8,254 | 13.07% |
| Scottish Homes | 164 | 164 | 0.00% | 135 | 134 | 0.75% |



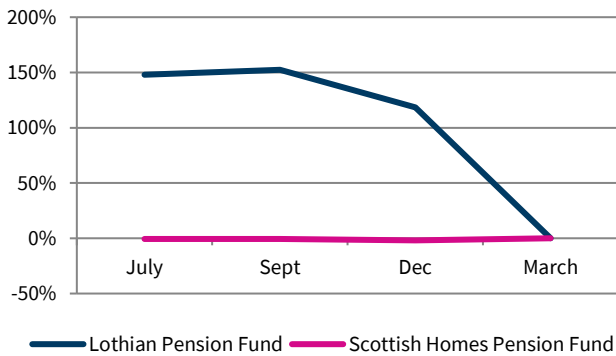
Source: Lothian Pension Funds Annual Report and Accounts

109. Hymans Robertson provided an estimate of the present value of the promised retirement benefits. The discount rate applied increased to 2.7% from 2.4% in the previous year. This has a negative effect on the scheme obligation, resulting in an increase in the obligation. The net pension obligation also includes the impact of the McCloud judgement as explained at paragraphs 50 and 51.

Financial Performance

- 110. As part of our audit we considered the Funds’ systems of budgetary control and financial management and did not identify any significant deficiencies.
- 111. Service update reports are provided to each meeting of the Pensions Committee. The reports include forecasts to the year-end and explanations for any movements.
- 112. In year update reports highlighted that a net withdrawals position was expected, however, the forecasts were significantly above the year-end position.

Exhibit 10: Reported movement against the year-end position



Source: Pensions Committee Service Updates

113. The Lothian Pension Fund predicted position in December 2018 was 118.3% higher than the actual year-end position. This was due to employee and employer contributions being £10 million higher than anticipated and lump sums being £5 million lower than forecast. While the actual position is better than forecast, we would recommend the Funds investigate how forecasting information can be improved.

Action plan point 1

Systems of internal control

- 114. We have evaluated the Funds’ key financial systems and internal financial controls to determine whether they are adequate to prevent material misstatements in the annual accounts. Our approach has included documenting the key internal financial controls and performing walkthroughs to confirm that they are operating as intended.
- 115. We identified three areas where there was an opportunity to improve the control environment:
 - registers of interest compliance monitoring;
 - review of bank reconciliations by a senior member of the finance team; and
 - verification of all key details on transfers of individuals from the scheme.
- 116. Full details of the controls weaknesses and our recommendations are outlined in appendix 2.

Action plan points 2 to 4

117. We identified a number of areas for improvement in 2017/18 which were followed up at the year-end. We have reported progress against outstanding actions in appendix 2.

Prevention and detection of fraud and irregularity

- 118. Our audit was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity. Lothian Pension Fund was not required to participate in the National Fraud Initiative in 2018/19 but did so voluntarily.
- 119. We found the Funds’ arrangements for the prevention and detection of fraud and other irregularities to be adequate and appropriate.

Standards of conduct

- 120. In our opinion the Funds’ arrangements in relation to standards of conduct and the prevention and detection of bribery and corruption are adequate.
- 121. Our conclusion has been informed by a review of the arrangements for adopting and reviewing standing orders, financial instructions and scheme of delegation and for complying with national and local codes of conduct.



Internal audit

122. An effective internal audit service is an important element of the Funds' governance arrangements. The City of Edinburgh Council provide the Funds' internal audit service. During our audit we considered the work of internal audit wherever possible to avoid duplication of effort and make the most efficient use of the Funds' audit resource
123. In 2018/19 it was noted that the service did not fully comply with Public Sector Internal Audit Standards in relation to quality assurance reviews. The Pensions Committee were advised that the instances of non-conformance have had no direct impact on the quality of internal audit reviews completed for the Funds in 2018/19.
124. Internal audit has advised that quality assurance reviews will be reinstated with effect from 1 April 2019.
125. In 2018/19 we did not place formal reliance on the work of internal audit, however, we have considered their findings in respect of our wider scope responsibilities and we are grateful to the internal audit team for their assistance during the course of our work.



6. Governance and transparency

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making and transparent reporting of financial and performance information.



Governance arrangements at the Funds are deemed to be appropriate.

Our assessment has been informed by a review of the corporate governance arrangements in place, the information provided to the Board and Committees as well as the risk management arrangements in place.

We identified a significant risk regarding the transfer of assets from Lothian Buses Pension Fund to Lothian Pension Fund. We have confirmed appropriate governance processes were in place during 2018/19 to ensure the transfer was in line with relevant regulations.



Significant audit risk

126. Our audit plan identified a significant risk in relation to financial sustainability under our wider scope responsibilities.

Governance and transparency: Lothian Buses Pension Fund merger

As noted in our financial statement section above, the Pensions Committee approved the transfer of the assets and liabilities of the Lothian Buses Pension Fund into the Lothian Pension Fund in March 2018, subject to the satisfactory completion of a revised admission agreement and shareholder guarantee. The transfer took place on 31 January 2019.

Mergers of local government pension schemes are highly unusual and therefore, there is significant risk around the governance, consultation and communication of the transfer.

Excerpt from the 2018/19 External Audit Plan

127. An investment strategy review in 2016 highlighted that Lothian Buses Pension Fund was defined in regulations as a sub-fund of Lothian Pension Fund. It was determined at this stage that there was an option for the Fund to be subsumed into Lothian Pension Fund. It was agreed at the meeting to begin exploring options to proceed with the merger.
128. As noted in the annual report and accounts section of the report, Lothian Buses Pension Fund was established under the Local Government Superannuation (Funds) (Scotland) Regulations 1986 (the 1986 Regulations). Regulation 8 of the 1986 Regulations outlines the process for dissolution of further funds. The administering authority may if they think fit dissolve a further fund and transfer the assets thereof, to the administering fund. Any entitlement to participate in the benefits of the further fund shall become an entitlement to participate in the benefits of the fund and the fund shall become the appropriate superannuation fund for those participants.
129. The administering authority may not dissolve a further fund unless they have given notice of not less than 28 days to the bodies whose employees are entitled to participate in that fund of their intention to dissolve the fund.
130. A transfer agreement ('the Deed of Transfer') was put in place between Lothian Buses and the City of Edinburgh Council in January 2019. This outlines terms and conditions for the transfer of the Fund to within the Main Fund.
131. Subsequent to this Lothian Buses and the City of Edinburgh Council entered into a revised admission agreement which states "The Authority and the Admission Body (together the "Parties") have agreed that the Authority shall transfer all of the assets and liabilities of the Lothian Buses Fund to the Main Fund, so that all benefits payable or prospectively payable under the Lothian Buses Fund will instead be payable under the Main Fund, with future contributions in respect of the Admission Body's participation in the Local Government Pension Scheme being paid into the Main Fund."
132. Following a review by the Funds actuary and legal advisers, it was determined that a guarantee would be required from the shareholders of Lothian Buses (City of Edinburgh Council; West Lothian Council; East Lothian Council and Midlothian Council).
133. We have concluded that Lothian Pension Fund has correctly assessed Lothian Buses Pension Fund as a 'further fund' as defined by the 1986 regulations and that appropriate confirmations from Lothian Buses and the City of Edinburgh Council were in place to allow the transfer to take place. In addition we have confirmed that revised admission



agreements and guarantees have been put in place in line with legal advice provided to the Funds.

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Governance structure

134. The Pensions Committee, supported by an Audit Sub-Committee, has been delegated responsibility for governance by the City of Edinburgh Council, the administering authority.
135. As outlined by the City of Edinburgh Council Scheme of Delegation the Pensions Committee has responsibility for the administration, management and investment strategy for the Funds.
136. In line with the requirements of the Public Service Pension Act 2013 the Pensions Committee is supported by a Pensions Board.
137. The Pensions Board is responsible for establishing arrangements that ensure proper conduct of the affairs of the Board and meet quarterly on a concurrent basis with the Pension Committee.
138. The Funds complied with best practice and appointed an independent professional observer to the Board and Committee. The appointed independent observer resigned in February 2018 and a replacement was appointed in May 2018.
139. In line with legislation if more than half of the members of the Pension Board disagree with a decision of the Pension Committee then they can request in writing that the Pension Committee review that decision. There have been no requests to review decisions in 2018/19.
- Regulated investment advisor, LPFI Ltd (from December 2018); and
 - two external independent investment consultants.
143. The joint Investment Strategy Panel covers joint working arrangement with Falkirk Pension Fund and Fife Pension Fund.
144. The Joint Investment Strategy Panel meets quarterly and considers the appropriate investment management structure required to implement the Funds' investment strategy. In addition it is responsible for:
- making recommendations about investment strategy; and
 - directing and monitoring strategy implementation and risk.
145. The primary focus of the panel during 2018/19 has been the implementation of existing strategies for Lothian Pension Fund, Lothian Buses Pension Fund (until merger with Lothian Pension Fund in February 2019) and Scottish Homes Pension Fund.
146. In addition to this following the merger of Lothian Buses Pension Fund with Lothian Pension Fund the Panel considered the Investment Strategy for the revised structure.
147. From December 2018, Lothian Pension Fund operated four investment strategies recognising the differing requirements of the various scheduled and admitted employers.

Training and development

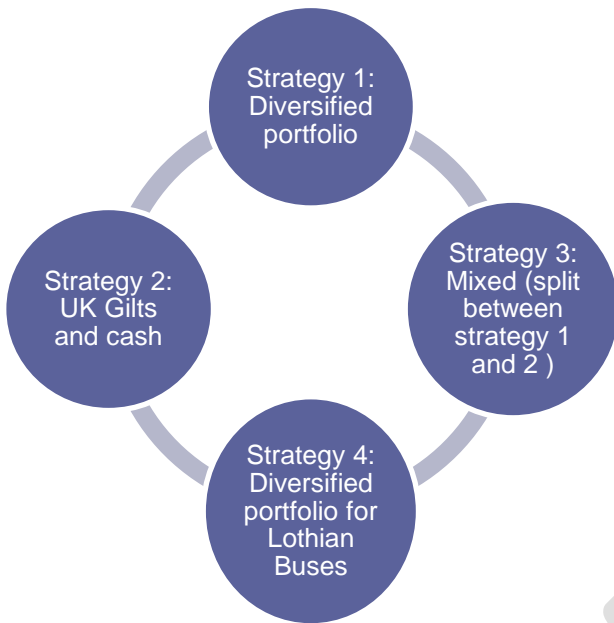
140. Due to the specialised nature of the Funds, it is vital that members have the appropriate knowledge and understanding to provide appropriate challenge and operate effectively. Training is therefore seen as a fundamental requirement for all Committee and Board members.
141. Our review found that all current Pension Committee and Board members met the requirement to have a minimum of 21 hours training.

Joint Investment Strategy Panel

142. The Pensions Committee has delegated responsibility for investment strategy to the Executive Director of Resource who takes advice from a Joint Investment Strategy Panel made up of:
- Chief Executive, LPFI Ltd (until December 2018);
 - Chief Investment Officer LPFI Ltd;



Exhibit 11: Lothian Pension Fund investment strategies



Source: Joint Investment Strategy Panel annual report

148. Scottish Homes Pension fund achieved full funding at the 2017 actuarial valuation and therefore the strategy is low risk and designed to protect from short term market changes. This is similar to Strategy 2 which focuses on investments in UK gilts and cash.

Openness & Transparency

149. Audit Scotland also cited a risk in relation to public sector organisations keeping pace with public expectations on openness and transparency.
150. In our opinion, the Funds demonstrates good practice with respect to openness and transparency in the following ways:
- Committee agendas and papers are published on the Funds' website in advance of meetings being held;
 - Committee minutes and updates are available to the public;
 - Key publications (including operational plan, results of annual review, annual accounts) are available on the Funds' website; and
 - the quality of reports presented to the Pensions Committee is such that it supports the transparency of decision making.

In September 2018 the Pensions Committee considered a report as to whether their proceedings should be included as part of The council web-casting facility. It was agreed that the

benefits arising from the existing format outweighed those that would arise from web-casting.

Impact of EU withdrawal

151. Audit Scotland has highlighted EU withdrawal as a significant risk facing public bodies across Scotland. Three streams of potential impact were identified:

- Workforce;
- Funding; and
- Regulation.

152. The Funds have considered the impact across all three areas, and have identified that this is an area of low risk for the pension fund. From an initial assessment of the workforce and funding streams no significant implications have been identified. This is in line with our understanding of the nature of the Funds'.

153. Regulations may have a more significant impact, however, the Funds consider that as a UK based pension Fund collaborating with other UK based funds the impact is expected to be limited

154. The primary consideration was the impact of the EU withdrawal on movement in investments and as outlined in the financial sustainability and value for money sections the Funds have tailored their objective and approach to focus on long term safeguarding of returns.

Key supplier dependency

155. Following the collapse of Carillion, it became apparent that public sector bodies face significant risks where suppliers are experiencing difficult trading conditions.
156. We have evaluated the Funds' key suppliers and considered the contract management arrangements as part of our work on expenditure and value for money
157. There are a number of areas where the Funds use one key supplier e.g. custodian, pensions administration and investment managers. However, we are aware appropriate contract management is in place and that there is a range of potential suppliers should a change be necessary. We therefore consider this to be low risk.
158. The Funds ICT environment is through the City of Edinburgh Council and their supplier. In 2018/19 the Funds have encountered delays and service disruptions across a number of ICT areas.



159. The ongoing issues are on the risk register and graded high risk and the Funds attend quarterly meetings with City of Edinburgh Council ICT officers and the supplier.
160. We consider the actions of the Funds with regard to key suppliers to be appropriate and proportionate to the level of risk.

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7. Value for money

Value for money is concerned with the appropriate use of resources and ensuring continual improvement of services delivered



The Funds' investment performance is subject to regular review by the Pension Committee.

The Funds have appropriate arrangements in place to secure value for money through appropriate monitoring of performance of investments and the administration of the Funds.

Investment manager operations

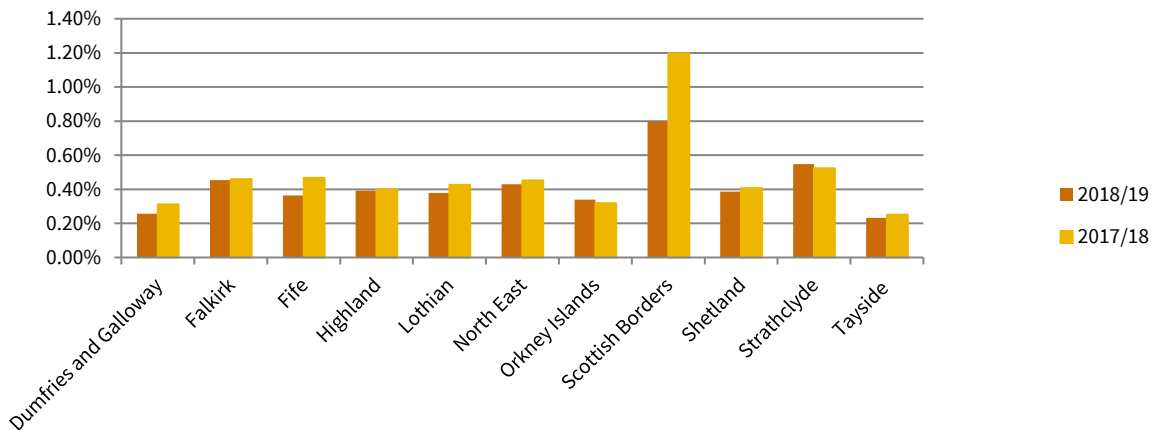
161. Lothian Pension Fund operates two special purpose vehicles: LPFE Ltd and LPFI Ltd. Both companies are wholly owned and controlled by the Council.
162. The special purpose vehicles were established to support the investment programme of the in-house investment team by providing organisational arrangements consistent with the capability, systems and controls of authorised investment companies.
163. Effective leadership is key to the success of the Funds achievement of objectives. In 2018/19 there was a significant change to the leadership team at LPFI Ltd.
164. In June 2018 the Chief Executive announced her intention to leave the Funds with a planned leaving date of December 2018. A new Chief Executive was appointed and commenced his position in January 2019.
165. There has been no significant change to the operation of the Funds to date and the proportion of funds managed internally has remained steady at approximately 85% of investments since 2015/16.

Management expenses

166. Lothian Pension Fund reported management expenses of £38.634 million in 2018/19, an increase of 1.8% from the prior year.
167. Management expenses are split into three main categories: administrative costs; investment manager expenses and oversight and governance costs. Investment management expenses account for 90% of total management expenses.
168. In year Lothian Pension Fund's investment manager expenses (excluding indirect expenses) fell marginally as a proportion of net assets. This is broadly in line with trends across the Local Government Pension Funds.



Exhibit 12: Lothian Pension Funds' Financial Position



Source: LGPS Scotland Unaudited Annual Report and Accounts

169. The analysis above does not include indirect investment management costs as CIPFA guidance states that only direct investment management costs i.e. those that the fund can control should be reported. Lothian Pension Fund reported £5.062 million of indirect manager expenses in 2017/18. It is not possible to benchmark the impact of indirect management costs across Scottish Local Government Pension Funds.
170. Investment manager expenses can vary due to a number of factors including actual returns on investments and the nature of the investments assets held.
171. The Funds undertake annual benchmarking exercises using externally provided data, covering 41 LGPS funds and a wider global universe of 346 funds.
172. Analysis of investment costs is carried out by an independent provider, CEM benchmarking Limited. In 2018/19 Lothian Pension Fund reported an actual investment cost of 0.43% of net assets which was below the benchmark of 0.55%.
173. The Funds credit the improved performance against benchmark to the high percentage of assets managed internally.
174. Analysis of pension administration costs was undertaken by the Chartered Institute of Public Finance Accountants. Pension cost per member was in 2018/19 £23.38, which is higher than the average cost of local authority funds of £21.74. The cost per member is broadly deemed to be in line with other local authority funds who operate within the range of costs of £11 to £61 per member.

175. The Funds have noted that there are restrictions over the comparability of the data and that the membership composition can have a significant impact on the cost. It is noted that there is a high degree of variation across the membership across LGPS Funds.

Monitoring investment performance

176. There is an annual review of investment performance in June for each of the Funds. The report provides a detailed analysis of each of the Fund's investment performance against its investment strategy. We concluded that Pension Committee and Board Members are engaged in monitoring the performance of investments.
177. In addition to monitoring at a Committee level the Funds' performance is calculated by an external provider on a monthly basis. The external provider compiles information covering monthly, quarterly, yearly, 3, 5, 10 since inception yearly performance measures. This information is presented to the Joint Investment Strategy Panel to allow for scrutiny investment performance of the Funds.

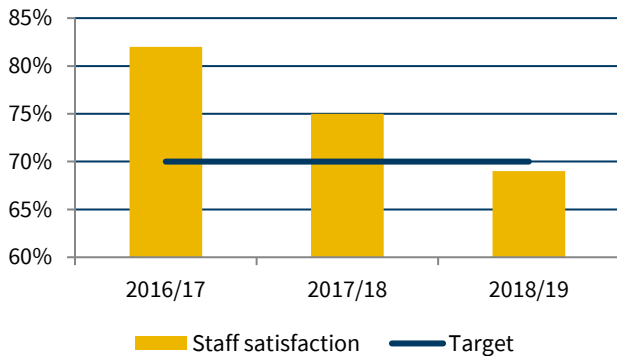
Administrative Performance

178. The Funds' have a Service Plan in place covering the period 2018- 2020. The Pensions Committee receive updates on the service plan at each meeting. The annual results for 2018/19 are presented in the Funds' Management Commentary.
179. The Performance Report highlights that the Funds are meeting the majority of their targets (90%) with only 1 area where performance was not in line with target levels:



180. The target for the staff engagement index was 70% but the Funds achieved a level of 69%. The funds recognise the importance of the workforce in achieving objectives and conduct an annual staff survey to monitor engagement.

Exhibit 13: Lothian Pension Funds' Financial Position



Source: Lothian Pension Funds unaudited annual report and accounts

181. The Funds have reported a decline over recent years and in 2018/19 they are below target.

Tendering for Services

182. The Funds make use of a range of service providers including investment managers, an actuary and a custodian. In order to ensure the Funds are achieving value for money it is good practice to tender for services at set intervals.
183. The Funds follow the City of Edinburgh Council procurement procedures and maintain a contract register.
184. A paper went to the Pensions Committee in December 2018 providing an update on the tender of custodian services.
185. We have concluded that contract arrangements in place at the Funds are appropriate.



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8. Appendices



Appendix 1: Respective responsibilities of the Funds and the Auditor

Responsibility for the preparation of the annual report and accounts

It is the responsibility of the Pensions Committee and the Chief Finance Officer, as Accountable Officer, to prepare financial statements in accordance with the Local Government (Scotland) Act 1973 and directions made thereunder.

In preparing the annual report and accounts, the Pensions Committee and the Chief Finance Officer, as Accountable Officer are required to:

- apply on a consistent basis the accounting policies and standards;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards as set out in the Code of Practice on Local Authority Accounting (the Code) have not been followed where the effect of the departure is material;
- prepare the accounts on a going concern basis unless it is inappropriate to presume that the Lothian Pension Fund will continue to operate.

The Chief Finance Officer is also responsible for

- keeping proper accounting records which are up to date; and
- taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditor responsibilities

We audit the annual report and accounts and give an opinion on whether:

- give a true and fair view, in accordance with applicable law and the Code, of the state of the affairs of the Funds as at 31 March 2018 and of the income and expenditure of the Council and its group for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the Code;
- they have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Authority Accounts (Scotland) Regulations 2014 and the Local Government in Scotland Act 2003;
- the information given in the Management Commentary is consistent with the annual report and financial statements.

We are also required to report, if in our opinion:

- adequate accounting records have not been kept; or
- the annual accounts and the part of the Remuneration and Staff Report to be audited are not in agreement with accounting records; or
- we have not received all the information and explanations we require for our audit; or
- There has been a failure to achieve a prescribed financial objective.

Wider scope of audit

The special accountabilities that attach to the conduct of public business, and the use of public money, mean that public sector audits must be planned and undertaken from a wider perspective than in the private sector. This means providing assurance, not only on the financial statements, but providing audit judgements and conclusions on the appropriateness, effectiveness and impact of corporate governance and performance management arrangements and financial sustainability.

The Code of Audit Practice frames a significant part of our wider scope responsibilities in terms of four audit dimensions: financial sustainability; financial management; governance and transparency; and value for money.



Independence

International Standard on Auditing (UK) 260 "Communication with those charged with governance" requires us to communicate on a timely basis all facts and matters that may have a bearing on our independence.

Non-audit services

In addition to our work on the Funds we are also responsible for the audit of the financial statements of LPFE Ltd and LPFI Ltd, the subsidiaries of Lothian Pension Fund. In addition to the audit of the subsidiaries, Scott-Moncrieff provides accounts preparation, corporation tax services and ad hoc VAT advice to both LPFE Ltd and LPFI Ltd.

All tax services are provided by an independent tax partner and staff who have no involvement in the audit of the financial statements.

The accounts are prepared from trial balances provided by LPFE Ltd and LPFI Ltd and no significant policies, disclosures, adjustments or estimates are decided by Scott-Moncrieff.

In 2018/19 Scott-Moncrieff undertook a review of pay arrangements at the request of LPFE Ltd. This review was undertaken by a team independent of the external audit team and who have no involvement in the audit of the financial statements.

Confirmation of independence

We confirm that we have complied with the FRC's Revised Ethical Standard (June 2016).

In our professional judgement, the audit process is independent and our objectivity has not been compromised in any way. In particular there are and have been no relationships between Scott-Moncrieff and the Funds, its Board members and senior management that may reasonably be thought to bear on our objectivity and independence.



Appendix 2: Action plan

Our action plan details the weaknesses and opportunities for improvement that we have identified during our audit.

Action plan grading structure

To assist the Funds in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been rated.

The rating structure is summarised as follows:

| Grade | Explanation |
|----------------|-----------------------------------------------------------------------------------|
| Grade 5 | Very high risk exposure - Major concerns requiring immediate attention. |
| Grade 4 | High risk exposure - Material observations requiring management attention. |
| Grade 3 | Moderate risk exposure - Significant observations requiring management attention. |
| Grade 2 | Limited risk exposure - Minor observations requiring management attention. |
| Grade 1 | Efficiency / housekeeping point. |



Current year action plan

| Action plan point | Issue & recommendation | Management comments |
|-------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>1. Accuracy of forecasting information</p> <p>Rating</p> <p>Grade 3</p> <p>Paragraph Ref</p> <p>110</p> | <p>Issue In year service update reports highlighted that a net withdrawals position was expected, however, the forecasts were significantly above the year-end position with December being 118% higher than the actual position.</p> <p>Risk There is a risk that the year-end position is significantly different to the forecast position with an adverse variance.</p> <p>Recommendation We recommend the Funds takes action to improve the quality of forecasting information presented to the Pensions Committee.</p> | <p>It should be noted that the cashflow forecasts reported to Pensions Committee as part of the regular "Service Plan update" are prepared on a strict cash basis. This differs from the year end reporting which reflects accrual of both expenditure and income.</p> <p>This clarification is highlighted in the narrative of the regular reporting to Pensions Committee.</p> <p>Relevant extract from the meeting of 26 September 2018 is -</p> <p>Membership and Cashflow monitoring</p> <p>a. The tables below detail the cashflows as at the end of July 2018 and projections for the financial year. These have been prepared on a cashflow basis (compared to the accruals basis of the year-end financial statements and budget projections).</p> <p>In future the financial statements will disclose reconciliation to the cash accounting basis together with explanatory narrative for any significant variances.</p> <p>Responsible officer: Chief Finance Officer, Lothian Pension Fund</p> <p>Implementation date: 31 May 2020</p> |



| Action plan point | Issue & recommendation | Management comments |
|----------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>2. Registers of interest</p> <p>Rating</p> <p>Grade 3</p> <p>Paragraph Ref</p> <p>117</p> | <p>Issue A compliance email has not been issued to the Pensions Board/Non-Elected Committee Members during 2018/19. This email should be sent on a quarterly basis, however, the last email was sent in March 2017.</p> <p>Risk There is a that the Funds do not hold an up to date register of interests for all the Pensions Board/Non-Elected Committee Members, and is therefore unable to identify any potential related party transactions.</p> <p>Recommendation We recommend that compliance e-mails are issued in line with the stated policy.</p> | <p>Pension Board and non-elected members are required to sign a Code of Conduct, as well as making declarations to the Funds dual interest and hospitality register. The last item on the dual interest register was declared in September 2018.</p> <p>At Pension Board meetings, declaration of interest is a standing agenda item. Should there be no declarations of interest, this is recorded in the minutes.</p> <p>The Fund has been undertaking a governance review over the last few months which includes a review of the code of conduct for Pension Board and Non-elected Committee members. If the Committee approves the new Code of Conduct in September 2019, all Committee members and Board members will be required to sign the new Code of Conduct (this includes Councillors). Thereafter, an annual refresh will be required.</p> <p>Although the Fund does consider the risk to be low, it does acknowledge that compliance emails have not been sent to Pensions Board and Committee members (non-Councillors) during the financial year. To strengthen policies and procedures as well as raise the profile of compliance further, quarterly e-updates to Pension Board and Pension Committee members from September onwards will now include a compliance reminder section.</p> <p>Responsible officer: Chief Risk Officer, Lothian Pension Fund</p> <p>Implementation date: 31 October 2019</p> |

| Action plan point | Issue & recommendation | Management comments |
|-------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>3. Review of bank reconciliations</p> <p>Rating</p> <p>Grade 3</p> <p>Paragraph Ref</p> <p>117</p> | <p>Issue As part of our testing of bank reconciliations we sample checked the controls in place across the year. We noted that for one sampled month the bank reconciliation had been completed but had not been reviewed by a senior member of the finance team.</p> <p>Risk There is a risk that there is an error in the bank reconciliation which is not detected.</p> <p>Recommendation We recommend that all bank reconciliations are subject to review by an appropriate individual.</p> | <p>Change in bank account reconciliation process took place during the year to become paperless. Month -end reconciliations are completed by the Finance team and then e-mailed to Finance management to review. Reconciliations have been reviewed. The recording (sign-off) of this validation, however, has not taken place. Procedure will be reviewed to better capture and record electronic approvals.</p> <p>Responsible officer: Chief Finance Officer, Lothian Pension Fund</p> <p>Implementation date: 31 October 2019</p> |



| Action plan point | Issue & recommendation | Management comments |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p data-bbox="129 257 413 360">4. Verification of pensioner details</p> <p data-bbox="129 367 413 427">Rating</p> <p data-bbox="129 479 413 539">Grade 3</p> <p data-bbox="129 591 413 651">Paragraph Ref</p> <p data-bbox="129 658 413 714">117</p> | <p data-bbox="475 250 956 409">Issue As part of our verification of controls we walked through a transfer out of a member. The sampled record did not have their date of birth confirmed or checked to supporting documentation.</p> <p data-bbox="475 439 956 539">Risk This is a key control in confirming pension eligibility and could lead to an error in payments made.</p> <p data-bbox="475 568 956 680">Recommendation We recommend that verification of key details are conducted in line with the stated procedures.</p> | <p data-bbox="986 250 1449 432">This case is an interfund transfer rather than a transfer to another pension scheme. An interfund transfer means that the member is transferring to the same scheme (LGPS) and the transfer value payment is simply a way of transferring the liability from one Fund to another.</p> <p data-bbox="986 479 1449 607">There is an agreement between the Scottish Funds that dates of birth do not need to be verified if already verified by one scheme. In this case, however, this did not happen in either fund.</p> <p data-bbox="986 618 1449 831">The existing documented LPF administration procedure already reflected requisite date of birth verification. In this case, the procedure had not been correctly followed (human error). The importance of the check has been re-iterated to the pensions administration team, both orally and by e-mail communication.</p> <p data-bbox="986 875 1449 931">Responsible officer: Chief Finance Officer, Lothian Pension Fund</p> <p data-bbox="986 965 1449 1021">Implementation date: 30 September 2019</p> |



Follow up of prior year recommendations

Of the four recommendations raised within our 2016/17 and 2017/18 interim audit reports and 2016/17 and 2017/18 annual audit reports, we note that one has been closed and three are ongoing. Details are given below.

1. Publication of the financial statements

| Initial rating | Issue & recommendation | Management comments |
|----------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Grade 2 | <p>Observation</p> <p>In 2017/18 Lothian Pension Fund received objections to the accounts relating to the public right to inspect the accounts. The objections related to the wording in the public inspection notice and the availability of the annual report and financial statements on the Lothian Pension Fund website.</p> <p>Recommendation</p> <p>We recommend that the annual report and financial statements are posted on the Lothian Pension Fund website, following approval from the Pensions Committee and in line with the public inspection notice.</p> | <p>Recommendation is accepted. Following consideration of the Annual Report 2019 (and Financial Statements) Unaudited by Pensions Committee, this will be posted on the Lothian Pension Fund website, supplementing the prior disclosure of all the reports to that Committee on the Council's website.</p> <p>Responsible officer: Chief Executive Officer, Lothian Pension Fund</p> <p>Implementation date: June 2019</p> |

| Current status | Audit Update | Management response |
|----------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Ongoing | <p>In 2018/19 we received an objection to the notice of the public right to inspect. Upon review there was found to be a delay in publishing the public inspection notice which is required to be published prior to 17 June as outlined by the 2014 Regulations. The notice was published in the local newspaper and on the City of Edinburgh Council website by 17 June 2019, however, was not available at Council offices until 26 June 2019.</p> <p>We recommend procedures are put in place to ensure all the regulations are complied with in 2019/20.</p> | <p>While detailed procedure notes are already in place, these will be reviewed to introduce an element of independent review, thereby ensuring all key steps are undertaken by the required dates.</p> |



2. Bank accounts

| Initial rating | Issue & recommendation | Management comments |
|----------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Grade 3 | <p>Observation</p> <p>The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010. require administering authorities to hold a separate bank account for funds and to be used to hold pension fund money.</p> <p>There is an ongoing issue that although the Funds' held their own bank accounts, monies were transferred to the City of Edinburgh Council holding account and the money was managed through this account. Actions were taken in 2017/18 to progress the issue of compliance, however, significant delays mean that during the year the Funds were not in fully compliant with the regulations.</p> <p>Recommendation</p> <p>We recommend the Funds put arrangements in place to ensure compliance with the regulations.</p> | <p>Quotation for a stand-alone ledger for the Funds was also sought from CGI, the Council's ICT provider, but this did not offer a cost-effective solution. Whilst LPF now fully anticipates a successful project delivery by the Council and CGI, with integration of the LPF requirement in the ledger specification, the option of complete separation, i.e. LPF to procure an alternative to the Council solution, is retained as "last resort".</p> <p>Responsible officer: Chief Finance Officer, Lothian Pension Fund</p> <p>Implementation date: As soon as possible, subject to the implementation of a revised financial ledger system by the Council to incorporate this functionality, or alternatively a separate procurement by LPF.</p> |

| Current status | Audit Update | Management response |
|----------------|------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Ongoing | <p>The resolution of this issue is linked to the procurement of a new ledger system which has not progressed in 2018/19.</p> | <p>LPF has requested that responsibility for "unfunded (discretionary) payments" be transferred to Scottish Public Pensions Agency (SPPA). Should this be accepted by SPPA, then there would be no requirement for LPF to utilise the Council's bank account.</p> <p>The procurement of a new ledger is also linked to LPF's consideration of its broader ICT service requirements.</p> |

3. User access controls

| Initial rating | Issue & recommendation | Management comments |
|----------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Grade 3 | <p>Observation</p> <p>Our review of the journals environment identified that all City of Edinburgh Council staff with access to Oracle, the financial ledger system, have the ability to post to the Funds' financial ledgers.</p> <p>Recommendation</p> <p>While our audit review in respect of the 2017/18 financial year did not identify any indications of user access being manipulated, we recommend that the Funds' officers in conjunction with City of Edinburgh Council</p> | <p>Recommendation is accepted.</p> <p>Responsible officer: Chief Finance Officer, Lothian Pension Fund</p> <p>Implementation date: March 2019</p> |



review user access controls for the financial ledger.

| Current status | Audit Update | Management response |
|----------------|------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Ongoing | This is an ongoing issue in 2018/19, however, we did not identify any instances where journals were posted by inappropriate users. | There remains no existing system-based means of preventing staff from posting journal entries affecting other organisations. Indications received suggest that the cost of introducing such controls would be prohibitive relative to the resulting benefits. The posting of journal entries exists, however, within a wider framework of financial analysis, peer review and reporting. Any cost-effective means of effecting further improvements in this area will be considered as part of the Council's Oracle system refresh due for implementation in mid-2020. |

4. Cyber essentials

| Initial rating | Issue & recommendation | Management comments |
|----------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Grade 3 | <p>Observation</p> <p>In 2017/18 In May 2017, a number of health boards across NHS Scotland were affected by the Wannacry global ransomware attack. In response to this the Scottish Government launched 'A Cyber Resilience Strategy for Scotland: Public Sector Action Plan, 2017/18'.</p> <p>The action plan outlines a number of requirements that public bodies should be taking forward. This includes an action for public bodies to achieve a Cyber Essentials Plus certification by the end of October 2018. The Funds are aware of the work but do not have a formal plan to achieve certification.</p> <p>Recommendation</p> <p>We recommend that the Funds make arrangements to ensure Cyber Essentials certification is achieved by 31 October 2018.</p> | <p>Recommendation is accepted. LPF is liaising with the Council's Chief Information Officer to secure requisite certification.</p> <p>Responsible officer: Chief Executive Officer, Lothian Pension Fund</p> <p>Implementation date: October 2018</p> |

| Current status | Audit Update | Management response |
|----------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|
| Completed | Our audit testing in 2018/19 confirmed that Cyber Essentials accreditation was not achieved by the October deadline and however, the Cyber Essentials Certification was achieved in 2018/19 by City of Edinburgh Council and the Funds.. | Not applicable |



Appendix 3: Unadjusted audit differences

We identified the following adjustment to the financial statements during our audit. We have discussed this with management and have agreed that it will not be reflected in the financial statements on the grounds of materiality.

| Adjusted difference | SoCNE | | Balance Sheet | |
|---------------------------------------------------------------------------------|---------------|----------|---------------|----------|
| | DR £m | CR £m | DR £m | CR £m |
| Past Service Cost | | 0.252 | | |
| Net interest cost | | 0.003 | | |
| Return on assets (excluding net interest) | | 0.027 | | |
| Pension liability | | | | 0.282 |
| <i>Being updated pension liability after the impact of the McCloud judgment</i> | | | | |
| Net impact on income / expenditure | £0.282 | | | |



Audited Annual Report and Accounts 2018/19





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Foreword

Report by the Convener of the Pensions Committee



I am delighted to present the Annual Report and Accounts for the Lothian Pension Fund and Scottish Homes Pension Fund for 2018/19.

During the year, a decision was taken to merge Lothian Buses Pension Fund with the Lothian Pension Fund by the Pensions Committee in March 2018. Following completion of a revised admission agreement and shareholders' guarantees, the merger took place on 1 February 2019. The merger puts in place an employer guarantee and, facilitated by the new employer asset tracking system, will see the creation of a bespoke investment strategy for Lothian Buses within the Lothian Pension Fund. This means that there will not be separate accounts or a valuation from this date. The change will not affect member benefits and is expected to result in more efficiencies leading to lower costs.

Within the wider Scottish Local Government Pension Scheme, the Scheme Advisory Board in Scotland initiated a consultation on the future structure of the LGPS in June 2018. The review will determine if the current 11 fund structure best serves the members and employers.

The consultation identified four options for consideration including retaining the current structure, greater co-operation between funds, pooling investments only and full merger into one or more new funds.

The Fund's preferred option would be to work with like-minded partners on a voluntary basis to develop a mutually beneficial merger solution. The Fund has made significant inroads in its collaboration via its FCA authorised company with two other LGPS funds. Partner funds are benefiting from Lothian's internal resource and we are sharing our costs. However, there has not yet been any significant impact on any of Lothian's investments. The arrangements are expected to evolve and for Lothian to benefit from greater overlap in investments. The governance of Lothian's collaborative arrangements is not straightforward. While other funds rely on advice from Lothian, they need to continue to be resourced appropriately to make decisions for their respective funds. Further, there are practical constraints to the expansion of this type of collaboration.

Finally, during the year Clare Scott stepped down after 13 years with the Fund, the last 6 years as Chief Executive Officer. I would like to record my personal thanks and those of the Pensions Committee and Board for leading the transformation of the Fund during her time with the Fund. Doug Heron joined as the new Chief Executive Officer in February of this year. I am delighted Doug has joined us and I believe he is ideally qualified to continue the successful delivery of the Lothian Pension Fund's work and look forward to working with him.

**Councillor Alasdair Rankin
Convener, Pensions Committee**



Report by the Convener of the Pensions Audit Sub-Committee



The function of the Pensions Audit Sub-Committee is to monitor the operation of the Fund's internal controls, governance, risk and compliance

arrangements and financial reporting.

The Sub-Committee formally met three times during the year. The key activities undertaken in 2018-19 included considering the Annual Report and Accounts and both the internal and external audit reports. Other highlights have covered risk assurance, fraud prevention, tax recovery on investment income and investment custodian services.

I believe the Audit Sub-Committee plays a valuable role in the governance of the pension funds and adds value to members and employers.

Councillor Cameron Rose Convener, Audit Sub-Committee

Report by the Chair of the Pension Board



The Pension Board, whilst not a directly decision-making body, holds an important scrutiny function and its role is in ensuring the Fund compliance with the Scheme's rules and other pensions regulations;

Including those set out by The Pensions Regulator which relate to the running of the Lothian Pension Fund, thereby ensuring both its effective and efficient governance and administration.

Its members are drawn equally from across the Fund's employers and members and is made up of five employer and five member representatives who meet in session before all quarterly Pension Committee meetings, which they also attend.

Each of the members appointed to the Board is required to undertake extensive training each year in order to ensure their continuing development and understanding of their role, and the management and the various operations of the Fund.

During the preceding 12 months the Board has once again dealt with a wide range of matters, including changes to its own constituent membership. Despite these unexpected personnel changes, the Board has continued to diligently fulfil all of its responsibilities.

I would therefore take this opportunity to offer my personal thanks to all those Board Members that have been involved with, and supported, the Board and its work during this past year.

Earlier in the year the Scottish Government, via the Scottish Scheme Advisory Board, instigated a major review of the 'Effectiveness of the Governance' arrangements for all 11 Local Government Pension Funds across Scotland. The Board has been involved in shaping the Fund's response to this important document taking part in a number of sessions to discuss the options the Fund felt would ultimately ensure the best long-term future for members and employers.



The Board also continued to maintain an active interest in relation to the governance of the Fund's Investment Strategy and its considerations of the various Environmental, Social and Governance issues being brought to its attention.

This year the Board was (for the first time) actively involved in supporting the Fund's selection process relating to the appointment of its new Independent Professional Observer (IPO). This is an important external role in supporting the Pensions Committee and Board.

Having been in existence since 2015 the Board members also considered its 'Constitution' and in particular the required 'annual rotation' of the position of Chair. It was generally felt (and subsequently unanimously agreed) that this arrangement did not give the Chair sufficient time in relation to both the understanding and duties of the role. The Board therefore (with the Pension Committee's subsequent agreement) opted to implement a change to its Constitution.

Therefore from 2019/20 the Chair will have (subject to certain caveats) the ability to undertake a further subsequent year in the role. This change will now see the position rotate every two years instead of annually and in accordance with this new rule, I will now be continuing as Board Chair until March 2020.

I look forward to once again working on your behalf and with all of the Members of the Board for a further year.

Jim Anderson
Union representative and Chair of the Pension Board

Report by the Independent Professional Observer

I was appointed as the Fund's independent professional observer in August 2018. My role helps strengthen Fund governance by providing the Pensions Committee and Pension Board with independent advice and impartial knowledge independently from the Fund officers.



I have more than 30 years of pension experience working with pension trustees and sponsors on a wide range of investment, actuarial and governance issues.

In my first term as observer I have held surgeries to assist the Pensions Committee and Pension Board to provide oversight of the pension funds. Topics such as funding, investment and collaboration have been considered in addition to the normal business of funds.

Andy McKinnell
Independent Professional Observer



Management commentary

Introduction

During the year we welcomed 4,379 new members to the Fund and supported 1,506 new retirements. We made 384,490 pension payments totalling more than £231 million to 30,623 members to support their lives in retirement. We scored 92.7% for member satisfaction. At Lothian Pension Fund we have a member-first mindset and we're proud to be the Local Government Pension Scheme for 84,317 public sector workers, former workers, or their beneficiaries, across Scotland.

Change in structure

During the year, and as stated in the Introduction from the Convener, the Committee approved the merger of the Lothian Buses Pension Fund with the Lothian Pension Fund and I am pleased to report that this was completed earlier this year and the path is set for us to realise a range of operational efficiencies and reductions in overheads.

Within the Lothian Pension Fund, we operate a unitised, or segmented, structure for assets and liabilities which allows us to monitor and manage assets and liabilities according to the sponsoring employer of the member. This allows us to develop and operate appropriate investment strategies and to ensure employers pay contributions aligned to the costs of benefit entitlement for their members.

As a result, Lothian Buses, like any other sponsoring employer in our Fund, pays only the costs of their

OUR MISSION

To provide a sustainable and valued saving solution for public sector employees and their employers.

members but now shares the benefit of lower administration costs from the merged Fund.

Funding Levels

The 2017 triennial valuation was completed in the previous financial year and reflected for Lothian Pension Fund, a funding level increase from 91% at 31 March 2014 to 98% at 31 March 2017.

For Lothian Buses Pension Fund, the funding level on the ongoing basis rose from 117% in 2014 to 121% at 31 March 2017, showing a surplus of £84million.

The funding level for Scottish Homes Pension Fund at 31 March 2017 was 104.7%, increased from 88.8% from the 2014 actuarial valuation.

The next valuation is expected to be undertaken at 31 March 2020. At the time of writing we expect a move to quadrennial, or four-yearly, valuations creating in effect a longer period between valuation points.

In practice this is not expected to result in any added volatility for funding levels across the longer period, with contribution stability mechanisms expected to continue to result in certainty of costs for employers across budget cycles.



Affordability of scheme membership

During the year we were pleased to work with a number of smaller sponsoring employers to facilitate their orderly exit from active scheme membership, allowing those employers to limit the extent of future balance sheet risk. The financial benefits of scheme membership to employees are significant and increasingly costly as economic conditions and longevity factors combine to sustain the pressure on contribution rates. Where employers, primarily community admitted bodies, have affordability concerns or wish to limit their balance sheet risk we seek to agree payment and investment strategy outcomes that achieve our shared goal of sustainable and secure benefits for members.

Our people

The team at LPF now number 68 performing functions of benefit administration and investment management, supported by functions which include member communications, legal, risk, compliance, finance and HR. The team are employees of LPFE limited, an arms-length external organisation of the administering authority, City of Edinburgh Council. LPFE operates under a company board with an independent non-executive member.

During the year we had a change in Chief Executive Officer with Clare Scott moving on in December 2018 and Doug Heron succeeding her in early 2019. During her 13 years with the Fund Clare was instrumental in developing the team and the operations that support our members. We would also like to recognise her contribution to the developments at national level through her role as an advisor to the Scheme Advisory Board (SAB).

The Fund is unique in SLGPS in holding FCA authorisation and employing professionals who manage investments primarily in-house instead of through more costly external asset manager appointments. Our total complement for such roles in our organisational structure grew in the year to 15.

The team therefore requires a matching of skills and experience similar to roles in the private sector and we recognise we must compete with financial services firms to attract and retain colleagues. We are only able to do so with progressive remuneration policies and during the prior year this included taking steps towards offering a variable remuneration component for eligible employees including senior management and our investment management colleagues.

This allows us to more ably retain and attract the specialist skills and experience we need to operate the in-house investment management model that we believe drives a significant reduction in our operating costs and better aligns our investment strategy with pension fund liability profiles. Such arrangements are uncommon in public sector pension funds and there may be member and public interest in the value they create. As a result of such expected interest and our commitment to transparency we have increased the level of disclosure in the remuneration section of this report.

Scottish LGPS (SLGPS) consultation

In the last year, under the direction of the Cabinet Secretary, the Scheme Advisory Board (SAB) undertook a consultation on the prospect of structural reform for the 11 individual funds that comprise the Scottish Local Government Pension



Scheme (SLGPS). Lothian Pension Fund, second largest to Strathclyde, responded in favour of structural reform, specifically the creation of conditions in which like-minded schemes could seek to merge. We await the outcome of the review but recognise there is potential for significant change in the way that assets are managed, and member benefits are administered for the more than 545,000 members of SLGPS.

Notwithstanding the prospect of structural change, we remain active, through our FCA-authorized legal entity, in enabling other funds to achieve their investment goals. This extends to our formal investment advisory partnerships with the pension funds for Falkirk and Fife, our club deal investment partnership with a further two funds, but also to our willingness to provide resource and capital to support operational, administration, commercial and technology related developments for the benefit of all of Lothian Pension Fund and the wider SLGPS.

Economic and investment market developments

With Brexit and developments in international trade markets, political and economic uncertainty have been themes for all defined benefit pension funds over the year. Lothian Pension Fund has for some time held a bias towards lower volatility strategies and during the year, undertook a detailed investment strategy review involving external advisers to best position the Fund for the uncertainty ahead.

Overall returns for our investments are reported in the Investments section of this report.

Interaction with regulators

We were pleased to be selected to be a member of the LGPS cohort review carried out by The Pensions Regulator (TPR) in the prior year. This interaction, made possible by TPR assuming responsibility for LGPS regulation in 2013, extended to a series of thematic reviews across a range of governance and administration aspects of our operations.

TPR expect to report on their findings from the cohort at aggregate level and we look forward to working with TPR as they develop policies and principles in support of better outcomes for LGPS stakeholders.

Future developments

The prospect of structural reform within SLGPS remains the most significant possible development to affect Lothian Pension Fund and we stand ready to work with the Scottish Advisory Board and policy-makers to ensure any change results in material benefit for the primary stakeholders of the LGPS, the members and their sponsoring employers. Aside from reform, the year ahead will see the team undertake significant member-first projects as we look to improve our technology and invest in the capability of our people, delivering more for members as a result.



DR STEPHEN S MOIR
Executive Director of
Resources
The City of Edinburgh Council
26 June 2019



DOUG HERON
Chief Executive Officer
Lothian Pension Fund
26 June 2019



Governance and Risk

The City of Edinburgh Council is the administering authority for the Scottish Local Government Pension Scheme (LGPS) in the Lothian area. The Council administers the benefits and invests the assets of two LGPS funds, Lothian Pension Fund and Scottish Homes Pension Fund. In this report we refer to these as the Fund.

Lothian Pension Fund is the second largest LGPS fund in Scotland with assets of £7.8 billion, 83 employers with active members and over 84,000 members. The Scottish Homes Pension Fund investments amount to £0.16 billion with 1,550 members.

Lothian Buses Pension Fund was merged with Lothian Pension Fund on 1 February 2019, changing the way in which the Fund is administered. At the time of merger, Lothian Buses Pension Fund had assets of £0.5bn and 3,700 members. Under the new arrangements, it retains a separate investment strategy.

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 Fund, Statement of Investment Principles, Funding Strategy Statement and Pensions Administration Strategy and Pensions Discretions Policy.

The Pensions Committee and Pensions Audit Sub-Committee

The day-to-day running of the Fund is delegated to a specialist team who undertake pension administration, accounting and investment

functions, managing the majority of the Fund's assets internally.

All pension matters are delegated to the Pensions Committee of the Council, supported by the Audit Sub Committee, and its members act as 'quasi trustees'. The Pensions Committee held four meetings and the Audit Sub Committee held three meetings during the year.

The table shows the Committee members for the year 2018/19.

| From 1 April 2018 to 31 March 2019 |
|------------------------------------------------------------|
| Pensions Committee |
| Councillor Alasdair Rankin (Convener) |
| Councillor Maureen Child |
| Councillor Neil Ross |
| Councillor Claire Miller |
| Councillor Cameron Rose |
| John Anzani (Member representative) |
| Richard Lamont (Employer representative, VisitScotland) |
| Pensions Audit Sub-Committee |
| Councillor Cameron Rose (Convener) |
| Councillor Maureen Child |
| John Anzani (Member representative) |

The Pension Board

The Pension Board was set up on the 1 April 2015 as a result of the Public Services Pensions Act 2013 and the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014.

The role of the Pension Board is to help ensure that the operation of the Funds is in accordance with the applicable law and Regulations.



The Board attends all Pensions Committee meetings and two representatives also attend the Pensions Audit Sub-Committee meetings.

The membership comprises of ten members, five representatives appointed from the employer bodies and five representatives appointed by trade unions for the membership of the Fund. The Pension Board membership for 2018/19 is shown in the table. There were two vacancies as of 31 March 2019.

| Member representatives | |
|--------------------------|----------------------------------------------------------------|
| Jim Anderson | Unison (Chair) |
| Thomas Carr Pollock | GMB |
| Brian Robertson | Unite |
| Thomas Howorth | Unison (appointed 24/9/18) |
| Diane Hogarth | Unite (resigned 18/6/18) |
| Tony Pearson | Unite (appointed 24/9/18) (resigned 25/3/19) |
| Employer representatives | |
| Sharon Cowle | Scottish Legal Complaints Commission (appointed 24/9/18) |
| Darren May | Scottish Water |
| Sharon Dalli | Police Scotland |
| Alan Williamson | Edinburgh College |
| Paul Ritchie | East Lothian Council (resigned 11/10/18) |
| Eric Adair | EDI Group (resigned 25/4/18) |

Pensions Committee and Pension Board training

The Committee and Board members must attend no less than 21 hours of training per year as outlined in the Fund's training policy which is available on our website at www.lpf.org.uk.

All new members of the Pensions Committee and Pension Board attend induction training. Other training provided internally covered topics including governance, guaranteed minimum pensions, responsible investment and investment strategy.

Committee and Board representatives also attended external conferences including the Pensions and Lifetime Savings Association Local Authority Investment Conference 2018 and the 2018 Local Authority Pension Fund Forum Annual conference.

All members of the Pension Committee and all Pension Board members achieved the required training hours during 2018/19. Pensions Committee members collectively attended 313 hours of training over the year and members of the Pension Board undertook 324 training hours.

Joint Investment Strategy Panel

Investment strategy guidance to the Committee is provided by a Joint Investment Strategy Panel (JISP), working in collaboration with the Falkirk Council and Fife Council pension funds. The JISP meets quarterly and includes senior officers and external investment advisers (currently Scott Jamieson and Gordon Bagot).

The Pensions Committee of each pension fund agrees their own investment strategy but delegates the implementation of strategy, including selection of investment managers, to officers.

The JISP advises the three pension fund administrating authorities on implementation of their respective investment strategies.



The assets of Lothian Pension Fund, Falkirk Council Pension Fund and Fife Council Pension Fund remain separate.

Lothian Pension Fund employees

The team is employed by an arms-length company, LPFE Limited (LPFE), which is wholly owned by the Council (in its capacity as administering authority for the Fund) and it is supervised by a board of directors chaired by the Council's Executive Director of Resources and includes the Convener of the Pensions Committee. The team is required to carry out certain activities for the Fund through its Financial Conduct Authority authorised vehicle, LPFI Limited (LPFI).

LPFI is also wholly owned by the Council (in its capacity as administering authority for the Fund). LPFI is supervised by a board of directors chaired by the Council's Head of Finance. Both the boards of LPFI and LPFE comprise an independent non-executive director (Leslie Robb). All the operations, costs and liabilities in relation to the Fund, including those of LPFE and LPFI, are borne by the Fund.

The day-to-day running of the Fund is carried out by a specialist investment and pensions team. The Fund's functions include investment, pension administration, employer liaison, data quality, customer support, accounting, legal, risk and compliance, communications, and general business support.

The investment responsibilities include carrying out in-house investment management and the monitoring and selection of external investment

managers, as well as external facing collaborative initiatives with other like-minded pension funds.

Over the year, senior officers directly involved in the governance of the Fund from the City of Edinburgh Council were:

Dr Stephen S Moir, Executive Director of Resources,
Hugh Dunn, Head of Finance
Katy Miller, Head of Human Resources

And senior officers from Lothian Pension Fund were:

Doug Heron, Chief Executive Officer from February 2019
Bruce Miller, Chief Investment Officer
Struan Fairbairn, Chief Risk Officer, (Legal, Risk and Compliance)
John Burns, Chief Finance Officer
Clare Scott, Chief Executive Officer to December 2018

Scheme Advisory Board

The Scheme Advisory Board for the Local Government Pension Scheme in Scotland was set up following the Public Service Pensions Act 2013. The Board's main function is to advise Scottish Ministers, when requested, on the desirability of changes to the Scheme. They can also provide advice to scheme managers and pension boards in relation to effective and efficient administration and management of the Scheme in Scotland.



The membership of the Scheme Advisory Board comprises of seven member representatives and seven employer representatives with a Joint Secretary to support each group. During the year, Councillor Rankin was a member and Chair of the Scheme Advisory Board and Fund officers have also advised the Board and Joint Secretaries. There is more information on the Scheme Advisory Board at www.lgpsab.scot.

Risk

An extensive risk register is maintained covering a wide range of issues across investments and benefit operations. The register is subject to internal review each quarter and a summary is reported to the Pensions Committee and Pensions Audit Sub-Committee. On an annual basis the Pensions Audit Sub-Committee reviews the register in full.

Risk Management

The LPF Group is committed to a strong control environment to ensure that risks are identified, understood, managed and monitored appropriately. The risks faced by the LPF Group and the Funds change over time and ongoing management of risk is crucial. The LPF Group also has a compliance policy and each manager is responsible for ensuring compliance within their area of responsibility.

As at 31 March 2019, the most significant risks (after taking account of risk reduction controls), as assessed using a score out of 100 by the Funds' management team, are shown in the table opposite.

Risk Assurance

The Fund operate a bespoke assurance framework designed to ensure they meets their objectives, are adequately resourced, managed to high professional standards, meet legislative requirements and have high customer satisfaction.

| Description | Impact | Likelihood | Risk score |
|--------------------------------------------------------------------------------------------------------------------------|--------|------------|------------|
| Adverse investment performance leading to pressure on employer contributions | 5 | 4 | 20 |
| Adverse movement against non-investment funding assumptions leading to pressure on employer contributions | 5 | 7 | 35 |
| Collapse/restructuring of an employer body leading to pressure on other employers | 4 | 8 | 32 |
| Failure of IT leading to poor ICT responsiveness, legal exposure and cost/risk implications | 8 | 8 | 64 |
| Human Resource within the team not sufficient to carry out core task in conjunction with active or anticipated projects. | 6 | 6 | 36 |



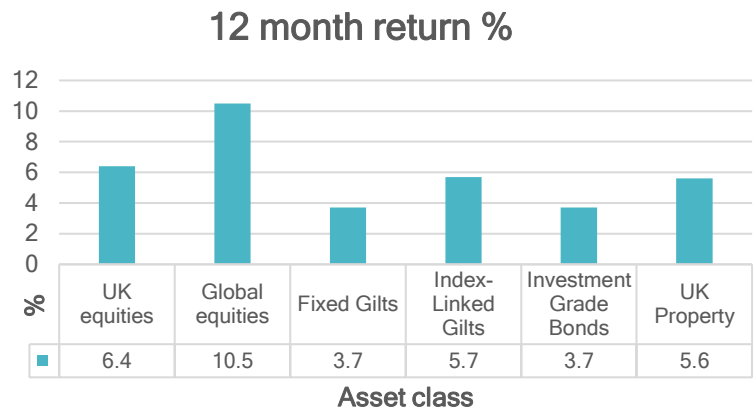
Investment

Investment markets

For the 12 months to 31 March 2019, UK equities (FTSE All Share) returned +6.4%, and global equities (MSCI ACWI, in GBP) returned +10.5%. Global equity returns for sterling-based investors were boosted by the weakness of the pound over the year (global equities returned +5.6% in local currency terms), as investors grappled with the wide range of potential Brexit outcomes. Equities fell sharply in Q4 2018, with markets falling as much as 14% from end September 2018 to their lows in late December, before rallying strongly through the first quarter of 2019.

UK and US government bond yields rose modestly through to September 2018, with the US 10-year bond yield breaching the 3% level for the first time since 2011. However, yields then fell through Q4 2018 as equity markets sold off. Towards the end of December, the US Federal Reserve signalled that the prospect of future rate rises was much less certain than many participants had expected. Bond yields then moved lower through Q1 2019, with US and UK 10-year bond yields ending the year to 31 March 2019 circa 30 basis points (0.3%) lower than they had been 12 months prior. In Europe, the 10-year Bund yield ended the year circa 50 basis points (0.5%) lower as investors sought the safety of German government bonds as economic data showed the internationally sensitive Eurozone slowing. In contrast, Italian bond yields were higher over the year amid heightened concerns over government finances and the domestic political situation.

The table below shows index returns over 12 months to 31 March 2019 for a range of asset classes.



Index: Bloomberg, MSCI UK Property

The OECD’s latest economic outlook (March 2019) includes further downgrades to 2019 GDP projections for the world’s major economies; this follows a previous set of downgrades in its November 2018 update. Dispersion between regions is highlighted, particularly between the US and Eurozone area, alongside the ongoing risk from a potential China growth shock. For the UK, the OECD estimate the economic loss since the 2016 Brexit referendum at between 0.7% and 1.7% of GDP, with continued uncertainty expected to impact negatively until the situation is resolved. Given this backdrop, it is not a surprise that the OECD also expect that “interest rates are set to stay lower for longer”.

The prospect of looser monetary policy has supported support risk assets in the short term and although the outlook for global growth is softer than it was, it remains positive overall. However, economic forecasts have been tilting further in a downward direction. That said, markets are inherently uncertain and a focus on long-term investment strategy remains a prudent approach for long-term investors.



Investment strategies

The investment strategies for the Fund reflects the long-term plans to maintain an acceptable balance between contribution stability and the achievement of positive long-term real returns from the assets owned.

During 2018/19, a review of the investment strategies was undertaken, taking into account the results of the 2017 actuarial valuation. The investment strategy is set at the broad asset class level of Equities, Gilts, Non-Gilt Debt, Real Assets and Cash, which are the key determinants of investment risk and return. Despite an expansion in the number of these 'policy groups' from 3 to 5, the strategic allocation for the whole Fund is broadly similar to the previous allocation, albeit expressed slightly differently.

Lothian Pension Fund

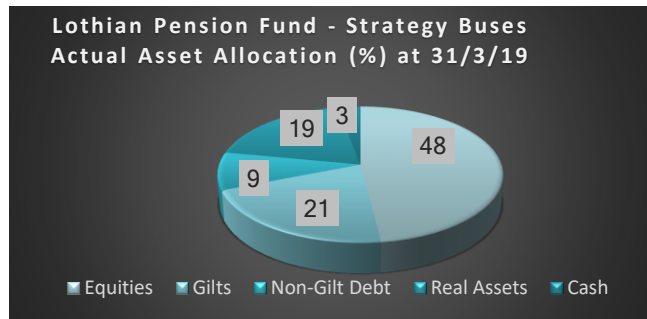
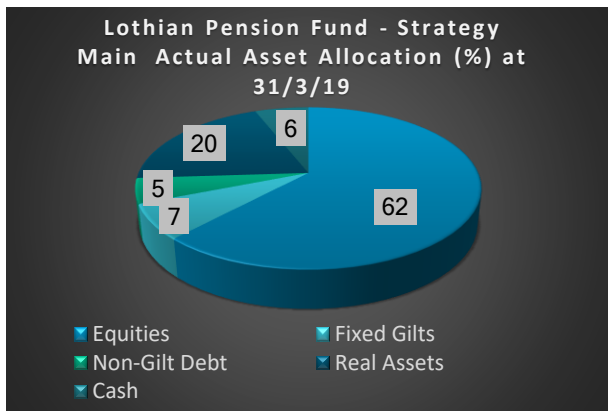
During the course of the year (1 February 2019), Lothian Buses Pension Fund merged into Lothian Pension Fund with a separate, fourth investment strategy specifically created for Lothian Buses within Lothian Pension Fund.

To provide suitable investment strategies for the differing employer requirements, the Fund currently operates four investment strategies. More than 90% of employer liabilities are funded under the Main Strategy, which adopts a long-term investment strategy aiming to maximise the investment return within reasonable and considered risk parameters and hence minimise the cost to the employer.

A small number of employers are funded in the Mature Employers Strategy, which invests in a portfolio of UK index-linked gilts (Mature Employer Gilts - MEG) to reduce funding level and contribution rate risk to a level appropriate to their circumstances. The liabilities funded by Mature Employers Strategy represent less than 1% of total Lothian Pension Fund liabilities.

Just over 1% of liabilities are funded by 50/50 Strategy, which is a 50/50 split of the above two strategies. 50/50 Strategy is for employers who are closed to new members but who do not yet qualify for Mature Employers Strategy.

Lothian Buses now has its own strategy, Strategy Buses, within the Fund with the actual asset allocation shown in the chart below. The liabilities associated with the Lothian Buses strategy represent approximately 7% of Lothian Pension Fund liabilities.



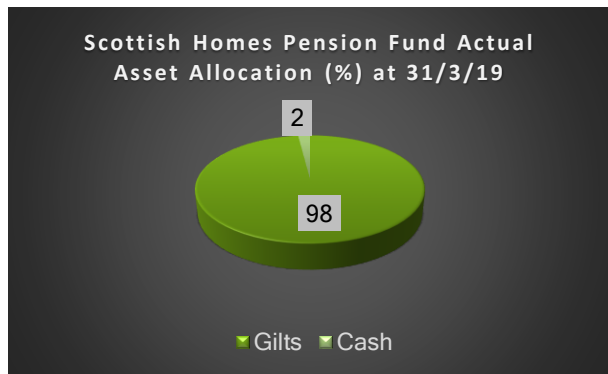


Scottish Homes Pension Fund

The Scottish Homes Pension Fund was invested in index-linked gilts and cash only on 31 March 2018, following the results of the 2017 actuarial valuation which showed that the Fund was 104%+ funded. The gilts were chosen to broadly match the expected liability payments as they fall due.

The analysis focused on the nature of the liabilities, including the proportion that are fixed and index-linked and the timing of expected pension payments. In addition, consideration of the availability of assets to match those payments was undertaken. This resulted in a restructuring of the Fund's bond holdings into both nominal and index-linked UK gilts in early 2019.

By cash flow matching the assets with future liability payments up to one year beyond the next actuarial valuation, which is expected in the March 2020, the Fund has minimised funding level risk.



Internal investment team

Strategies for the Fund are implemented and monitored by an experienced internal team of investment professionals supported by external advisers. Over recent years, the internal team has expanded with very positive effects on costs and capabilities. This is reflected in two structural shifts. Firstly, the percentage of Lothian Pension Fund's listed equity assets managed internally has risen from 23% to 85% and most publicly traded bond assets are also now managed internally. Secondly, the Fund has altered the construction of the listed equity portfolios, increasing the global mandates from 32% to more than 85%.

Despite these large changes in Lothian Pension Fund, performance has been ahead of benchmark over the last five years and this has been achieved with lower risk than the benchmark. The Fund's guiding principle is to use strong internal investment capabilities to their maximum potential and to retain external managers for specialist mandates.



Responsible Investment

The Pensions Committee publicly endorsed and adopted an approach to investing known as Responsible Investment (RI) over a decade ago - in 2008, the Fund became a signatory to the Principles for Responsible Investment (PRI), a United Nations-backed initiative.

This is the cornerstone of the Fund's investment approach, and over the years, the six principles have become increasingly embedded into its investment processes.

- **Principle 1:** We will incorporate ESG issues into investment analysis and decision-making processes.
- **Principle 2:** We will be active owners and incorporate ESG issues into our ownership policies and practices.
- **Principle 3:** We will seek appropriate disclosure on ESG issues by the entities in which we invest.
- **Principle 4:** We will promote acceptance and implementation of the Principles within the investment industry.
- **Principle 5:** We will work together to enhance our effectiveness in implementing the Principles.
- **Principle 6:** We will each report on our activities and progress towards implementing the Principles.

PRI Annual Assessment

All PRI signatories agree to the PRI organisation undertaking a comprehensive annual assessment of their approach to RI. This independent appraisal is made publicly available on our website www.lpf.org.uk with a summary of Lothian's latest evaluation is shown below. It highlights that the Fund's processes and approach to Responsible Investment are rated at or above the median of asset owner signatories across all categories measured.

“Responsible investment is an approach to investing that aims to incorporate environmental, social and governance (ESG) factors into investment decisions, to better manage risk and generate sustainable, long-term returns.”
PRI



PRI rates Lothian's approach to RI highly

Summary Scorecard

| AUM | Module Name | Your Score | Your Score | Median Score |
|------------------------------------------------|--------------------------------------------|------------|------------|--------------|
| | 01. Strategy & Governance | A | | A |
| Indirect - Manager Sel., App. & Mon | | | | |
| <10% | 02. Listed Equity | A | | B |
| <10% | 05. Fixed Income - Corporate Non-Financial | A | | B |
| <10% | 07. Private Equity | A | | B |
| <10% | 08. Property | A | | B |
| 10-50% | 09. Infrastructure | A | | A |
| Direct & Active Ownership Modules | | | | |
| >50% | 10. Listed Equity - Incorporation | B | | B |
| >50% | 11. Listed Equity - Active Ownership | A | | B |

Ethics and Lobbyist Activity

As a public sector asset owner, which strives for high standards of transparency within the constraints of commercial sensitivities, Lothian Pension Fund is subject to considerable scrutiny of its investments. Lobby groups often present ethical arguments for divestment of specific investments. They create adverse publicity to further their campaigns, sometimes being highly selective in their use of facts to raise awareness and to create impact, often with an incomplete understanding of the investments that they oppose.

Campaigners often imply or state that 'Responsible Investment' is synonymous with 'Ethical Investing'.

Lothian Pension Fund is not an 'ethical investor', and nor is it an 'unethical investor'. Rather, it is guided at all times by the legal principle of fiduciary duty and its Principles for Responsible Investment. It recognises that certain investments have the potential to be more contentious than others, but it does not operate a narrow or restrictive policy of excluding investments from its universe of potential investments. What it does do is assess the likely impact of controversial business activities and practices on investment returns by incorporating Environmental, Social and Governance (ESG) considerations into its decision-making processes.

In a world with often complex social, legal or moral issues, it would be impossible to invest efficiently in a manner that meets the expectations of each activist or campaigner. In the past year, special interest groups have demanded divestment of holdings in tobacco producers, defence companies, energy producers and banks.



In contrast to the baseline views of many typical activist representations the Fund does not finance these companies – the Fund is simply a shareholder – and it does not take sides in the moral debate on these investments, but it does recognise that many of the issues raised have the potential to affect financial risk. The information provided by campaigners or other interested groups will always be given due consideration as part of the risk management process and in line with its fiduciary duty to its members and employers. The Fund’s purpose is to ensure that there are sufficient funds to pay pensions to members as they fall due.

Stewardship Code

Another foundation on which the Fund’s Responsible Investment approach is built is the UK Stewardship Code. The premise on which the Code was established is that effective stewardship benefits companies, investors and the economy as a whole. As a large institutional asset owner with voting rights in UK listed companies, Lothian Pension Fund is expected to adhere to the Code on a ‘comply or explain’ basis. The Fund complies. Its close adherence to the Code means that it is classified as a Tier 1 signatory. “To protect and enhance the value that accrues to the ultimate beneficiary, Institutional investors should follow these principles:

- publicly disclose their policy on how they will discharge their stewardship responsibilities.
- have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.
- monitor their investee companies.
- establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.
- be willing to act collectively with other investors where appropriate.
- have a clear policy on voting and disclosure of voting activity.
- report periodically on their stewardship and voting activities.

More information on the Code can be found on the FRC website at www.frc.org.uk.

Voting

As the UK Stewardship Code makes clear, responsible institutional shareholders must exercise their shareholder rights to vote at company annual general meetings (AGMs) and extraordinary general meetings (EGMs). Voting can send a strong message to company management about how it is conducting business.

Lothian Pension Fund votes on the resolutions of 100% of the companies in which it is invested. Two of its external providers are charged with voting on the Fund’s behalf based on pre-agreed policies. Baillie Gifford, who manage assets for Lothian, and Hermes EOS, the Fund’s voting and engagement partner, do this. Their quarterly voting activity is available on Lothian’s website www.lpf.org.uk/invest.

AGMs present asset owners with other way to influence management on important issues. Shareholders can file resolutions which allow all other shareholders to vote on matters that are not raised by management.



During 2018/19, Lothian co-filed a resolution for BP’s AGM in May 2019 calling for greater transparency and disclosure on the company’s approach to carbon emission and low-carbon transition planning. The resolution was backed by BP management and supported by 99.14% of investors. BP has since committed to provide investors with a new strategy consistent with the goals of the Paris Agreement, as well as providing further disclosure on capital expenditure and various company metrics and targets, including annual progress reports

Engagement

There is more to Stewardship and Responsible Investment than voting and filing resolutions. Monitoring and engaging with companies on matters of strategic importance is regarded as a key responsibility of institutional investors, which can improve corporate governance standards and protect shareholder value.

The Fund commits significant resources to engagement activity. Most is undertaken by the Fund’s voting and engagement service provider and partner, Hermes EOS. What Hermes EOS brings to the Fund is a focus on and expertise in engagement activities as well as scale provided by its other like-minded clients. These allow Lothian to use its position as a shareholder more effectively as Hermes EOS engages on behalf of a wide shareholder base and is, therefore, more likely to influence management to enact positive change in investee companies.

Hermes EOS consults with its clients to develop an engagement plan so that it can prioritise engagement activity. The latest plan (available on the Fund’s website) highlights 12 main themes for engagement over the three-year period 2019-21.



In this schematic, these themes surround the core subjects of engagement activity – environment, social issues, governance and strategy, risk and communication.

Each theme is described in detail in the engagement plan, including background information on the importance of each theme, the main outcome objectives, the methodology for tackling each engagement theme and Hermes EOS’s description of best practice in each area.

Lothian stands behind Hermes EOS in achieving progress in each of these areas, and the internal team offers support and ideas where appropriate to Hermes EOS in carrying out this vital work.



Collaboration

Engagement activity is highly suitable for collaborative efforts. It is a complex area that benefits from scale. When Hermes EOS engages with companies, it can speak for asset owners with shareholdings worth up to £390bn. Lothian participates in other collaborative initiatives, which helps it fulfil its commitment to be an active and responsible asset owner:

- **LAPFF**, the Local Authority Pension Fund Forum, is a collaborative shareholder engagement group, comprising 80 UK local authority pension funds and 6 of the LGPS pension fund pools in England & Wales. The Convener of Lothian Pension Fund's Pensions Committee, Councillor Rankin, is on the executive board of LAPFF and has represented LAPFF and its member funds in high level engagement with company management.
- **The Cross-Pool RI Working Group** was one of several working groups formed when the England and Wales pools were being set up to take a leadership role in the process. The RI working group was formed to pioneer best practice in RI and share that across the pools. While Scottish funds are not involved in pooling, Lothian was invited to contribute to the group. Participation in the group has been an invaluable source of knowledge and expertise that allowed Lothian to take a leading position amongst UK asset owners in implementation of RI policy.
- **Diversity Project Scotland**. The Diversity Project is "a cross-company initiative championing a more inclusive culture within the Savings and Investment profession." Lothian Pension Fund has long championed diversity in its investee companies and has committed to diversity in its own ranks. Both investment and human resources staff are participating in this initiative.
- **Climate Action 100+** is a collaborative investor initiative supported by PRI and Hermes EOS. Lothian Pension Fund has recently become a participant member. Signatories to Climate Action 100+ are requesting the boards and senior management of companies to:
 - Implement a strong governance framework which clearly articulates the board's accountability and oversight of climate change risks and opportunities;
 - Take action to reduce greenhouse gas emissions across the value chain, consistent with the Paris Agreement's goal of limiting global average temperature increase to well below 2 degrees Celsius above pre-industrial level;
 - Provide enhanced corporate disclosure in line with the final recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) to enable investors to assess the robustness of companies' business plans against a range of climate scenarios, including well below 2-degrees Celsius, and improve investment decision-making.





As a participant member, Lothian will be directly involved in company engagement with Climate Action 100+, not just through its service provider, Hermes EOS, but directly through the internal team. It is a clear signal that Lothian Pension Fund is focused on the long-term impact of climate change and regulatory pressure on existing business models from expert industry knowledge and from working with experienced engagers in this field.

The internal investment management team already regularly engages with company managements in the normal course of doing due diligence on companies as shareholders or potential shareholders. These meetings, or engagements, are an opportunity to discuss the key factors affecting company performance and strategy, and, of course, these include any significant ESG issues pertinent to that company. Further information on Climate action 100 is available at www.climateaction100.org.

Climate Change

Climate change has become the global issue of our time. As of February 2019, 184 states and the EU (representing 88% of global greenhouse gas emissions) had ratified or acceded to the Paris Agreement of the United Nations Framework Convention on Climate Change. Under this agreement, each country must determine, plan and regularly report on the contribution it undertakes to mitigate global warming. The three key aims of the agreement are:

- Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1.5°C above pre-industrial levels, recognising that this would significantly reduce the risks and impacts of climate change;
- Increasing the ability to adapt to the adverse impacts of climate change and foster climate resilience and low greenhouse gas emissions development, in a manner that does not threaten food production;
- Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.

Separate to this, but part of the overall worldwide change in culture with regards to greenhouse gas emissions, the Financial Stability Board (FSB) of the Bank of England launched the Taskforce on Climate-Related Financial Disclosures (TCFD). TCFD aims to “develop voluntary, consistent climate-related financial risk disclosures for use by companies in providing information to investors, lenders, insurers, and other stakeholders.” Further information is available at www.fsb-tcfd.org.

As asset owners, Lothian has been engaging with the companies in its portfolios to enhance disclosures on emissions in line with the recommendations of TCFD, as well as working alongside peer organisations to promote the aims of the TCFD and reporting the Fund’s approach to climate change-related risks and opportunities in its PRI reporting.



As part of the TCFD resources, investors and asset owners also have guidance on how to report their approach to climate-related risks and opportunities. These recommendations are split into four key areas of reporting.



Governance relates to the organisation's governance and climate-related risks and opportunities.

Strategy relates to the actual and potential impacts of climate-related risks and opportunities on the organisation's businesses, strategy and financial planning.

Risk management relates to the processes used by the organisation to identify, assess and manage climate-related risks.

Metrics and Targets relates to metrics and targets used to assess and manage relevant climate-related risks and opportunities.

The TCFD is in its relative infancy and Lothian Pension Fund is challenging companies to improve their disclosure and rapidly integrating the specifics of climate change into the risk management and governance of the Fund. Over the few years, it has undertaken substantial work on the issue.

Climate Change - Governance

In accordance with Scheme Regulations, the Pensions Committee and Pension Board are required to undertake a minimum of 21 hours training. Each year, the Fund's provider of voting and engagement services is invited to present to and interact with the Committee and Board. During 2018/19, they received specific training on climate change-related risks and opportunities. This was followed up with the first climate-specific reporting for the Committee, a carbon footprint of the Fund's equity holdings in June 2018. The simplicity of output of a single carbon footprint number belied the complexity of the subject matter, and the following recommendations were agreed:

- Reaffirm the Fund's commitment to integrate environmental, social and governance (ESG) considerations, such as carbon efficiency trends, into its decision-making
- Note that the Fund scrutinises and engages with investment managers to ensure that they are taking ESG issues, including climate change and carbon risk, into account in their investment decision-making
- Reaffirm the Fund's policy of not divesting solely on the grounds of non-financial factors
- Note that the Fund will monitor research on the link between ESG factors (including carbon-related factors) and financial performance to inform future investment strategy, such as stock selection criteria for quantitative strategies; and



- Agree that the Fund should aim to influence engagement activity based on its shareholdings of companies that perform poorly on carbon efficiency measurements.

The carbon footprint report will be updated on an annual basis as part of an annual review of climate-related risks and opportunities.

More broadly, the Committee and Board considers a paper on the Fund's approach to Stewardship on an annual basis. This also covers climate related issues. During 2018/19, the Pension Fund organised an event on responsible investing, to which major stakeholders and elected officials of local authority employers were invited to review the Fund's approach, with the opportunity for discussion with the investment managers, legal professionals, representatives from PRI and Hermes EOS and Committee and Board members. For those unable to attend the event and for those that require to understand the Fund's approach because they receive attention from lobbyists on a range of issues, a recording of the event has been made available on the Fund's website.

Climate-related risks and opportunities are an integral part of the overall investment process for Lothian Pension Fund, and so the Pensions Committee delegates investment decision-making to officers and investment managers with advice from the Joint Investment Strategy Panel. Climate-related risk management is reviewed as part of the regular monitoring process, which includes analysis of ESG integration in the investment mandates. For Real Estate and Infrastructure managers, the Fund has recently incorporated GRESB data into the monitoring process to better assess climate-related risk within the Fund.

Climate Change - Strategy

The Fund recognises the contribution that some specific sectors and industrial activities have towards climate change. While many prefer to label companies in carbon-intensive industries 'bad' and those in low-carbon and alternative energy businesses as 'good', in reality investment is more nuanced than this. The Fund has a policy of engagement rather than blanket divestment, which allows us to exert influence on companies to improve their business practices, align with the Paris goals, and disclose internal climate-related risk and opportunity management with TCFD compliant reporting. Recent academic research commissioned by Lothian Pension Fund* suggests that divestment at best is ineffective, and at worst provides a clear disincentive for management to change.

The Fund's approach to engagement relies heavily on our engagement and voting partner, Hermes EOS. Hermes EOS engages with companies on a range of engagement issues including climate change. The internal management team also engages with company management on a regular basis as part of company roadshows and investment conferences.

*University of Edinburgh Master's in Economics Dissertation, "In response to the recent Paris Agreement, how might pension funds contribute to helping reduce global climate change through investment policy?", Cooper, 2019



In addition, the Fund has joined the Climate Action 100+ investor initiative and is actively participating in engagement with one of the 167 target companies in the list of systemically important carbon emitters produced by the initiative.

Regular training and development for all staff on climate related issues is provided. This includes governance functions, management, investment decisions makers, and pensions administration staff. This creates an internal culture that is serious about the risks to capital posed by the carbon transition.

The holdings of the Fund can be broadly classified under three approaches: fundamentally managed equity, quantitatively managed equity, passively managed government debt and externally managed funds (covering all asset classes). As part of the stock selection process for the fundamentally managed portfolios, any fundamentally material climate-related risks and opportunities (such as carbon pricing and the low carbon transition) are individually assessed by the managers and monitored in the portfolio holdings. Both the fundamental and quantitatively managed equity funds utilise engagement with managers to improve practices. The selection and monitoring process for external managers incorporates ESG elements, and this is continuing to be refined.

The internal managers continue to monitor opportunities in the green energy and future technology space, both in the public and private markets. Much of the public spending on green energy is being done by the incumbent energy providers (the diversification of carbon-extractive companies and carbon burning utilities).

Climate Change - Risk Management

The Fund produces annual carbon footprints for listed equities. Individual companies within this exercise can have their weighted average carbon intensity measured, allowing a look through into the concentration of carbon emission risk associated with each company. This has been useful in helping to guide engagement efforts and highlighting companies that could pose a capital risk in the event of an acceleration in the low carbon transition. To date, no divestment due to outsized climate-related risks have been made. Specific research budget has been allocated to data services associated with ESG and climate-related risks and opportunities.

Climate Change - Monitoring and Metrics

The Joint Investment Strategy Panel, Committee and Board all receive regular papers on general ESG (including climate related) issues and on specific climate-related risks and opportunities. The internal management team has a suite of tools available to them. Within equities, the team utilises MSCI ESG tools, including Carbon Metrics. This allows the managers in depth assessment of ESG risks and individual carbon emissions data for all the underlying companies enabling the Fund to produce annual carbon footprints for the equity portion of the Fund.



Recent additions of data from the Transition Pathway Initiative and Carbon Action 100+ are being incorporated into the equity management process.

Recent access to GRESB data in the infrastructure and real estate asset classes is being assessed and will be incorporated into reporting in these areas over time. Support for the Carbon Disclosure Project also allows access to useful research that is considered during due diligence on investments.

Manager Selection and Monitoring

While most of Lothian Pension Fund assets are equities and bonds that are managed internally, a proportion of investments are managed by third party managers. These external managers transact in public and private markets, investing in the equity and debt of infrastructure-related, corporate and property assets. One of the core elements of due diligence in the appointment process of managers centres on their approach to ESG issues. After appointment, Lothian continues to monitor the managers quarterly and as part of this quarterly reporting and monitoring cycle, managers are obliged to provide information on ESG related issues arising and how the managers are reacting to them.

Impact

An emerging theme in global responsible investment is Impact Investing – the provision of capital to address social and/or environmental issues. Investments are made in projects that aim to generate both a positive financial return and a non-financial return – the latter is often referred to as an environmental dividend or a social dividend.

These non-financial positive impacts can be linked to the aims of the United Nation’s Sustainable Development Goals (SDGs), which can be viewed at <https://sustainabledevelopment.un.org> and are a collection of 17 global policy areas identified to provide the greatest transformational potential to society. While these SDGs were written for policymakers, some investment professionals have begun to adopt them to target specific non-financial outcomes from their investment activities.



Lothian Pension Fund is regularly presented with these types of investment, and while not targeting Social and Environmental Impact alone, it will invest in them where they are expected to deliver an appropriate risk-adjusted return. The Fund makes investments in Private Equity, Private Debt, Infrastructure and Real Estate, which involve the deployment of capital into new projects, which are expected to have a positive impact, such as wind farms and other clean energy and modern, sustainable, energy efficient buildings. In this way, the Fund’s capital creates jobs, cutting edge new environments, and the clean energy that society will need in a low-carbon future – and all while providing sustainable risk-adjusted returns for the Fund.



Infrastructure Investment

Infrastructure investments have the potential to generate attractive risk-adjusted returns, with cash flows often linked to inflation. The long-term and defensive nature of these assets also can provide an element of diversification to the Fund's investment strategy.

Over the last decade, the Fund has developed its reputation, networking and execution capabilities to secure access to investment opportunities within this market niche. The Fund's experienced team appraises, and invests in primary and secondary funds as well as co-investments, to achieve its target allocation in a cost-effective manner. An important element of the implementation strategy is to work closely with investment managers to ensure execution certainty and to diligence the commercial and legal terms. Collectively, Lothian and its collaboration partners committed over £200 million in 2018/19 in infrastructure investment.

Lothian Pension Fund has a long-standing commitment to responsible investment. In addition to becoming a signatory of the UNPRI (United Nations Principles of Responsible Investment) in 2008, the Fund has subscribed to GRESB (Global Real Estate Sustainability Benchmark) to further enhance our analysis of environmental, social and governance issues.

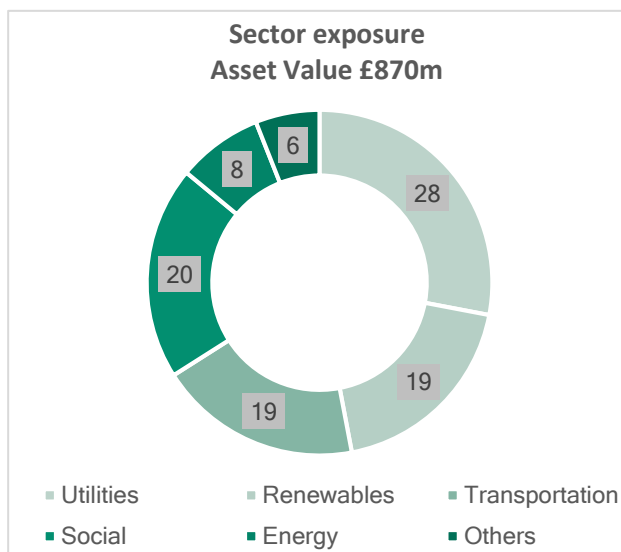
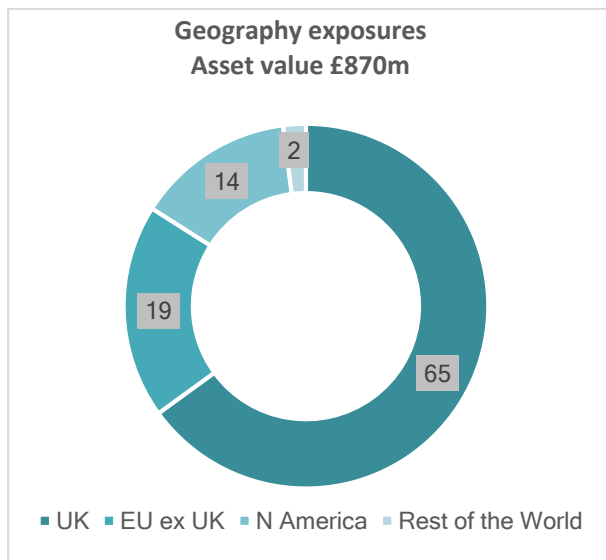
Infrastructure investments represented 11.1% of the value of Lothian Pension Fund assets at 31 March 2019, comprising one of the largest and most diversified allocations among UK LGPS funds. Of the total infrastructure investment of £870 million (31 March 2018: £795 million) invested in infrastructure, the majority is invested in the UK.

During 2018/19, Lothian Pension Fund completed two primary fund investments, acquired seven secondary fund interests and invested in three co-investments. Approximately £135 million has been invested over the year in UK, European and Global infrastructure assets. During the same period, £173 million has been distributed to the Fund. There were two successful realizations during the period generating proceeds of £48 million and recording a blended net internal rate of return of 22.3% and a total value to paid-in multiple of 1.8x. Distributions from secondary fund investments contributed £91 million.

Secondary fund investments completed following the global financial crisis in 2007-2008 boosted returns. The Fund invested £402 million in ownership interests of 23 funds from 2010 to 2019. It has received £309 million of distributions from those investments and the remaining invested value at 31 March 2019 was £329 million. This generated a total value to paid-in multiple of 1.6x and an internal rate of return of 17% to date.



The geographic and sector exposures for Lothian Pension Fund infrastructure allocations (at 31 March 2019) are shown in the charts below.

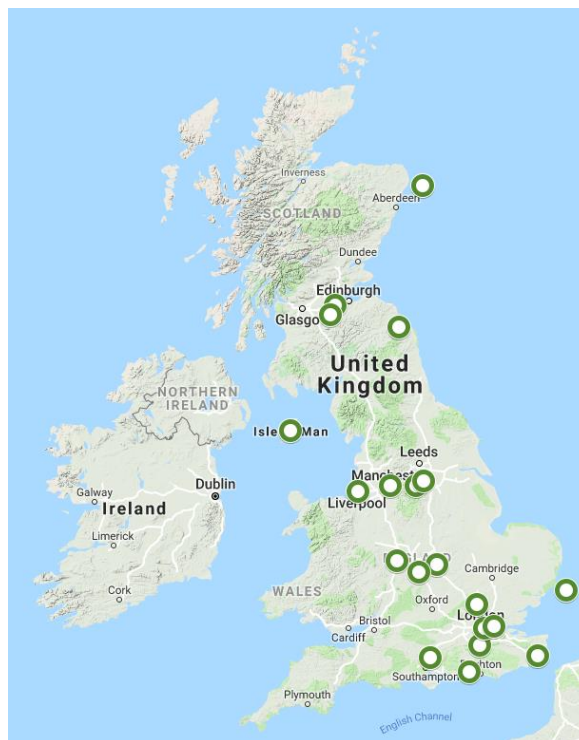


Infrastructure investments in the UK contributed 64% (or £559 million) of the total. The Funds' 20 largest UK investments, representing £400 million of value, are shown in the map below.

Investments are made across a diverse range of projects, in the areas of:

- social infrastructure (including hospitals, schools and roads);
- regulated utilities (including water and electricity);
- energy & renewables (including solar and wind);
- transportation (including ports and rail); and
- others (including car parks and smart meters).

The Fund recognises the role infrastructure investment can make to addressing part of the current environmental challenges related to climate change. Approximately, 20% of the infrastructure portfolio is invested in renewable energy. During the year, the Fund allocated £47 million to co-investments in UK renewable energy projects – a diversified portfolio of wind farms and in an energy from waste facility.





Funding Strategy Statement

The Funding Strategy Statement covers the funding strategies for Lothian Pension Fund and Scottish Homes Pension Fund and can be viewed on our website at www.lpf.org.uk/publications.

The purpose of the Funding Strategy Statement is:

- to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward;
- to support the regulatory framework to maintain as nearly constant employer contribution rates as possible; and
- to take a prudent longer-term view of funding those liabilities.

These objectives are desirable individually but may be mutually conflicting.

The Funding Strategy Statement also ensures that the regulatory requirements to set contributions to ensure the solvency and long-term cost efficiency of the Funds (as defined by the Public Service Pensions Act 2013) are met.

Key policies, including the Fund's Admission Policy and Policy on Employers Leaving the Fund are appended to the Funding Strategy Statement. The policy on Employers Leaving the Fund sets out the Fund's approach to dealing with employer exits, including principles for determining payment of cessation debt.

The Funding Strategy Statement was revised at the 2017 Actuarial Valuation and reflects CIPFA

guidance "Preparing and maintaining a funding strategy statement in the Local Government Pension Scheme 2016". In addition to updates required as a result of changes to the Scheme Regulations and other pensions legislation, these included:

- the introduction of a new medium risk investment strategy intended to smooth the path to exit and reduce the deficit risk when an employer leaves the fund
- the requirement for employers to provide written confirmation that minimum contribution rates set by the Actuary are not unaffordable.

As required by Scheme Regulations, the Fund consulted with employers as part of the review process. Further amendments have been made to incorporate changes to Scheme Regulations in 2018 and an update to the Fund's bulk transfer policy. A consultation on these amendments is in progress.

The Fund must be able to meet all benefit payments as and when they fall due. These payments will be met by contributions (resulting from the funding strategy), or asset returns (derived from the investment strategy). A formal review of the Fund's investment strategies is undertaken at least every three years to ensure appropriate alignment with liabilities. Further information on the investment strategies can be found in the Fund's Statement of Investment Principles also available at www.lpf.org.uk.



Financial Performance

Administration expenses

A summary of the Fund's administrative expenditure for 2018/19, against the budget approved by Pensions Committee, is shown in the table below. This budget includes adjustment agreed by Pensions Committee during the financial year.

The budget focuses on controllable expenditures and therefore excludes all benefit payments and transfers of pensions from the Fund. Similarly, income does not include contributions receivable and pension transfers to the Fund. The total net cost outturn of £28,703k against budgeted of £29,410k represented an underspending of £707k (2.4%) for the Fund. The key budget variances serving to generate this underspending were:

- Investment management fees - £1,169k overspending. This budget also includes investment management fees deducted from capital but excludes the performance related element of these charges due to their unpredictable nature. Broadly speaking both invoiced and uninvoiced investment management fees were within expectations. The overspending related entirely to investment property operational costs, arising from a tenant company entering administration, and the resultant debt being written-off and recognised in the Fund Account.
- Supplies and Services - £605k underspending. Implementation delay of the investment front office software system was the major factor.
- Employees - £602k underspending. This reflected general recruitment delays in the filling of vacant posts and revised accounting advice in respect of the treatment of the vested elements of variable pay.

| | Approved budget | Actual outturn | Variance |
|------------------------------------------------|-----------------|----------------|--------------|
| | £000 | £000 | £000 |
| Employees | 4,379 | 3,777 | (602) |
| Transport & Premises | 250 | 224 | (26) |
| Supplies and Services | 1,934 | 1,329 | (605) |
| Investment Managers Fees* | 22,300 | 23,469 | 1,169 |
| Other Third-Party Payments | 1,439 | 1,120 | (319) |
| Capital funding - Depreciation | 132 | 62 | (70) |
| Direct Expenditure | 30,720 | 29,981 | (453) |
| Support Costs | 286 | 250 | (36) |
| Income | (1,310) | (1,528) | (218) |
| Total net controllable cost to the Fund | 29,410 | 28,703 | (707) |

*Does not include performance element. In 2018/19, £8.5m was paid in fees in relation to the Fund's private market investments.



Reconciliation to total costs

| | Actual outturn |
|---------------------------------------------------------------------------------------|----------------|
| | £000 |
| Actual outturn on budgeted items above | 28,703 |
| Add: Securities lending revenue included in income above | 943 |
| Investment management fees deducted from capital – performance related element | 8,531 |
| IAS19 LPFE retirement benefits | 594 |
| LPFE deferred tax on retirement benefits | (101) |
| Corporation tax | 29 |
| Total cost to the Fund (inclusive of full cost investment management fees) | 38,699 |
| Per Fund Accounts | |
| Lothian Pension Fund Group | 38,634 |
| Scottish Homes Pension Fund | 65 |
| Total | 38,699 |

Cash-flow

Cashflow to and from a pension fund is very dependent upon the profile of its membership. Specifically, a maturing membership, where the proportion of active to deferred and pensioner members is reducing, would be expected to see a reduction in contributions received, together with additional outlays on payments to pensioners.

Lothian Pension Fund continued to experience a net reduction in value from its dealings with members. That said, the Fund has seen a £6.8million improvement in this position during the year with outlays exceeding receipts by £13.0million, compared to higher net withdrawals of £19.8million in the previous financial year. This reflects both the first year of higher employer contributions, as determined by the actuarial valuation 2017 results, and the upward trend in the number of active members.

Scottish Homes Pension Fund is a mature fund with no active members. As a result, pension outlays are met from investment income, supplemented by asset sales. Net pension outlays were £7.3million representing a £0.4million change in position from 31 March 2018 (net withdrawals of £6.9million).



It is anticipated that for the next few years these cash flow trends will remain broadly consistent.

Membership statistics and funding statements from the Actuary are provided for both Funds in the Fund Accounts sections.

2017 Actuarial Valuations

The most recent triennial assessment of the funding position of the pension funds was undertaken by the Fund's Actuary as at 31 March 2017. In general, the results showed that despite better than expected asset returns since the 2014 actuarial valuation, employer costs increased due to a reduction in future expected investment returns. The Funding Strategy Statement was reviewed and amended following consultation with employers.

For Lothian Pension Fund, the funding level increased from 91% at 31 March 2014 to 98% at this valuation. The deficit decreased from £417million at 31 March 2014 to £145million at 31 March 2017. Reflecting the differences in the employers in the Fund, a third investment strategy was introduced for employers which are closed to new entrants but not close to exiting the Fund. The Fund also introduced a requirement for employers to provide written confirmation that minimum contribution rates set by the Actuary are affordable. It is not in the best interests of the individual employers or the Fund for employers to continue to accrue unaffordable pension liabilities. Three employers indicated that the minimum contribution rates were unaffordable and the Fund worked with them to manage their exit from the Fund. The Fund continues to work with employers to put in place funding agreement to address repayment of debt when an employer leaves, in order to avoid employer default or insolvency.

The funding level for Scottish Homes Pension Fund at 31 March 2017 was 104.7%, increased from 88.8% from the 2014 actuarial valuation. Consultation was undertaken with the Scottish Government on the potential benefits offered by revising the Funding Agreement for this Fund. However, it advised that it does not wish to revisit this and as a result the investments of the Fund are now fully invested in index-linked government bonds and cash.

Investment management cost transparency

Local authorities are required to account for pension funds in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). The Code is based on approved accounting standards issued by the International Accounting Standards Board and interpretations of the International Financial Reporting Interpretations Committee, except where these are inconsistent with specific statutory requirements. The Code also draws on approved accounting standards issued by the International Public Sector Accounting Standards Board and the UK Financial Reporting Council where these provide additional guidance. Guidance is still awaited from CIPFA as to how these costs should be standardised and reported in the Annual Reports of LGPS Funds.



CIPFA published this guidance in July 2014, which promoted greater transparency of investment management fees. These principles were adopted as best practice in the presentation of the Lothian Pension Fund audited Annual Report 2015. In June 2016, CIPFA revised its guidance including the following “Investment costs incurred by a separate legal entity, or in respect of investment decisions over which the pension fund has no control, should not be included in the Fund Account.” The revised guidance changed the disclosure of fees for fund of funds investment arrangements. A “fund of funds” is an investment holding a portfolio of other investment funds rather than investing directly in funds. Typically, fees are payable to the “fund of funds” manager as well as to the managers of the underlying funds. Generally, under the revised guidance from CIPFA, the second and third layer of fees would not be disclosed with just the fees from the “fund of funds” manager stated.

In the preparation of the Fund’s Annual Report for 2014/15 and 2015/16, the Fund made efforts to be completely transparent on the totality of costs incurred for managing its investment assets. The Fund’s disclosures included all layers of fees. At its meeting on 28 September 2016, the Pensions Committee agreed to instruct the Committee Clerk to communicate to the Chartered Institute of Public Finance and Accountancy (CIPFA), Audit Scotland and the Scottish Local Government Pension Scheme Advisory Board (SLGPSAB), the Committee’s and Convener’s disquiet with the relaxation of the principle of full cost transparency of investment management fees, as explicit in CIPFA’s revised guidance “Accounting for Local Government Pension Scheme Management Costs”.

In May 2018, CIPFA published “Proposals for LGPS Fund Reporting in a ‘Pooled World’”. “This sets out proposals for revised reporting for LGPS pension funds to meet a number of objectives”, including “to further enhance reporting of costs reflecting the introduction of the LGPS SAB Code of Transparency for asset managers, and initiatives underway by the Financial Conduct Authority (FCA) and Department for Work and Pensions (DWP) which aim to create more transparent and granular reporting standards for both providers and trustees This paper has been issued by CIPFA as good practice which is to be incorporated into 2018/19 Annual Report guidance for local government pension funds.”

Most recently, in March 2019, CIPFA published “preparing the annual report - Guidance for Local Government Pension Scheme Funds (LGPS) 2019 Edition”. The purpose of this guidance is to assist local government pension funds with the preparation and publication of the annual report required by Regulation 55 of The Local Government Pension Scheme (Scotland) Regulations 2018.

The Pensions and Lifetime Saving Association (PLSA) confirmed the launch of new templates in May 2019 in relation to its Cost Transparency Initiative. The aim of the initiative being to provide a standardised way for asset managers to report costs and charges to investors. Guidance is still awaited from CIPFA as to how these costs will be standardised and reported in the Annual Reports of LGPS Funds.



The financial statements of Lothian Pension Fund and Scottish Homes Pension Fund continue to include full transparency for both Funds' internal and external investment management fees.

| | Investment management expenses in compliance with CIPFA guidance | Investment management expenses per 2017/18 financial statements | Disclosure in excess of CIPFA guidance |
|-----------------------------|------------------------------------------------------------------|-----------------------------------------------------------------|----------------------------------------|
| | £000 | £000 | £000 |
| Lothian Pension Fund | 31,041 | 36,103 | 5,062 |
| Scottish Homes Pension Fund | 84 | 84 | 0 |
| TOTAL | 31,125 | 36,187 | 5,062 |

Investment cost benchmarking

Investment strategy focuses on risk adjusted returns, net of costs. The Fund has participated in investment cost benchmarking provided by CEM, an independent benchmarking expert for global pension funds with a database of 346 global pension funds representing £7.3 trillion in assets. To provide a fair comparison, CEM calculates a benchmark based on fund size and asset mix, which are key drivers of investment costs.

The latest analysis shows Lothian Pension Fund's investment costs of 0.43% of Fund assets were significantly lower than CEM's benchmark cost of 0.55%, an equivalent annual saving of approximately £8.0m. This saving largely reflects the fact that the Fund manages a relatively high percentage of assets internally compared with other similar pension funds and that it has low exposure to fund-of-fund investment vehicles.



Performance and Administration

Key Performance Indicators 2018/19

The Fund has a strong commitment to customer service which drives the continuous development of our services to ensure the best possible service for customers whilst recognising potential demands of the future. We set challenging performance targets and measure these through key indicators reported to our Pensions Committee and Pension Board and internal indicators reported to internal management.

The table shows our performance against these targets.

| 2018/2019 | Target | Actual |
|-----------------------------------------------------------------------------------------------------------|---------------------|----------|
| Maintain Customer Service Excellence Standard (CSE) (Annual assessment) | Retain | Retained |
| Audit of Annual Report and Accounts 2017/18 | Unqualified opinion | Met |
| Proportion of members receiving a benefit statement and by August | 100% | 100% |
| Overall satisfaction of employers, active members and pensioners measured by surveys | 90% | 92.7% |
| Percentage by value of pension contributions received within 19 days of end of month to which they relate | 99% | 99.7% |
| Investment performance and Risk of Lothian Pension Fund over rolling 5 year period | Meet benchmark | Met |
| Monthly pension payroll paid on time | Met | Met |
| Level of sickness absence | 4.0% | 3.9% |
| All staff complete at least two days training per year | Yes | 100% |
| Staff engagement index | Greater than 70% | 69% |

Value for money

Value for Money is the term used to assess whether an organisation has obtained the maximum benefit from services it acquires or provides, within the resources available to it. It has three components to take account of economy, efficiency and effectiveness. The Fund participates in benchmarking provided by the Chartered Institute of Public Finance and Accountancy (CIPFA). The purpose is to help identify the areas where improvements can be made to deliver better value for money. The exercise carried out facilitates:

- comparison between costs and performance
- the provision of evidence to support decisions on budget relating to the sustainability and capability of the investment and administrative teams to enhance customer satisfaction

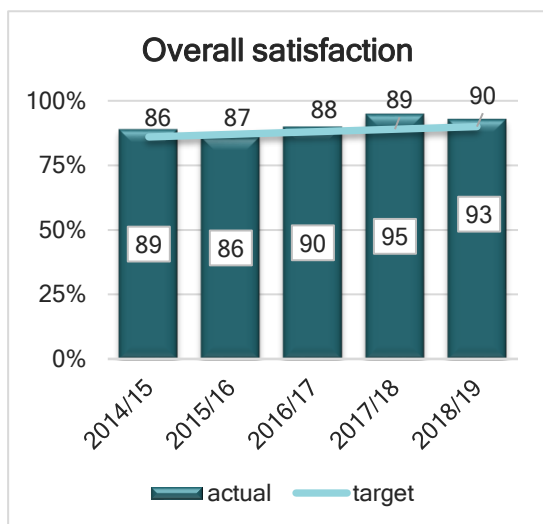


- sharing of information and ideas with peers; and
- a review of performance trends over time.

The outputs and analyses have served to supplement internal performance management information. However, the Chartered Institute of Public Finance and Accountancy (CIPFA) has stated that, in order to protect its commercial interests, its benchmarking reports “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”. We are therefore unable to include full information on the results in the Annual Report.

A summary of the benchmarking is as follows:

- Lothian Pension Fund’s cost per member of £23.38 falls within the very wide range of local authority funds of c£11 to £61. However, the cost is higher than the average of all funds of £21.71. The average of funds of comparable scale is £21.16.
- The composition of a Fund’s membership impacts costs. Active members represent 39.3% of the Fund membership compared with an average of 34.2%, and pensioners represent 30.8% compared with 24.1%, with the consequence that deferred members represent a lower proportion of membership (22.2%) than the typical fund (29.9%). As deferred members are less demanding on administration services, these factors would tend to increase pension administration and payroll workload and therefore cost.
- Also of note is that the proportion of staff holding relevant pension administration qualifications is significantly higher than the average (more than double).
- Moreover, the Fund’s administration performance is above average for 7 of the 9 industry standard indicators, in certain instances by a considerable margin.



Customer and complaint feedback

Listening to feedback is key to our services, with the Fund carrying out surveys to monitor individual and overall satisfaction. Our overall satisfaction continues to improve and in 2018/19 remains above the 90% target at 92.7%. This exceeds the target of 90%.

We also monitor complaints and ensure we respond and resolve where possible, within 20 working days. We investigate and learn from both formal and informal complaints to ensure we are continuously improving our services. Complaints are split by those about the service we provide and those about how Scheme Regulations are applied.



We carried out 20,389 processes in 2018/19 and there were very few complaints made, less than 0.1%. Complaints covered a broader range of issues including taking small pensions as a cash lump sum and the time it took to pay a Cash Equivalent Transfer Value to new pension providers.

Internal Dispute Resolution Procedure (IDRP)

Pensions law requires that the Local Government Pension Scheme must have a formal procedure in place for resolving disputes arising from the running of the scheme. The IDRP is a two stage process. An external independent appointed person deals with disputes at the first stage. The second stage is dealt with by the Scottish Ministers.

In 2018/19, there were seven stage 1 disputes for investigation. If a member remains dissatisfied with the Stage 1 decision, they have six months to take their appeal to Stage 2. In 2018/19, there were six Stage two disputes and one remaining from 2017/18 which is included in the statistics below.

| Reason for dispute | | Stage 1 outcome | Stage 2 outcome | On-going |
|----------------------------------------------------------------|---|-----------------|-----------------|----------|
| Error | 1 | 1 not upheld | 1 not upheld | 0 |
| Overpayment | 1 | 1 not upheld | | 1 |
| Awards, eg early payment of deferred pension on health grounds | 5 | 5 not upheld | 1 upheld | 4 |

Further information about the IDRP and complaints procedure is available on our website at www.lpf.org.uk/complaints.

Our data

We issued 100% of benefit statements by the statutory deadline of 31 August 2018. Although we have achieved over 99% in the past 2 years, this is the first time we have achieved 100% since the target was introduced by the Pensions Regulator in 2015.

All of our employers submit contribution data each month and in October, the Fund moved over to a new service following a tendering process. The previous provider did not tender and so a new service that integrates with our pension administration software was sought. This employer data portal has allowed us to continue to ensure accuracy of member data.

We measure our pension record keeping standards against The Pension Regulator's best practice guidance. Poor record-keeping can lead to significant additional costs in areas such as administration, error correction, claims from members as well as fines from The Pensions Regulator.



Over the year, we have continued data accuracy improvements with our employers and carried out significant additional work as part of the introduction of the new employer portal. We are also carrying out external tracing of members where we do not hold a current address.

Historically, the Fund has prepared its assessment of common and conditional data in-house, calculated as an overall percentage of member records passed in each category tested.

Due to the complexity of the Regulator's illustrative list of conditional data requirements, previous results were based on a small number of conditional data categories. The Annual Report and Accounts 2017/18 cited a score of 99.9% for both the common and conditional data.

This year, the Fund has utilised a new Data Quality Service provided by the software supplier. The Fund can now provide data score measurements required by the Regulator based on more comprehensive analysis and based on the percentage of clean member records without a single data failure.

The conditional data now interrogates five data categories; Member Benefits, Member Details, CARE Benefits, HMRC Data and Contracted Out Data.

The Funds' (combined Lothian Pension Fund and Scottish Homes Pension Fund) scores as at 31 March 2018 were 95.6% for common data and 90.9% for conditional data. As this is the first time using the new software, issues were identified with the way some historic data has been recorded, rather than data being unavailable. The software supplier stated that the general quality of the Fund's common data was of a high standard compared with other LGPS funds.

In order to maximise the cost efficiency of this annual outsourced assessment, the member data extract was run on 13 August 2019, with effective date as at 31 March 2019. This enables the data cleansing of member records undertaken by the Funds prior to issuing the Annual Benefit Statements to be reflected in the assessment. This timeframe also aligns to the submission of the annual scheme return to TPR by 30 November 2019.

Lothian Pension Fund and Scottish Homes Pension Fund scored 98.3% and 96.5% respectively for common data and 95.4% and 96.7% for conditional data as at 31 March 2019. This is the first year of having separate scoring for each Fund.

Guaranteed Minimum Pension (GMP)

GMP is the minimum pension which a United Kingdom occupational pension scheme must provide for those employees who were contracted out of the State Earnings-Related Pension Scheme (SERPS) between 6 April 1978 and 5 April 1997. The UK Government has mandated a reconciliation of Guaranteed Minimum Pension details held on scheme pension administration records to those held by HMRC. This was to be completed by the 31 March 2019.

An internal team has been working on this project since the announcement and the reconciliation was 100% complete by March 2019. Underpayments of pensions are being corrected and put into payment, together with lump sum arrears.



The Scottish Ministers have decided any LGPS pension in payment affected by the exercise should not be reduced. Instead it is expected that overpayments will be held separately and remain static going forward and not receive any Pension Increase that may be due on other LGPS pension benefits.

Pension Administration

The introduction of the career average pension scheme in April 2015 has meant that pension administration has become more complex for both the Fund and employers.

New Scheme Regulations were introduced with effect from 1 June 2018 introducing a number of changes, the most significant of which lowered the earliest age members can voluntarily retire to 55.

However, changes were not made to previous transitional Regulations 2014 which meant important regulatory references within the Transitional Regulations were incorrect and therefore not competent. Legal advice at the time confirmed that using these Regulations could leave the Fund open to challenge.

The Fund therefore put a hold on paying retirement and death in service benefits for members with membership prior to April 2015. A letter of comfort from the Scottish Government was received 2 months later which allowed the resumption of these payments.

Also, on 29 October 2018, the UK Government announced a change in the discount rate used to set employer contribution in public service pension schemes. As a result, the Fund had to suspend all non-club Cash Equivalent Transfer Values (CETVs) and Divorce CETVs until new factors were made available on 29 November 2018.

Our in-house pension administration team provides a dedicated service for the pension fund members. We monitor the time taken to complete our procedures. Key procedures include processing of retirement and dependent benefits, providing information for new members, transfers and retirement quotes. Despite the challenging environment, 92% of key procedures in 2018/19 were completed in target. However, in other areas, some delays were experienced while this key work was prioritised.

The table below shows the number and type of retirements in 2018/19.

| | Ill health | Early - age 60 to NPA | Early – age 55 to 59 | Redundancy | Efficiency | Late | TOTAL |
|-----------------------------|------------|-----------------------|----------------------|------------|------------|------|-------|
| Lothian Pension Fund | 118 | 907 | 140 | 115 | 61 | 165 | 1506 |
| Scottish Homes Pension Fund | 0 | 21 | 0 | 0 | 0 | 0 | 21 |



The table below shows performance against key procedures in 2018/19.

| | Target | Actual |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------|--------|
| Proportion of critical pensions administration work completed within standards – individual performance within this indicator are shown below | Greater than 91% | 92.2% |
| Provide a maximum of one guaranteed Cash Equivalent Transfer Value (CETV) within 10 working days of receiving a request | 90% | 96.7% |
| Payment of CETV within 20 working days of receiving all completed transfer out forms | 95% | 97.2% |
| Pay lump sum retirement grant within 7 working days of receiving all the information we need from the member | 95% | 97.5% |
| Notification of dependant benefits within 5 working days of receiving all necessary paperwork | 95% | 98.3% |
| Acknowledge of the notification of the death of a member to next of kin within 5 working days. | 95% | 97.2% |
| Respond in writing within 20 working days to formal complaints that have escalated from frontline resolution, or recorded directly as an investigation | 95% | 100% |
| Provide transfer-in quote within 10 working days of receiving the Cash Equivalent Transfer Value (CETV) from member's previous pension provider. | 95% | 80.4% |
| Notify members holding more than 3 months, but less than 2 years' service, of their options at leaving. As there is a one month and a day lying period, the target is within 10 days of the end of the lying period or after the employer providing full leaving information if later, | 80% | 77.0% |
| Pay a refund of contributions within 7 working days of receiving the completed declaration and bank detail form. | 90% | 87.7% |
| Notify early leavers entitled to deferred benefits of their rights and options within 10 days of being informed of end of pensionable service. | 90% | 81.7% |
| Estimate requested by employer of retirement benefits within 10 working days | 90% | 82.3% |
| Pay any lump sum death grant within 7 working days of receipt of the appropriate documentation | 95% | 92.7% |
| Proportion of non-key procedures completed within standard including Additional Regular Contributions, responding to member communications, updating nominations and maintaining the member database. | 75% | 73.6% |



The Fund also participates in the National Fraud Initiative which is a data matching exercise led by Audit Scotland and is carried out every two years. The 2018/19 matching exercise started in Autumn 2018 and matches were made available to the Fund from 31 January 2019. We are currently investigating these and will report the outcomes to the Pensions Committee in September 2019. In 2018/19, the total value of pension overpayments written off under delegated authority (overpayments up to £3,000) between 1 September 2017 and 31 August 2018 was £1,860.33.

There were three cases with a total of £74,978 written off as overpayment of pensions by the Pensions Committee.

The most significant overpayment was for a widow who did not notify us of remarriage. The pension should have been stopped on remarriage due to earlier pension scheme rules that prohibit payment of a widow's pension on remarriage which resulted in the overpayment. However, these regulations do allow reinstatement at a future date should the remarriage end. A caveat has been put in place that any reinstatement would only be paid once the recovery of the overpaid pension amount had taken place.

Online services

The Fund is moving towards providing as many services as possible online. We currently have 44% of active members registered for the online service. We provide retirement estimates and refund information online and are investigating ways to increase the use of improve processing times and enhance services for our members. Information for members is also available via email, phone and in person visitors to our offices.

Lothian PENSION FUND

Help Home Login

Login

LOGIN - Please enter your username and password below. PLEASE NOTE: the fields turn green to indicate you have completed them, it does not mean that the entry is correct. Not registered? You can sign up to [register](#) or [re-register](#) here.
If you have received an activation key, please [complete your registration](#) here.

Username

Password

[CLICK HERE IF YOU HAVE FORGOTTEN YOUR PASSWORD](#)
[CLICK HERE IF YOU HAVE FORGOTTEN YOUR USERNAME](#)

Login

As part of the pension software tender process, we introduced a new portal for employers to send monthly contribution returns. Data can now be automatically uploaded to the pension software system allowing automation of tasks previously requiring to be done manually.

This project resulted in a small number of employers' data being delayed whilst changes to processes and matching of information was carried out. In 2019/20, all employers should be fully utilising the service.



Unclaimed Monies Account

Where a member leaves the Fund with less than 2 years membership they are entitled to a refund or transfer to another pension provider. Where we do not receive a response to any of our correspondence, we record these as Status 3: Exit – No liability with a marker as unclaimed. We report this figure monthly and at 1 April 2019 the unclaimed amount was £909,056.44 with 2,527 records with the unclaimed marker.

We are continuing to check these unclaimed records and contacting these members to remind them of their options and will work to ensure monies are refunded or transferred where possible.

Employer performance

The Pensions Administration Strategy sets out the roles and responsibilities of both the Fund and employers, specifying the levels of services the parties will provide to each other and referring to four key areas where the Fund will pass on the costs of poor performance from employers:

- Late payment of contributions
- Late submission of membership information at the end of the year
- Failure to supply the Fund with information required to provide members with pensions savings statements; and
- Failure to provide details of member contributions monthly.

These areas are particularly important to ensure compliance with legislation, including accurate data to administer the new career average pension scheme and the requirement to provide members with a pension forecast by 31 August each year. Charges for late payment of contributions are as stated in the Scheme Regulations whilst other charges have been set to reflect the additional time spent in resolving queries and pursuing late information.

The Fund monitors employer performance against the standards set out in the Pension Administration Strategy. Results are reported to employers by way of an annual performance report, with more regular reporting for larger employers.

Due to the ongoing migration to the new data transfer portal, we are unable to provide accurate statistics for new members. Employers have continued to provide new member data and we will be in a position to report accurately in 2019/20.

Whilst the provision of leaver information in target has increased slightly, the majority were received out of target. We have continued to target historical cases and provide missing leaver queries to employers monthly. We are confident that historical cases have now been completed and employers can focus on 'business as usual' cases in 2019/20.



Unfortunately, most retirement information continues to be provided out of target. Just over half of all retirements occur where members are over age 55 and voluntarily take their pension benefits with a permanent actuarial reduction. Only 35% of these retirements were received in target. We shall continue our engagement with employers to seek requisite improvement.

Overall employer performance for 2018/19 is shown below, with 2017/18 shown for comparison purposes.

| Case type | Target (working days) | 2017/18 | | | 2018/19 | | |
|-------------------|-----------------------|-----------------|----------------------|-----------------|-----------------|----------------------|-----------------|
| | | Number received | Number within target | % within target | Number received | Number within target | % within target |
| New members | 20 | 6,204 | 5,439 | 88% | 4,379 | N/A | N/A |
| Leavers | 20 | 2,460 | 1,058 | 43% | 3,628 | 1,715 | 47% |
| Retirements | 20 | 1,050 | 427 | 41% | 1,249 | 488 | 39% |
| Deaths in Service | 10 | 26 | 13 | 50% | 11 | 7 | 64% |

Employer contributions

We monitor the payment of employer contributions as employers are required under the Pensions Act 1995 to pay contributions by the 19th of the month after the deduction was made. This is a key performance indicator with a target of was 99% contributions paid in time.

The primary rate for the whole Fund at the triennial valuation for 2018/19 was 31.8% shown as a percentage of pay. Each employer has its own individual rate based on its own circumstances.

99.7% of contributions by value were paid on time. Of the 1,022 payments made, 46 were paid later than the 19th and these are shown in the table. The option to levy interest on overdue contributions was not exercised in 2018/19 as late contributions were not received significantly later than the 19th significant.



| Employer | Number of late payments | Employer | Number of late payments |
|---------------------------------|-------------------------|-------------------------|-------------------------|
| Scotland's Learning Partnership | 10 | Young Scot Enterprise | 2 |
| Freespace Housing | 5 | Baxterstorey | 1 |
| Skanska | 5 | Canongate Youth Project | 1 |
| Homeless Action Scotland | 4 | Enjoy East Lothian | 1 |
| North Edinburgh Dementia Care | 3 | Morrison Construction | 1 |
| EDI Group Ltd | 3 | Scottish Futures Trust | 1 |
| Four Square | 2 | St Columba's Hospice | 1 |
| Heriot Watt University | 2 | Visit Scotland | 1 |
| Stepping Out Project | 2 | West Lothian College | 1 |
| TOTAL | | | 46 |

Scotland's Learning Partnership was late with payments on ten occasions. It should be noted that, on 26 April 2019, the Scottish Public Pensions Agency (SPPA) advised that "Ministers have agreed that Scottish Government will provide a guarantee in respect of the liabilities for the staff from the former Community Learning Scotland who transferred to the Local Government Pension Scheme". This guarantee was signed on 3 June 2019.

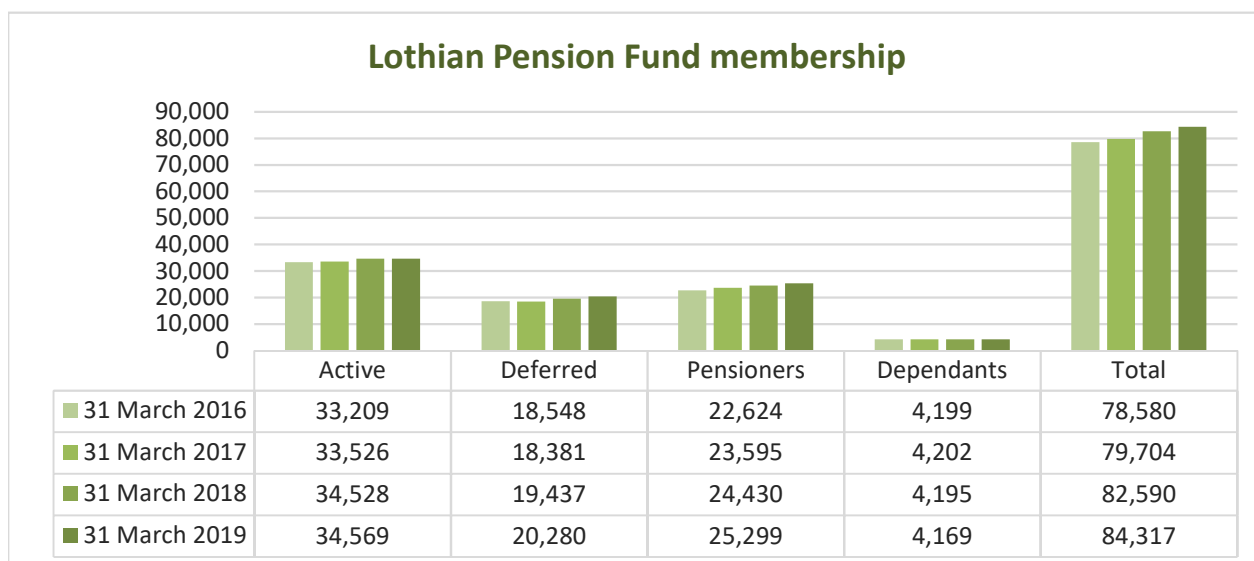
Management commentary approved by:

ANDREW KERR
Chief Executive Officer
The City of Edinburgh Council
25 September 2019

DOUG HERON
Chief Executive
Lothian Pension Fund
25 September 2019

JOHN BURNS
Chief Finance Officer
Lothian Pension Fund
25 September 2019

Lothian Pension Fund



Membership include Lothian Buses members as the Funds were merged in January 2019. Lothian Buses membership as at 31 March 2019 totalled 898 active members, 1,011 deferred members, 1,382 pensioner members and 384 dependants.

Investment Strategy

In order to provide suitable investment strategies for the differing requirements of employers, the Fund currently operates four investment strategies. Most employer liabilities are funded under the Main Strategy, which adopts a long-term investment strategy, aiming to maximise the investment return within reasonable and considered risk parameters and hence minimise the cost to the employer. The investment strategy is set at broad asset class levels, which are the key determinants of investment risk and return. During 2018, the previous broad asset classes of Equities, Index-linked assets and Alternatives were replaced by five policy groups - Equities, Real Assets, Non-Gilt Debt, Gilts and Cash - to better reflect the risk and return characteristics of each group.

A small number of employers are funded in the Mature Employers Strategy, which invests in a portfolio of UK index-linked gilts to reduce funding level and contribution rate risk as these employers approach exit from the Fund. The liabilities funded by the Mature Employers Strategy represent less than 1% of total liabilities.

The 50/50 Strategy enables another small group of less mature employers to fund liabilities with a 50/50 mix of the Main Strategy and the Mature Employers Strategy. The liabilities funded by the 50/50 Strategy represent just over 1% of total liabilities.

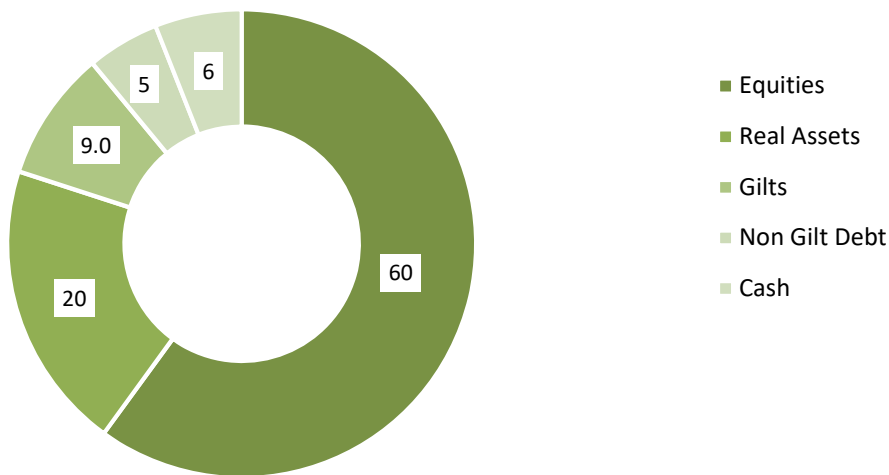
The Buses Strategy was introduced on 31 January 2019 when the assets and liabilities of Lothian Buses Pension Fund were consolidated into the Lothian Pension Fund. It is the same strategy that the Buses Pension Fund followed previously (agreed by Committee in 2016) when it was managed as a separate Fund

Following on from the 2017 actuarial valuation and a comprehensive review of strategy. This review focused on the Main Strategy because the Mature Employers Strategy is entirely invested in gilts, the 50/50 Strategy is invested in a 50/50 combination of the Main Strategy and the Mature Employers Strategy, and the Buses Strategy is the previously agreed Lothian Buses Strategy.

The conclusion of the strategy view was that the Fund should continue with its previous investment strategy (65% invested in lower risk equities) whilst continuing to monitor the impact of bond yields. Opportunities to reduce risk, by reducing equities by up to 15%, should be considered if bond yields and funding levels increase significantly. The Fund's investment strategy was approved by the Pensions Committee in December 2018.

| Lothian Pension Fund At 31 March 2019 | Main Strategy | Mature Ers Strategy | 50/50 Strategy | Buses Strategy | Total Fund Strategy |
|---------------------------------------|---------------|---------------------|----------------|----------------|---------------------|
| Equities | 65.0% | 0.0% | 32.5% | 51.5% | 63.1% |
| Real Assets | 18.0% | 0.0% | 9.0% | 18.0% | 17.7% |
| Non-Gilt Debt | 10.0% | 0.0% | 5.0% | 10.5% | 9.9% |
| Gilts | 7.0% | 100.0% | 53.5% | 20.0% | 9.3% |
| Cash | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| Total | 100% | 100% | 100% | 100% | 100% |

Actual Asset Allocation (%) at 31 March 2019



A key objective of the Fund's investment strategy is to reduce risk and this is largely achieved by reducing risk within the equity pool of assets. Implementation of the strategy has involved a shift from a regional to a global manager structure. Significant steps have been taken in this regard in prior years with the introduction of the internally managed global equity portfolios. As such, 2018/19 represented much more of a "steady state" in terms of the structure within the equity exposure.

The activity in recent years (2012-2015) has been to increase the proportion of internally managed global equity strategies to reduce investment risk. The resultant equity pool of assets is expected to perform relatively well when equity markets are weak and produce good positive absolute returns in rising equity markets.

Almost 85% of the Fund's listed equities are managed internally with the majority of these in low cost, low turnover strategies, which are expected to enhance the Fund's risk-adjusted returns over the long term. The Fund also hedges exposures to the currencies of overseas listed equities with the explicit aim of reducing volatility rather than seeking to generate improved returns. The Fund therefore maintains exposure to currencies that are expected to reduce volatility, such as the US Dollar and Japanese Yen which tend to fall as equities rise, and hedges exposure to currencies that are expected to increase volatility, such as the Australian Dollar which tends to rise as equities rise.

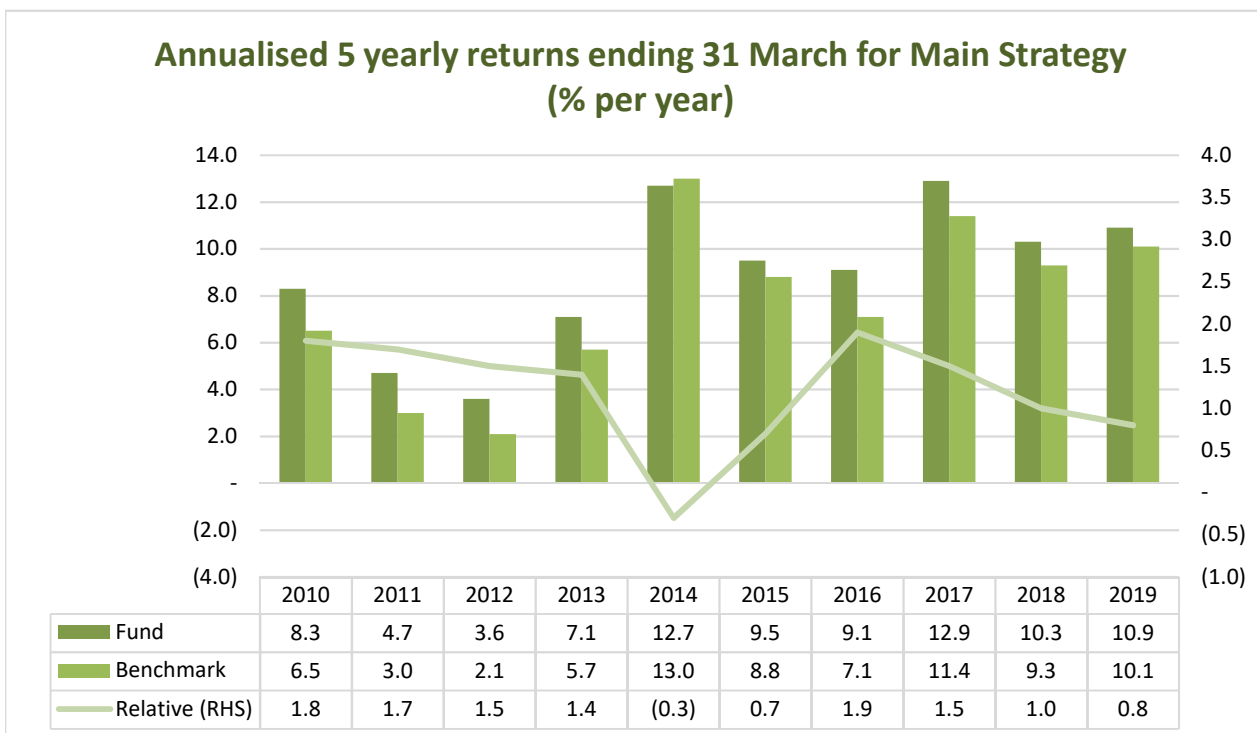
Investment performance

The Fund's performance over the last year and over longer-term timeframes is shown in the table below.

| Annualised returns to 31 March 2019 (% per year) | 1 year | 5 year | 10 years |
|-----------------------------------------------------|--------|--------|----------|
| Lothian Pension Fund - Main Strategy | 9.6 | 10.9 | 11.8 |
| Benchmark* | 9.1 | 10.1 | 11.5 |
| Lothian Pension Fund - Mature Employers Strategy | 4.9 | - | - |
| Benchmark | 4.6 | - | - |
| Retail Price Index (RPI) | 2.5 | 2.3 | 3.0 |
| Consumer Price Index (CPI) | 2.0 | 1.4 | 2.2 |

*Comprises equity, index-linked gilts and cash indices as well as an inflation-linked index for the alternatives allocation

**estimated



The objectives of the Fund are:

- over long-term economic cycles (typically 5 years or more) the achievement of the same return as that generated by the strategic allocation
- over shorter periods, the Fund should perform better than the strategic allocation if markets fall significantly.

The performance of the Mature Employers Strategy was broadly in line with benchmark over the year, returning +4.9%. Performance of this strategy has also been broadly in line with benchmark since inception (29 March 2016), with a return of +8.4% per annum.

The Fund's return has exceeded its objective of meeting the benchmark return over the economic cycle, with both the 5 and 10 year return ahead of benchmark. The direction of the Fund's performance when markets are increasing and decreasing is one way of measuring volatility. The lower volatility objective and strategy for the Main Strategy was put in place in December 2013 and over this period market volatility has been relatively benign, for the most part. Nevertheless, performance since the change in structure (with the launch of the global low volatility equity portfolio and the shift from regional passive to active) indicates that the Fund is delivering returns with lower volatility than its benchmark.

For the Main Strategy, performance from March 2014 to March 2019 has been:

- better than the strategic allocation when markets fell (18 out of 60 months) with average performance of 0.41% better than the strategic benchmark and,
- marginally worse than the strategic allocation when markets were rising (42 out of 60 months) with average performance 0.09% behind the strategic benchmark.

Risk analysis also shows that the portfolio is positioned well if markets fall significantly.

Lothian Pension Fund

Fund Account for year ended 31 March 2019

This statement shows a summary of the income and expenditure that the Pension Fund has generated and consumed in delivering the Local Government Pension Scheme. Included are employers' and employees' contributions and investment income, as well as the cost of providing benefits and administration of the Fund.

| Lothian Pension Fund | | | Lothian Pension Fund | |
|-------------------------------|------------------|--------------------------------------------------------------|----------------------|------------------|
| Parent | Group | | Parent | Group |
| Restated | Restated | | | |
| 2017/18 | 2017/18 | | 2018/19 | 2018/19 |
| £000 | £000 | Note | £000 | £000 |
| Income | | | | |
| 156,402 | 156,402 | Contributions from employers | 175,672 | 175,672 |
| 45,409 | 45,409 | Contributions from members | 47,416 | 47,416 |
| 4,204 | 4,204 | Transfers from other schemes | 3,852 | 3,852 |
| 206,015 | 206,015 | | 226,940 | 226,940 |
| Less: expenditure | | | | |
| 158,139 | 158,139 | Pension payments including increases | 167,997 | 167,997 |
| 45,117 | 45,117 | Lump sum retirement payments | 50,270 | 50,270 |
| 6,642 | 6,642 | Lump sum death benefits | 5,542 | 5,542 |
| 600 | 600 | Refunds to members leaving service | 720 | 720 |
| 129 | 129 | Premiums to State Scheme | (82) | (82) |
| 13,174 | 13,174 | Transfers to other schemes | 13,028 | 13,028 |
| 2,049 | 2,250 | Administrative expenses | 2,283 | 2,532 |
| 225,850 | 226,051 | | 239,758 | 240,007 |
| (19,835) | (20,036) | Net (withdrawals)/additions from dealing with members | (12,818) | (13,067) |
| Returns on investments | | | | |
| 171,948 | 171,948 | Investment income | 190,975 | 190,975 |
| (25,539) | (25,539) | Change in market value of investments | 503,734 | 503,734 |
| (35,067) | (35,685) | Investment management expenses | (35,938) | (36,102) |
| 111,342 | 110,724 | Net returns on investments | 658,771 | 658,607 |
| 91,507 | 90,688 | Net increase in the Fund during the year | 645,953 | 645,540 |
| 7,083,573 | 7,083,034 | Net assets of the Fund at 1 April 2018 | 7,175,080 | 7,173,722 |
| 7,175,080 | 7,173,722 | Net assets of the Fund at 31 March 2019 | 7,821,033 | 7,819,262 |

Lothian Pension Fund

Net Assets Statement as at 31 March 2019

This statement provides a breakdown of type and value of all net assets at the year end.

| Lothian Pension Fund | | | | Lothian Pension Fund | |
|----------------------|------------------|-------------------------------------------|-----------|----------------------|------------------|
| Parent | Group | | | Parent | Group |
| Restated | Restated | | | | |
| 31 March | 31 March | | | 31 March | 31 March |
| 2018 | 2018 | | | 2019 | 2019 |
| £000 | £000 | Investments | Note | £000 | £000 |
| 7,139,849 | 7,139,849 | Assets | | 7,790,671 | 7,790,671 |
| (5,362) | (5,362) | Liabilities | | (1,912) | (1,912) |
| 7,134,487 | 7,134,487 | Net investment assets | 14 | 7,788,759 | 7,788,759 |
| | | Non current assets | | | |
| 1,525 | 1,525 | Debtors | 24 | 3,457 | 3,457 |
| 168 | 168 | Computer systems | | 430 | 430 |
| 60 | - | Share Capital | | 60 | - |
| - | 292 | Deferred tax | 29a | - | 393 |
| 1,753 | 1,985 | | | 3,947 | 4,280 |
| | | Current assets | | | |
| 3,083 | 3,083 | The City of Edinburgh Council | 28 | 884 | 884 |
| 48,833 | 48,926 | Cash balances | 21, 28 | 35,897 | 36,238 |
| 16,406 | 16,476 | Debtors | 25 | 22,345 | 22,568 |
| 68,322 | 68,485 | | | 59,126 | 59,690 |
| | | Non current liabilities | | | |
| - | (1,715) | Retirement benefit obligation | 30 | - | (2,309) |
| - | - | Creditors | | - | (13) |
| - | (1,715) | | | - | (2,322) |
| | | Current liabilities | | | |
| (29,482) | (29,520) | Creditors | 26 | (30,799) | (31,145) |
| (29,482) | (29,520) | | | (30,799) | (31,145) |
| 7,175,080 | 7,173,722 | Net assets of the Fund at 31 March | | 7,821,033 | 7,819,262 |

The unaudited accounts were issued on 26 June 2019 and the audited accounts were authorised for issue on 25 September 2019.

JOHN BURNS FCMA CGMA, PgC
Chief Finance Officer, Lothian Pension Fund
25 September 2019

Notes to the net asset statement

The financial statements summarise the transactions of the Fund during the year and its net assets at the year end. They do not take account of the obligations to pay pensions and benefits which fall due after the end of the year. The actuarial position of the Fund, which does take account of such obligations, is discussed in the Actuarial Valuation section of this report and these financial statements should be read in conjunction with that information. In addition, as required by IAS26, the Actuarial Present Value of Promised Retirement Benefits is disclosed in the notes to these financial statements.

Notes to the Financial Statements

1 Statement of Accounting Policies

The statement of accounting policies for all Funds can be found on page 105.

2 Prior Year Restatement of Financial Statements

At its meeting on 26 March 2018, the Pensions Committee approved the merger of the assets and liabilities of the Lothian Buses Pension Fund into the Lothian Pension Fund, subject to the satisfactory completion of a revised admission agreement and shareholder guarantees. Having received the necessary admission agreement and shareholder guarantees, the Lothian Buses Pension Fund assets were merged into Lothian Pension Fund on 1 February 2019.

As per the statement of accounting policies on page 106, the Fund has deemed the most appropriate treatment for the transfer of assets is 'transfer by merger'. This requires a restatement of 2017/18 financial figures of Lothian Pension Fund to include Lothian Buses Pension Fund assets for the same period.

The analysis below demonstrates the impact of merging Lothian Buses Pension Fund assets and liabilities in to Lothian Pension Fund Parent and Group Fund Account and Net Asset Statement for the 2017/18 financial period.

| Lothian Pension Fund Parent 2017/18 £000 | | Lothian Pension Fund Group 2017/18 £000 | | Lothian Buses 2017/18 £000 | | RESTATED Lothian Pension Fund Parent 2017/18 £000 | | RESTATED Lothian Pension Fund Group 2017/18 £000 | |
|---------------------------------------------|------------------|--------------------------------------------|--|-------------------------------|--|---------------------------------------------------------|------------------|--------------------------------------------------------|--|
| Income | | | | | | | | | |
| 148,821 | 148,821 | 7,581 | | | | 156,402 | 156,402 | | |
| 43,421 | 43,421 | 1,988 | | | | 45,409 | 45,409 | | |
| 4,191 | 4,191 | 13 | | | | 4,204 | 4,204 | | |
| 196,433 | 196,433 | 9,582 | | | | 206,015 | 206,015 | | |
| Less: expenditure | | | | | | | | | |
| 149,384 | 149,384 | 8,755 | | | | 158,139 | 158,139 | | |
| 42,533 | 42,533 | 2,584 | | | | 45,117 | 45,117 | | |
| 6,359 | 6,359 | 283 | | | | 6,642 | 6,642 | | |
| 596 | 596 | 4 | | | | 600 | 600 | | |
| 129 | 129 | - | | | | 129 | 129 | | |
| 12,517 | 12,517 | 657 | | | | 13,174 | 13,174 | | |
| 1,950 | 2,151 | 99 | | | | 2,049 | 2,250 | | |
| 213,468 | 213,669 | 12,382 | | | | 225,850 | 226,051 | | |
| (17,035) | (17,236) | (2,800) | | | | (19,835) | (20,036) | | |
| Returns on investments | | | | | | | | | |
| 163,869 | 163,869 | 8,079 | | | | 171,948 | 171,948 | | |
| (43,288) | (43,288) | 17,749 | | | | (25,539) | (25,539) | | |
| (32,643) | (33,261) | (2,424) | | | | (35,067) | (35,685) | | |
| 87,938 | 87,320 | 23,404 | | | | 111,342 | 110,724 | | |
| 70,903 | 70,084 | 20,604 | | | | 91,507 | 90,688 | | |
| 6,595,430 | 6,594,891 | 488,143 | | | | 7,083,573 | 7,083,034 | | |
| 6,666,333 | 6,664,975 | 508,747 | | | | 7,175,080 | 7,173,722 | | |

Notes to the Financial Statements

3 Lothian Pension Fund Group (cont)

| Note | Description |
|------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 28 | Related party transactions and balances Describes transactions during the year and balances at year end which relate to the parent and the companies. |
| 29a | Consolidated Lothian Pension Fund group - LPFE Limited - deferred tax Describes the deferred tax non-current asset of the Company. See 2 f) ii) in the Statement of Accounting Policies and General notes for more information. |
| 29b | Consolidated Lothian Pension Fund group - LPFE Limited and LPFI Limited - share capital Describes the share capital of the Company. |
| 30 | Retirement benefits obligation - group Provides the information on the retirement benefits obligation of the Company as required under IAS19 - Employee Benefits. See 2 q) ii) in the Statement of Accounting Policies and General notes for more information. |

Prior to the consolidation of the group accounts, the LPFE and LPFI boards met on the 21st May 2019 and approved their respective audited financial statements for 2018/19. The figures used in the consolidation are from these audited financial statements.

4 Events after the Reporting Date

There have been no events since 31 March 2019, and up to the date when these accounts were authorised, that require any adjustments to these accounts.

5 Contributions from employers

The total contributions receivable for the administering authority, other scheduled bodies and admitted bodies were as follows:-

| By category | 2017/18* £000 | 2018/19 £000 |
|-----------------------------------------------|------------------|-----------------|
| Primary Contribution (future service) | 144,549 | 160,778 |
| Secondary Contribution (past service deficit) | 7,694 | 8,057 |
| Strain costs | 2,747 | 4,082 |
| Cessation contributions | 1,412 | 2,755 |
| | 156,402 | 175,672 |

| By employer type | 2017/18* £000 | 2018/19 £000 |
|-----------------------------|------------------|-----------------|
| Administering Authority | 55,041 | 59,830 |
| Other Scheduled Bodies | 81,273 | 92,644 |
| Community Admission Bodies | 19,629 | 22,414 |
| Transferee Admission Bodies | 459 | 784 |
| | 156,402 | 175,672 |

Notes to the Financial Statements

5 Contributions from employers (cont)

Employer contributions, as calculated by the Fund Actuary, comprise two elements:

- An estimate of the cost of benefits accruing in the future, referred to as the "primary contribution rate" previously referred to as the "future service rate", which is expressed as a percentage of payroll and;
- an adjustment for the solvency of the Fund based on the benefits already accrued, known as the "secondary contribution rate". If there is a surplus, there may be a contribution reduction; if there is a deficit there may be a contribution increase. For all employers, contributions to cover any Past Service Deficit are expressed as a fixed monetary sum, rather than as a percentage of payroll and are payable on a monthly basis that is one twelfth of the annual total.

Included within the above contributions are accruals for:

- receipt of six months past service deficit for Scottish Learning Partnership (SLP) of £24k. The Fund continues to pursue these payments, whilst noting that the Scottish Government has indicated that it expects to sign as guarantor for SLP liabilities.
- City of Edinburgh Council has advised the Fund of revised sums in respect of assumed pensionable pay. £107k has been accrued covering payments due in the financial period 2015/16 to 2017/18. These payments will be transferred to the Fund in the first quarter of 2019/20.

Where an employer makes certain decisions which result in benefits being paid early, this results in a "strain" on the Fund. The resulting pension strain costs are calculated and recharged in full to that employer.

Any employer that ceases to have at least one actively contributing member is required to pay cessation contributions.

6 Contributions from members

| By employer type | 2017/18* £000 | 2018/19 £000 |
|-----------------------------|------------------|-----------------|
| Administering Authority | 15,633 | 16,437 |
| Other Scheduled Bodies | 23,463 | 24,507 |
| Community Admission Bodies | 6,161 | 6,217 |
| Transferee Admission Bodies | 152 | 255 |
| | 45,409 | 47,416 |

7 Transfers in from other pension schemes

| | 2017/18* £000 | 2018/19 £000 |
|----------------------|------------------|-----------------|
| Group transfers | - | - |
| Individual transfers | 4,204 | 3,852 |
| | 4,204 | 3,852 |

Notes to the Financial Statements

8 Pensions payable

| By employer type | 2017/18* £000 | 2018/19 £000 |
|-----------------------------|------------------|-----------------|
| Administering Authority | 73,922 | 76,932 |
| Other Scheduled Bodies | 70,484 | 75,860 |
| Community Admission Bodies | 13,537 | 14,993 |
| Transferee Admission Bodies | 196 | 212 |
| | 158,139 | 167,997 |

Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998 [Section 31] allows employers to pay additional pensions on a voluntary basis.

As is typical within the Local Government Pension Schemes (LGPS), arrangements exist whereby additional teachers' pensions and employee pensions are paid with the payment of funded pensions. In order that such are not regarded as "unauthorised payments" by HMRC, these pension payments are met by the administering authority through a general fund bank account and recharged to the body or service which granted the benefits.

As "unfunded payments" are discretionary benefits, they are not relevant to the sums disclosed in the Fund accounts. As such, Lothian Pension Fund provides payment and billing services to certain employers on a no charge agency agreement basis.

The Fund has requested that responsibility for these "unfunded transfer payments" should transfer to the Scottish Public Pension's Agency (SPPA). A response from SPPA is awaited.

9 Lump sum retirement benefits payable

| By employer type | 2017/18* £000 | 2018/19 £000 |
|-----------------------------|------------------|-----------------|
| Administering Authority | 16,623 | 17,374 |
| Other Scheduled Bodies | 23,234 | 27,818 |
| Community Admission Bodies | 5,131 | 5,053 |
| Transferee Admission Bodies | 129 | 25 |
| | 45,117 | 50,270 |

10 Lump sum death benefits payable

| By employer type | 2017/18* £000 | 2018/19 £000 |
|-----------------------------|------------------|-----------------|
| Administering Authority | 3,375 | 2,943 |
| Other Scheduled Bodies | 2,854 | 2,049 |
| Community Admission Bodies | 413 | 550 |
| Transferee Admission Bodies | - | - |
| | 6,642 | 5,542 |

Notes to the Financial Statements

11 Transfers out to other pension schemes

| | 2017/18* | 2018/19 |
|----------------------|----------|---------|
| | £000 | £000 |
| Group transfers | - | - |
| Individual transfers | 13,174 | 13,028 |
| | 13,174 | 13,028 |

12a Total management expenses

In accordance with CIPFA guidance, the analysis below considers the combined administration and investment management expenses in notes 12b and c and splits out the costs to include a third category covering oversight and governance expenditure.

| | LPF Parent 2017/18* £000 | LPF Group 2017/18* £000 | LPF Parent 2018/19 £000 | LPF Group 2018/19 £000 |
|--------------------------------|-----------------------------------|----------------------------------|----------------------------------|---------------------------------|
| Administrative costs | 1,693 | 1,879 | 1,988 | 2,176 |
| Investment management expenses | 33,943 | 34,241 | 34,422 | 34,629 |
| Oversight and governance costs | 1,481 | 1,815 | 1,811 | 1,829 |
| | 37,117 | 37,935 | 38,221 | 38,634 |

12b Administrative expenses

| | LPF Parent 2017/18* £000 | LPF Group 2017/18* £000 | LPF Parent 2018/19 £000 | LPF Group 2018/19 £000 |
|--------------------------------------------------------------|-----------------------------------|----------------------------------|----------------------------------|---------------------------------|
| Employee Costs | 1,198 | 1,222 | 1,494 | 1,540 |
| System costs | 306 | 307 | 304 | 305 |
| Actuarial fees | 127 | 127 | 72 | 72 |
| External/Internal audit fees | 68 | 74 | 49 | 52 |
| Legal fees | 2 | 2 | 20 | 20 |
| Printing and postage | 120 | 120 | 111 | 111 |
| Depreciation | 60 | 60 | 45 | 45 |
| Office costs | 107 | 107 | 100 | 100 |
| Sundry costs less sundry income | 61 | 60 | 88 | 73 |
| IAS19 retirement benefit adjustments - see note 30 | - | 206 | - | 249 |
| Deferred tax on retirement benefit obligation - see note 29a | - | (35) | - | (42) |
| Corporation tax | - | - | - | 6 |
| | 2,049 | 2,250 | 2,283 | 2,531 |

LPFE, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer the pension funds. The Fund has a service level agreement in place with the Council for certain support services. Costs directly attributable to a specific Fund are charged to the relevant Fund, costs that are common to the two Funds are allocated on a defined basis.

Notes to the Financial Statements

12c Investment management expenses

| | LPF Parent 2017/18* £000 | LPF Group 2017/18* £000 | LPF Parent 2018/19 £000 | LPF Group 2018/19 £000 |
|-------------------------------------------------------------|-----------------------------------|----------------------------------|----------------------------------|---------------------------------|
| External management fees - | | | | |
| invoiced | 4,931 | 4,931 | 4,977 | 4,977 |
| deducted from capital (direct investment) | 19,777 | 19,777 | 17,657 | 17,657 |
| deducted from capital (indirect investment) | 5,912 | 5,912 | 5,062 | 5,062 |
| Securities lending fees | 191 | 191 | 189 | 189 |
| Transaction costs - Equities | 1,207 | 1,207 | 1,498 | 1,498 |
| Property operational costs | 337 | 337 | 2,615 | 2,615 |
| Employee costs | 1,368 | 1,471 | 2,075 | 2,165 |
| Custody fees | 396 | 396 | 356 | 356 |
| Engagement and voting fees | 93 | 93 | 114 | 114 |
| Performance measurement fees | 85 | 85 | 92 | 92 |
| Consultancy fees | 52 | 52 | 125 | 125 |
| Research fees | 65 | 65 | 329 | 329 |
| System costs | 322 | 323 | 441 | 442 |
| Legal fees | 71 | 99 | 134 | 137 |
| Depreciation | 8 | 8 | 16 | 16 |
| Office costs | 84 | 84 | 76 | 76 |
| Sundry costs less sundry income | 168 | (38) | 182 | (57) |
| IAS19 retirement benefit adjustments - see note 30 | - | 824 | - | 345 |
| Deferred tax on retirement benefit obligation - see note 29 | - | (140) | - | (59) |
| Corporation tax | - | - | - | 23 |
| Corporation tax losses utilised by CEC group | - | 8 | - | - |
| | 35,067 | 35,685 | 35,938 | 36,102 |

Investment costs directly attributable to a specific fund are charged to the relevant Fund, costs that are common to all three funds are allocated based on the value of the Funds as at the year end.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions or in the proceeds of investment sales (see note 15 - Reconciliation of movements in investments and derivatives).

The external investment management fees (deducted from capital) above include £8.5m (£6.1m direct, £2.4m indirect) in respect of performance-related fees compared to £9.4m in 2017/18 (£7.1m direct, £2.3m indirect).

It should be noted that Lothian Pension Fund's disclosure on investment management fees exceed CIPFA's "Accounting for Local Government Pension Scheme Management Costs" revised guidance on cost transparency which came into effect from 1st April 2016. Consistent with previous years, the Fund recognises fees deducted from investments not within its direct control (such as fund of fund fees) to give a full picture of its investment management costs. Further details can be found on page 31. This further disclosure highlights an extra £5.1m in costs (2018 £5.9m).

Notes to the Financial Statements

13 Investment income

| | 2017/18* £000 | 2018/19 £000 |
|--------------------------------------------|------------------|-----------------|
| Income from bonds | 4,267 | 11,622 |
| Dividends from equities | 138,584 | 152,814 |
| Unquoted private equity and infrastructure | 7,601 | 5,005 |
| Income from pooled investment vehicles | 6,207 | 2,432 |
| Gross rents from properties | 23,079 | 23,501 |
| Interest on cash deposits | 708 | 2,156 |
| Stock lending and sundries | 957 | 943 |
| | 181,403 | 198,473 |
| Irrecoverable withholding tax | (9,455) | (7,498) |
| | 171,948 | 190,975 |

Included within the dividend from equities income for the year is cross border withholding tax yet to be received. The Fund's custodian Northern Trust manages this process and due to the high certainty of success it is assumed that the Fund will make full recovery of these reclaims. For the period of 2018/19 £4,526k of the stated income relates to tax yet to be received. At the 31st March 2019 £9,066k (including prior periods) of investment income receivable related to cross border withholding tax. The Fund monitors these claims to ensure its optimum tax efficiency and provides an annual progress report to the Pensions Audit Sub-Committee.

Notes to the Financial Statements

14 Net investment assets

| | Region | 31 March 2018* | 31 March 2019 |
|-------------------------------------------------------|----------|----------------|---------------|
| Investment Assets | | £000 | £000 |
| Bonds | | | |
| Public sector fixed interest | UK | 153,585 | 158,219 |
| Public sector index linked gilts quoted | UK | 582,893 | 697,211 |
| | | 736,478 | 855,430 |
| Equities | | | |
| Quoted | UK | 557,735 | 641,038 |
| Quoted | Overseas | 3,729,729 | 3,918,803 |
| | | 4,287,464 | 4,559,841 |
| Pooled investment vehicles | | | |
| Private equity, infrastructure, private debt & timber | UK | 527,172 | 616,556 |
| Private equity, infrastructure, private debt & timber | Overseas | 597,899 | 633,487 |
| Property | UK | 108,125 | 90,358 |
| Other | UK | 31,357 | 31,978 |
| | | 1,264,553 | 1,372,379 |
| Properties | | | |
| Direct property | UK | 392,743 | 411,978 |
| | | 392,743 | 411,978 |
| Derivatives | | | |
| Derivatives - forward foreign exchange | | 12,121 | 3,025 |
| | | 12,121 | 3,025 |
| Cash deposits | | | |
| Deposits | | 426,380 | 569,190 |
| | | 426,380 | 569,190 |
| Other investment assets | | | |
| Due from broker | | 2,947 | 1,037 |
| Dividends and other income due | | 17,163 | 17,791 |
| | | 20,110 | 18,828 |
| Total investment assets | | 7,139,849 | 7,790,671 |
| Investment liabilities | | | |
| Derivatives | | | |
| Derivatives - forward foreign exchange | | (204) | (854) |
| | | (204) | (854) |
| Other financial liabilities | | | |
| Due to broker | | (5,158) | (1,058) |
| | | (5,158) | (1,058) |
| Total investment liabilities | | (5,362) | (1,912) |
| Net investment assets | | 7,134,487 | 7,788,759 |

Notes to the Financial Statements

15a Reconciliation of movement in investments and derivatives

| | Market value at 31 March 2018* £000 | Purchases at cost & derivative payments £000 | Sale & derivative receipts £000 | Change in market value £000 | Market value at 31 March 2019 £000 |
|---------------------------------------------|----------------------------------------|-------------------------------------------------|------------------------------------|--------------------------------|---------------------------------------|
| Bonds | 736,478 | 227,909 | (150,897) | 41,940 | 855,430 |
| Equities | 4,287,464 | 1,090,848 | (1,122,578) | 304,107 | 4,559,841 |
| Pooled investment vehicles | 1,264,553 | 219,829 | (261,125) | 149,122 | 1,372,379 |
| Property | 392,743 | 21,290 | - | (2,055) | 411,978 |
| Derivatives - futures | - | 30 | (30) | - | - |
| Derivatives - forward foreign exchange | 11,917 | 8,223 | (12,199) | (5,770) | 2,171 |
| | 6,693,155 | 1,568,129 | (1,546,829) | 487,344 | 7,201,799 |
| Other financial assets / liabilities | | | | | |
| Cash deposits* | 426,380 | | | 16,376 | 569,190 |
| Broker balances* | (2,211) | | | 14 | (21) |
| Investment income due* | 17,163 | | | - | 17,791 |
| | 441,332 | | | 16,390 | 586,960 |
| Net financial assets | 7,134,487 | | | 503,734 | 7,788,759 |

The change in market value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions and in the proceeds from sales and are therefore included in the tables above.

| | Market value at 31 March 2017* £000 | Purchases at cost & derivative payments £000 | Sale & derivative receipts £000 | Change in market value £000 | Market value at 31 March 2018* £000 |
|---------------------------------------------|----------------------------------------|-------------------------------------------------|------------------------------------|--------------------------------|----------------------------------------|
| Bonds | 732,628 | 42,200 | (39,305) | 955 | 736,478 |
| Equities | 4,494,078 | 907,719 | (962,127) | (152,206) | 4,287,464 |
| Pooled investment vehicles | 1,223,996 | 70,066 | (149,092) | 119,583 | 1,264,553 |
| Property | 356,741 | 40,758 | (17,329) | 12,573 | 392,743 |
| Derivatives - futures | - | 11 | 163 | (174) | - |
| Derivatives - forward foreign exchange | 657 | 2,983 | (3,722) | 11,999 | 11,917 |
| | 5,141,969 | 1,063,737 | (1,171,412) | (7,270) | 6,693,155 |
| Other financial assets / liabilities | | | | | |
| Cash deposits* | 432,072 | | | (18,272) | 426,380 |
| Broker balances* | (852) | | | 3 | (2,211) |
| Investment income due* | 29,042 | | | - | 17,163 |
| | 256,994 | | | (18,269) | 441,332 |
| Net financial assets | 5,398,963 | | | (25,539) | 7,134,487 |

* As per CIPFA disclosures the change in market value intentionally does not balance opening/closing market values

Notes to the Financial Statements

15d Reconciliation of fair value measurements within level 3

| | Market value at 31 March 2018* | Level 3 transfers | | Purchases at cost & derivative payments | Sales & derivative receipts | Unrealised gains / (losses) | Realised gains / (losses) | Market value at 31 March 2019 |
|---------------------------|--------------------------------|-------------------|-----|-----------------------------------------|-----------------------------|-----------------------------|---------------------------|-------------------------------|
| | | in | out | | | | | |
| Pooled investments | | | | | | | | |
| Infrastructure | 773,193 | - | - | 136,416 | (137,747) | 32,426 | 40,572 | 844,860 |
| Property | 66,638 | - | - | - | (15,891) | (1,611) | (153) | 48,983 |
| Private Equity | 90,403 | - | - | 2,283 | (26,834) | 18,669 | (8,362) | 76,159 |
| Timber | 118,235 | - | - | 579 | (14,724) | 11,044 | 8,894 | 124,028 |
| Private debt | 143,245 | - | - | 80,893 | (21,155) | (95) | 2,108 | 204,996 |
| - | - | - | - | - | - | - | - | - |
| Freehold Property | 392,743 | - | - | 21,290 | - | (2,055) | - | 411,978 |
| | 1,584,457 | - | - | 241,461 | (216,351) | 58,378 | 43,059 | 1,711,004 |

Unrealised and realised gains and losses are recognised in the profit and losses on disposal and changes in the market value of investments line of the fund account.

16 Derivatives - forward foreign exchange

Summary of contracts held at 31 March 2019

| Contract settlement within | Currency bought | Currency sold | Local currency bought 000 | Local currency sold 000 | Asset value £000 | Liability value £000 |
|----------------------------|-----------------|---------------|------------------------------|----------------------------|---------------------|-------------------------|
| Up to one month | GBP | AUD | 49,327 | 91,691 | 59 | (702) |
| Up to one month | CAD | GBP | 12,909 | 7,565 | - | (152) |
| Up to one month | GBP | CAD | 142,170 | 242,817 | 2,720 | - |
| Up to one month | USD | JPY | 253 | 28,011 | - | - |
| Up to one month | GBP | JPY | 26 | 3,800 | - | - |
| Up to one month | USD | ZAR | 531 | 7,661 | - | - |
| One to six months | USD | CHF | 7,393 | 6,991 | 246 | - |

Open forward currency contracts at 31 March 2019

| | |
|-------|-------|
| 3,025 | (854) |
|-------|-------|

Net forward currency contracts at 31 March 2019

| |
|-------|
| 2,171 |
|-------|

Prior year comparative

Open forward currency contracts at 31 March 2018*

| | |
|--------|-------|
| 12,121 | (204) |
|--------|-------|

Net forward currency contracts at 31 March 2018

| |
|--------|
| 11,917 |
|--------|

The above table summarises the contracts held by maturity date, all contracts are traded on an over-the-counter basis.

In order to maintain appropriate diversification of investments in the portfolio and take advantage of wider opportunities, the Lothian Pension Fund invests over half of the fund in overseas markets. A currency hedging programme, using forward foreign exchange contracts, has been put in place to reduce the extent to which the Fund is exposed to certain currency movements.

Notes to the Financial Statements

17 Investment managers and mandates

| Manager | Mandate | Market value at 31 March 2018* £000 | % of total 31 March 2018 % | Market value at 31 March 2019 £000 | % of total 31 March 2019 % |
|-----------------------------------------|---------------------------|----------------------------------------|-------------------------------|---------------------------------------|-------------------------------|
| In-house | UK all cap equities | 139,655 | 2.0 | 144,692 | 1.9 |
| In-house | UK mid cap equities | 131,607 | 1.8 | 121,698 | 1.6 |
| Total UK equities | | 271,262 | 3.8 | 266,390 | 3.5 |
| In-house | European ex UK equities | 130,696 | 1.8 | 125,418 | 1.6 |
| In-house | US equities | 146,279 | 2.3 | 160,148 | 2.1 |
| Total regional overseas equities | | 276,975 | 4.1 | 285,566 | 3.7 |
| In-house | Global high dividend | 988,159 | 13.9 | 1,006,587 | 12.9 |
| In-house | Global low volatility | 1,097,057 | 17.7 | 1,249,276 | 16.1 |
| In-house | Global multi factor value | 934,708 | 15.0 | 993,535 | 12.8 |
| Harris | Global equities | 273,298 | 3.8 | 278,794 | 3.6 |
| Nordea | Global equities | 268,444 | 3.8 | 306,617 | 3.9 |
| Baillie Gifford | Global equities | 141,217 | 2.0 | 123,103 | 1.6 |
| Total global equities | | 3,702,883 | 56.1 | 3,957,912 | 50.9 |
| In-house | Currency hedge | 11,885 | 0.2 | 1,925 | - |
| Total currency overlay | | 11,885 | 0.2 | 1,925 | - |
| Total listed equities | | 4,263,005 | 64.2 | 4,511,793 | 58.1 |
| In-house | Private equity unquoted | 90,403 | 1.3 | 76,159 | 1.0 |
| In-house | Private equity quoted | 67,490 | 0.9 | 78,382 | 1.0 |
| Total private equity | | 157,893 | 3.2 | 154,541 | 2.0 |
| Total equity | | 4,420,898 | 67.4 | 4,666,334 | 60.1 |
| In-house | Index linked gilts | 530,560 | 7.4 | 595,360 | 7.6 |
| In-house | Mature employer gilts | 54,571 | 0.8 | 116,095 | 1.5 |
| Total inflation linked assets | | 585,131 | 7.4 | 711,455 | 9.1 |
| In-house | Property | 37,447 | 0.5 | 35,421 | 0.5 |
| Standard Life | Property | 495,917 | 7.0 | 516,767 | 6.6 |
| Total property | | 533,364 | 7.5 | 552,188 | 7.1 |
| In-house | Infrastructure unquoted | 773,194 | 10.8 | 844,860 | 10.8 |
| In-house | Infrastructure quoted | 21,931 | 0.3 | 24,819 | 0.3 |
| In-house | Timber | 118,235 | 1.7 | 124,029 | 1.6 |
| Total other real assets | | 913,360 | 12.8 | 993,708 | 12.7 |
| Baillie Gifford | Corporate bonds | 30,490 | 0.4 | 31,835 | 0.4 |
| In-house | Private debt | 143,245 | 2.0 | 204,996 | 2.6 |
| In-house | Sovereign bonds | 158,280 | 2.2 | 165,183 | 2.1 |
| Total debt assets | | 332,015 | 4.7 | 402,014 | 5.1 |

Notes to the Financial Statements

17 Investment managers and mandates (cont)

| | | Market value at 31 March 2018 £000 | % of total 31 March 2017 % | Market value at 31 March 2019 £000 | % of total 31 March 2018 % |
|--------------------------------|-------------|---------------------------------------------|-------------------------------------|------------------------------------------|-------------------------------------|
| Manager | Mandate | | | | |
| In-house | Cash | 348,105 | 4.9 | 462,976 | 5.9 |
| In-house | Transitions | 1,614 | 0.0 | 84 | 0.0 |
| Total cash and sundries | | 349,719 | 4.9 | 463,060 | 5.9 |
| Net financial assets | | 7,134,487 | 100.0 | 7,788,759 | 100.0 |

Over the last two years no single investment represented more than 5% of the net assets of the Fund.

18 Securities lending

During the year Lothian Pension Fund participated in a securities lending arrangement with the Northern Trust Company. As at 31 March 2019, £407.2m (2018 £271.7m) of securities were released to third parties. Collateral valued at 107.3% (2018 105.5%) of the market value of the securities on loan was held at that date.

19 Property holdings

| | 2017/18 £000 | 2018/19 £000 |
|----------------------------|-----------------|-----------------|
| Opening balance | 356,741 | 392,743 |
| Additions | 40,875 | 21,290 |
| Disposals | (17,329) | - |
| Net change in market value | 12,456 | (2,055) |
| Closing balance | 392,743 | 411,978 |

As at 31 March 2019, there were no restrictions on the realisability of the property or the remittance of income or sale proceeds. As at 31 March 2018 The Fund had approval in place for the planning, design and contractor procurement to potentially re-develop 100 St John Street, London. During the year this has progressed and the Fund is currently in the process of developing 100 St John Street, London. As at 31 March 2019 the Fund is contractually obliged to further construction costs of £4.8m

The future minimum lease payments receivable by the Fund are as follows

| | 2017/18 £000 | 2018/19 £000 |
|----------------------------|-----------------|-----------------|
| Within one year | 23,327 | 23,257 |
| Between one and five years | 66,574 | 58,867 |
| Later than five years | 101,160 | 92,633 |
| | 191,061 | 174,757 |

Notes to the Financial Statements

20 Financial Instruments

20a Classification of financial instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the fair value amounts of financial assets and liabilities by category and net assets statement heading. No financial assets were reclassified during the accounting period.

All financial instruments are marked to market (at fair value) in the Fund accounting records, hence there is no difference between the carrying value and fair value.

| Classification of financial instruments - parent | 31 March 2018 | | | 31 March 2019 | | |
|--------------------------------------------------|-----------------------------------------------|-----------------------|-----------------------------------------|-----------------------------------------------|-----------------------|-----------------------------------------|
| | Designated as fair value through fund account | Loans and receivables | Financial liabilities at amortised cost | Designated as fair value through fund account | Loans and receivables | Financial liabilities at amortised cost |
| | £000 | £000 | £000 | £000 | £000 | £000 |
| Investment assets | | | | | | |
| Bonds | 736,477 | - | - | 855,430 | - | - |
| Equities | 4,287,464 | - | - | 4,559,841 | - | - |
| Pooled investments | 1,264,553 | - | - | 1,372,379 | - | - |
| Property Leases | 4,376 | - | - | 2,284 | - | - |
| Derivative contracts | 12,121 | - | - | 3,025 | - | - |
| Margin balances | - | - | - | - | - | - |
| Cash | - | 426,380 | - | - | 569,189 | - |
| Other balances | - | 20,110 | - | - | 18,828 | - |
| | 6,304,991 | 446,490 | - | 6,792,959 | 588,017 | - |
| Other assets | | | | | | |
| City of Edinburgh Council | - | 3,083 | - | - | 884 | - |
| Cash | - | 48,833 | - | - | 35,897 | - |
| Share Capital | - | 60 | - | - | 60 | - |
| Debtors - current | - | 16,406 | - | - | 22,345 | - |
| Debtors - non-current | - | 1,525 | - | - | 3,457 | - |
| | - | 69,907 | - | - | 62,643 | - |
| Assets total | 6,304,991 | 516,397 | - | 6,792,959 | 650,660 | - |
| Financial liabilities | | | | | | |
| Investment liabilities | | | | | | |
| Derivative contracts | (204) | - | - | (854) | - | - |
| Other investment balances | - | - | (5,158) | - | - | (1,058) |
| | (204) | - | (5,158) | (854) | - | (1,058) |
| Other liabilities | | | | | | |
| Creditors | - | - | (29,482) | - | - | (30,799) |
| Liabilities total | (204) | - | (34,640) | (854) | - | (31,857) |
| Total net assets | 6,304,787 | 516,397 | (34,640) | 6,792,105 | 650,660 | (31,857) |
| Total net financial instruments | | | 6,786,544 | | | 7,410,908 |
| Amounts not classified as financial instruments | | | 388,536 | | | 410,125 |
| Total net assets - parent | | | 7,175,080 | | | 7,821,033 |

Notes to the Financial Statements

20a Classification of financial instruments (cont)

Classification of financial instruments - adjustments to parent to arrive at group

| | 31 March 2018 | | | 31 March 2019 | | |
|-------------------------------------------------------|--------------------------------------------------------|--------------------------|-----------------------------------------------|--------------------------------------------------------|--------------------------|-----------------------------------------------|
| | Designated as fair value through fund account | Loans and receivables | Financial liabilities at amortised cost | Designated as fair value through fund account | Loans and receivables | Financial liabilities at amortised cost |
| | £000 | £000 | £000 | £000 | £000 | £000 |
| Other assets | | | | | | |
| Cash | - | 93 | - | - | 341 | - |
| Share Capital | - | (60) | - | - | (60) | - |
| Debtors - current | - | 70 | - | - | 223 | - |
| Debtors - non-current | - | 292 | - | - | 393 | - |
| | - | 395 | - | - | 897 | - |
| Assets total | - | 395 | - | - | 897 | - |
| Other liabilities | | | | | | |
| Retire. benefit obligation | - | - | (1,715) | - | - | (2,309) |
| Creditors | - | - | (38) | - | - | (346) |
| Creditors - non current | - | - | - | - | - | (13) |
| Liabilities total | - | - | (1,753) | - | - | (2,668) |
| Total net assets | - | 395 | (1,753) | - | 897 | (2,668) |
| Total adjustments to net financial instruments | | | (1,358) | | | (1,771) |
| Total net assets - group | | | 7,173,722 | | | 7,819,262 |

20b Net gains and losses on financial instruments

| | 2017/18 £000 | 2018/19 £000 |
|---------------------------------------------------------------|-----------------|-----------------|
| Designated as fair value through fund account | (19,843) | 489,399 |
| Loans and receivables | (18,269) | 16,390 |
| Financial liabilities at amortised cost | - | - |
| Total | (38,112) | 505,789 |
| Gains and losses on directly held freehold property | 12,573 | (2,055) |
| Change in market value of investments per fund account | (25,539) | 503,734 |

Notes to the Financial Statements

20c Fair Value Hierarchy

The valuation of financial instruments has been classified into three levels, according to the quality and reliability of information used to determine fair values.

Level 1

Financial instruments at Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities and unit trusts.

Quoted investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Level 2

Financial instruments at Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3

Financial instruments at Level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data. Such instruments would include unquoted equity investments, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investments in unquoted private equity, infrastructure, timber and European real estate are based on valuations provided by the general partners to the funds in which the Fund has invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of International Financial Reporting Standards (IFRS). The valuations are typically undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

| | 31 March 2019 | | | Total £000 |
|------------------------------------------------------------|------------------|-----------------|------------------|------------------|
| | Level 1 £000 | Level 2 £000 | Level 3 £000 | |
| Investment assets | | | | |
| Designated as fair value through fund account | 4,563,196 | 928,453 | 1,299,026 | 6,790,675 |
| Non-financial assets at fair value through profit and loss | - | - | 411,978 | 411,978 |
| Total investment assets | 4,563,196 | 928,453 | 1,711,004 | 7,202,653 |
| Investment liabilities | | | | |
| Designated as fair value through fund account | - | (854) | - | (854) |
| Total investment liabilities | - | (854) | - | (854) |
| Net investment assets | 4,563,196 | 927,599 | 1,711,004 | 7,201,799 |

Notes to the Financial Statements

20c Fair Value Hierarchy

| | 31 March 2018 | | | |
|------------------------------------------------------------|------------------|-----------------|------------------|------------------|
| | Level 1 £000 | Level 2 £000 | Level 3 £000 | Total £000 |
| Investment assets | | | | |
| Designated as fair value through fund account | 4,372,429 | 736,477 | 1,197,953 | 6,306,859 |
| Non-financial assets at fair value through profit and loss | - | - | 386,500 | 386,500 |
| Total investment assets | 4,372,429 | 736,477 | 1,584,453 | 6,693,359 |
| Investment liabilities | | | | |
| Designated as fair value through fund account | - | (204) | - | (204) |
| Total investment liabilities | - | (204) | - | (204) |
| Net investment assets | 4,372,429 | 736,273 | 1,584,453 | 6,693,155 |

21 Nature and extent of risk arising from financial instruments

Risk and risk management

The Fund's primary aim is to ensure that all members and their dependants receive their benefits when they become payable. Investment strategy C aims to maximise the returns from investments within reasonable risk parameters and hence minimise the long-term cost to employers. It achieves this by investing in a diverse range of assets to reduce risk to an acceptable level. In addition, the Fund ensures that sufficient cash is available to meet all liabilities when they are due to be paid.

Responsibility for the Fund's overall investment strategies rests with the Pensions Committee. The Joint Investment Strategy Panel and the internal investment team monitor investment risks on a regular basis. Investment risk management tools are used to identify and analyse risks faced by the Fund's investments.

Consideration of the Fund's investment risk is part of the overall risk management of the pensions operations. Risks are reviewed regularly to reflect changes in activity and market conditions.

Types of investment risk

There are various ways of considering investment risks for pension funds. For the purposes of this note, market risk is the potential for an investor to experience losses from falls in the prices of investments. All financial instruments, including cash deposits, present a risk of loss of capital and risks vary depending on different asset classes.

Market risk also changes over time as economic conditions and investor sentiment change. The Fund considers overall fluctuations in prices arising from a variety of sources: market risk, foreign exchange risk, interest rate risk, credit risk, etc. The different risks may, to some extent, offset each other.

The overall market risk of the Fund depends on the actual mix of assets and encompasses all the different elements of risk.

Notes to the Financial Statements

21 Nature and extent of risk arising from financial instruments (cont)

The Fund manages these risks in a number of ways:

- assessing and establishing acceptable levels of market risk when setting overall investment strategy. Importantly, risk is considered relative to the liabilities of the Fund
- diversification of investments in terms of type of asset, investment styles, investment managers, geographical and industry sectors as well as individual securities
- taking stewardship responsibilities seriously and pursuing constructive engagement with the companies in which we invest
- monitoring market risk and market conditions to ensure risk remains within tolerable levels
- using equity futures contracts from time to time to manage market risk. Options are not used by the Fund.

Sensitivity analysis

Asset prices have a tendency to fluctuate. The degree of such fluctuation is known as “volatility” and it differs by asset class. The table sets out the long-term volatility assumptions used in the Fund’s asset-liability modelling undertaken by KPMG investment advisers:

| Asset type | Potential price movement (+ or -) |
|------------------------------|-----------------------------------|
| Equities - Developed Markets | 20.5% |
| Equities - Emerging Markets | 30.0% |
| Private Equity | 30.0% |
| Timber and Gold | 18.0% |
| Secured Loans | 7.5% |
| Fixed Interest Gilts | 6.7% |
| Index-Linked Gilts | 11.2% |
| Infrastructure | 12.0% |
| Property | 13.0% |
| Cash | 0.9% |

Volatility is the standard deviation of annual returns. Broadly speaking, in two years out of three, the asset’s change in value (which could be a gain or a loss) is expected to be lower than the volatility figure, but in one year out of three, the change in value is expected to be higher than the volatility figure.

Asset classes do not always move in line with each other. The extent to which assets move together is known as their “correlation”. A lower correlation means that there is less risk of assets losing value at the same time.

The overall Fund benefits from “diversification” because it invests in different asset classes, which don’t all move in line with each other. Consequently, the aggregate risk at the Fund level is less than the total risk from all the individual assets in which the Fund invests. The following table shows the risks at the asset class level and the overall Fund level, with and without allowance for correlation.

Notes to the Financial Statements

21 Nature and extent of risk arising from financial instruments (cont)

| | Value at 31 March 2019 £m | % of fund % | Potential Change +/- % | Value on increase £m | Value on decrease £m |
|-----------------------------------|------------------------------------|----------------|---------------------------------|----------------------------|----------------------------|
| Equities - Developed Markets | 4,253 | 54.6 | 20.5% | 5,124.9 | 3,381.1 |
| Equities - Emerging Markets | 256 | 3.3 | 30.0% | 332.8 | 179.2 |
| Private Equity | 155 | 2.0 | 30.0% | 201.5 | 108.5 |
| Timber and Gold | 124 | 1.6 | 18.0% | 146.3 | 101.7 |
| Secured Loan | 237 | 3.0 | 7.5% | 254.8 | 219.2 |
| Fixed Interest Gilts | 165 | 2.1 | 6.7% | 176.1 | 153.9 |
| Index-Linked Gilts | 711 | 9.1 | 11.2% | 790.6 | 631.4 |
| Infrastructure | 870 | 11.2 | 12.0% | 974.4 | 765.6 |
| Property | 552 | 7.1 | 13.0% | 623.8 | 480.2 |
| Cash and forward foreign exchange | 466 | 6.0 | 0.9% | 470.2 | 461.8 |
| Total [1] | 7,789 | 100.0 | 16.8% | 9,095.3 | 6,482.7 |
| Total [2] | | | 13.2% | 8,814.0 | 6,764.0 |
| Total [3] | | | 13.8% | 8,863.1 | n/a |

[1] No allowance for correlations between assets

[2] Including allowance for correlations between assets

[3] Including allowance for correlation between assets and liabilities.

The value on increase/decrease columns illustrate the monetary effect of the percentage change in the volatility column. The actual annual change in value is expected to be lower than this in two years out of three, but higher in one year out of three.

It can be seen that the risk to the overall Fund assets [2] is lower than the total of the risks to the individual assets.

However, because the purpose of a pension scheme is to make payments to scheme beneficiaries, the true risk of a pension scheme is not measured in absolute terms, but relative to its liabilities [3].

This risk analysis incorporates volatility from market, interest rate, foreign exchange, credit, and all other sources of risk, and, importantly, makes allowance for how these risks may offset each other.

Credit risk

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit risk in their pricing and consequently the risk of loss is implicitly provided for in the value of the Fund's assets and liabilities (as outlined in Market Risk above).

In essence, the Fund's entire investment portfolio is exposed to some sort of credit risk. However, through the selection of counterparties, brokers and financial institutions the Fund reduces the credit risk that may occur through the failure to settle a transaction in a timely manner.

Cash deposits, derivatives and securities lending are the major areas of credit exposure where credit risk is not reflected in market prices.

Notes to the Financial Statements

21 Nature and extent of risk arising from financial instruments (cont)

Cash deposits

At 31 March 2019, cash deposits represented £605.1m, 7.74% of total net assets. This was held with the following institutions:

| | Moody's Credit Rating at 31 March 2019 | Balances at 31 March 2018 £000 | Balances at 31 March 2019 £000 |
|------------------------------------------------------------|----------------------------------------|-----------------------------------|-----------------------------------|
| Held for investment purposes | | | |
| Northern Trust Global Investment Limited - liquidity funds | Aaa-mf | 10,571 | 13,517 |
| Northern Trust Company - cash deposits | Aa2 | 324,100 | 443,357 |
| The City of Edinburgh Council - treasury management | See below | 91,709 | 112,315 |
| Total investment cash | | 426,380 | 569,189 |
| Held for other purposes | | | |
| The City of Edinburgh Council - treasury management | See below | 48,833 | 35,897 |
| Total cash - parent | | 475,213 | 605,086 |
| Cash held by LPFE/LPFI Limited | | | |
| Royal Bank of Scotland | A1 | 93 | 341 |
| Total cash - group | | 475,306 | 605,427 |

The majority of Sterling cash deposits of the Fund are managed along with those of the administering authority (the City of Edinburgh Council) and other related organisations which are pooled for investment purposes as a treasury cash fund. Management of the cash fund is on a low risk basis, with security of the investments the key consideration.

| | Moody's Credit Rating at 31 March 2019 | Balances at 31 March 2018 £000 | Balances at 31 March 2019 £000 |
|---------------------------------------------|----------------------------------------|-----------------------------------|-----------------------------------|
| Money market funds | | | |
| Deutsche Bank AG, London | Aaa-mf | 608 | 3,979 |
| Goldman Sachs | Aaa-mf | 1 | 58 |
| Aberdeen Standard Sterling Liquidity Fund | Aaa-mf | 20,830 | 21,746 |
| Bank call accounts | | | |
| Bank of Scotland | Aa3 | 13,876 | 14,578 |
| Royal Bank of Scotland | A1 | 511 | 573 |
| Santander UK | Aa3 | 368 | 1 |
| Barclays Bank | A1 | 11 | 13 |
| Svenska Handelsbanken | Aa2 | 689 | 6 |
| HSBC Bank PLC | Aa3 | 52 | 14 |
| Notice accounts | | | |
| HSBC Bank PLC | Aa3 | - | 17,527 |
| UK Pseudo-Sovereign risk instruments | | | |
| Other Local Authorities [1] | Aa1 | 103,596 | 89,717 |
| | | 140,542 | 148,212 |

[1] Very few Local Authorities have their own credit rating but they are generally assumed to have a pseudo-sovereign credit rating (which in the UK at 31 March 2019 was 'Aa1').

Notes to the Financial Statements

21 Nature and extent of risk arising from financial instruments (cont)

The Council has in place institutional restrictions on investments and counterparty criteria. These include -

- (a) UK Government and other UK local Authorities with no limit, other public bodies up to £20 million per
- (b) Money market funds (MMFs) no more than £30 million or 15% with any one Fund.
- (c) Financial Institutions: Banks and Building Societies with multiple criteria based on a range of short and long term credit ratings, as well as any security, provided from maximum of £60 million / 20% of assets under management (AUM) for institutions with the highest criteria to £10 million / 5% of AUM for institutions with the lowest acceptable criteria.

No breaches of the Council's counterparty criteria occurred during the reporting period and the Fund does not expect any losses from non-performance by any of its counterparties in relation to deposits.

Securities lending

The Fund participates in a securities lending programme as described above. The Fund is potentially exposed to credit risk in the event of the borrower of securities defaulting. This risk is mitigated by the contractual commitment that borrowers provide collateral in excess of 100% of the value of the securities borrowed. In addition, Northern Trust has signed an agreement requiring it to make good any losses arising from the lending programme.

Derivatives

The Fund transacts foreign currency derivatives over-the-counter and hence is exposed to credit risk in the event of a counterparty defaulting on the net payment or receipt that remains outstanding. This risk is minimised by the use of counterparties that are recognised financial intermediaries with acceptable credit ratings and by netting agreements. At 31 March 2019, the Fund was owed £2.2m on over-the-counter foreign currency derivatives.

Refinancing risk

Refinancing risk is the risk that the Fund will be bound to replenish a significant proportion of its pension fund financial instruments at a time of unfavourable interest rates. The Fund is not bound by any obligation to replenish its investments and hence is not exposed to refinancing risk.

Liquidity risk

Liquidity risk reflects the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund therefore ensures that there is adequate cash and liquid resources to meet its commitments. Cash flow projections are prepared on a regular basis to understand and manage the timing of the Fund's cash flows.

The majority (estimated to be approximately 78% (2018 77%)) of the Fund's investments could be converted to cash within three months in a normal trading environment.

22 Actuarial statement

The Scheme Actuary has provided a statement describing the funding arrangements of the Fund. This can be found at the end of this section.

Notes to the Financial Statements

23 Actuarial present value of promised retirement benefits

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standard 19 (IAS19) assumptions, is estimated to be £9,435m (2018 £8,254m). This figure is used for statutory accounting purposes by Lothian Pension Fund and complies with the requirements of IAS26. The assumptions underlying the figure match those adopted for the Administering Authority's FRS102/IAS19 reports at each year end.

The figure is only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

| | 31 March 2018 % p.a. | 31 March 2019 % p.a. |
|------------------------------------|-------------------------|-------------------------|
| Inflation / pensions increase rate | 2.4 | 2.5 |
| Salary increase rate | 4.1 | 4.2 |
| Discount rate | 2.7 | 2.4 |

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2016 model, assuming that the current rate of improvements has reached a peak and will converge to a long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies, in years, at age 65 are summarised below:

| | 31 March 2018 | | 31 March 2019 | |
|------------------------------------------------|---------------|------------|---------------|------------|
| | Males | Females | Males | Females |
| Current pensioners | 21.7 years | 24.3 years | 21.7 years | 24.3 years |
| Future pensioners (assumed to be currently 45) | 24.7 years | 27.5 years | 24.7 years | 27.5 years |

Commutation assumption

An allowance is included for future retirements to elect to take 50% of the maximum additional tax-free cash up to HMRC limits for pre-April 2009 service and 75% of the maximum tax-free cash for post-April 2009 service.

24 Non-current Debtors

| | LPF Parent 31 March 2018 £000 | LPF Group 31 March 2018 £000 | LPF Parent 31 March 2019 £000 | LPF Group 31 March 2019 £000 |
|--|-------------------------------------------|------------------------------------------|-------------------------------------------|------------------------------------------|
| | Contributions due - employers' cessation | 1,525 | 1,525 | 3,457 |
| | 1,525 | 1,525 | 3,457 | 3,457 |

In accordance with the Funding Strategy Statement and in recognition of severe affordability constraints facing the charitable sector, "Funding Agreements" have been put in place to allow certain former employers to repay cessation valuation debt over longer terms (up to twenty years), to avoid potential default or insolvency.

The above debtors all relate to community admission bodies.

Notes to the Financial Statements

25 Debtors

| | LPF Parent 31 March 2018* £000 | LPF Group 31 March 2018* £000 | LPF Parent 31 March 2019 £000 | LPF Group 31 March 2019 £000 |
|-------------------------------------------------|--------------------------------------------|-------------------------------------------|-------------------------------------------|------------------------------------------|
| Contributions due - employers | 12,250 | 12,250 | 16,831 | 16,831 |
| Contributions due - members | 3,690 | 3,690 | 4,691 | 4,691 |
| Benefits paid in advance or recoverable | 33 | 33 | 6 | 6 |
| Sundry debtors | 97 | 168 | 503 | 717 |
| Prepayments | 325 | 335 | 314 | 323 |
| LPFE & LPFI Limited Loan facility - see note 28 | 11 | - | - | - |
| | 16,406 | 16,476 | 22,345 | 22,568 |

26 Creditors

| | LPF Parent 31 March 2018* £000 | LPF Group 31 March 2018* £000 | LPF Parent 31 March 2019 £000 | LPF Group 31 March 2019 £000 |
|----------------------------------------------|--------------------------------------------|-------------------------------------------|-------------------------------------------|------------------------------------------|
| Benefits payable | 7,062 | 7,062 | 8,886 | 8,886 |
| VAT, PAYE and State Scheme premiums | 1,432 | 1,571 | 1,354 | 1,738 |
| Contributions in advance | 18,290 | 18,290 | 17,785 | 17,785 |
| Miscellaneous creditors and accrued expenses | 2,168 | 2,354 | 2,332 | 2,488 |
| Office - operating lease | 243 | 243 | 220 | 220 |
| Corporation tax | - | - | - | 28 |
| Intra group creditor - see note 28 | 287 | - | 222 | - |
| | 29,482 | 29,520 | 30,799 | 31,145 |

27 Additional Voluntary Contributions

Active members of the Lothian Pension Fund have the option to pay additional voluntary contributions (AVCs). These AVCs are invested separately from the main funds, securing additional benefits on a money purchase basis for those members that have elected to contribute. The investment of the AVCs is managed by Standard Life and Prudential.

In accordance with regulation 4 (2) (b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010, AVCs are not included in the pension fund financial statements.

| Total contributions during year for Lothian Pension fund | 2017/18* £000 | 2018/19 £000 |
|-------------------------------------------------------------|------------------|-----------------|
| Standard Life | 312 | 312 |
| Prudential | 2,059 | 2,225 |
| | 2,371 | 2,537 |

| Total value at year end for Lothian Pension Fund | 31 March 2018* £000 | 31 March 2019 £000 |
|-----------------------------------------------------|------------------------|-----------------------|
| Standard Life | 4,850 | 4,685 |
| Prudential | 6,634 | 7,676 |
| | 11,484 | 12,361 |

Notes to the Financial Statements

28 Related parties

The City of Edinburgh Council

The Lothian Pension Fund and the Scottish Homes Pension Fund are administered by the City of Edinburgh Council. Consequently there is a strong relationship between the Council and the Pension Funds.

LPFE, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer the pension funds. The Fund has a service level agreement in place with the Council for certain support services. Costs directly attributable to a specific Fund are charged to the relevant Fund, costs that are common to the two Funds are allocated on a defined basis.

Transactions between the Council and the Fund are managed via a holding account. Each month the Fund is paid a cash sum leaving a working balance in the account to cover the month's pension payroll costs and other expected costs.

| | 31 March 2018* | 31 March 2019 |
|-------------------------------------|----------------|---------------|
| | £000 | £000 |
| Year end balance of holding account | 3,083 | 884 |
| | 3,083 | 884 |

Part of the Fund's cash holdings are invested on the money markets by the treasury management operations of the Council, through a service level agreement. During the year to 31 March 2019, the fund had an average investment balance of £139.1m (2017/18 £119.9m). Interest earned was £977.1k (2017/18 £453.6k).

| Year end balance on treasury management account | 31 March 2018* | 31 March 2019 |
|-------------------------------------------------|----------------|---------------|
| | £000 | £000 |
| Held for investment purposes | 91,709 | 112,315 |
| Held for other purposes | 48,833 | 35,897 |
| | 140,542 | 148,212 |

Scheme employers

All scheme employers to the fund are (by definition) related parties, a full list of employers can be found on page 84. The employer contributions for the ten largest scheme employers are as follows -

| | 31 March 2018* | 31 March 2019 |
|-----------------------------|----------------|---------------|
| | £000 | £000 |
| City of Edinburgh Council | 50,041 | 59,694 |
| West Lothian Council | 22,895 | 25,841 |
| Scottish Water | 9,526 | 15,975 |
| East Lothian Council | 13,812 | 14,746 |
| Midlothian Council | 13,148 | 14,041 |
| Lothian Buses | 7,581 | 7,002 |
| Edinburgh Napier University | 4,938 | 5,199 |
| Heriot-Watt University | 3,324 | 3,026 |
| Scottish Police Authority | 2,945 | 3,016 |
| Edinburgh College | 2,289 | 2,676 |

Notes to the Financial Statements

28 Related parties (cont)

Governance

As at 31 March 2019, all members of the Pensions Committee, with the exception of Richard Lamont, and all members of the Pension Board, were members of the Lothian Pension Fund. One member of both the Pensions Committee and the Pension Board are in receipt of pension benefits from Lothian Pension Fund.

Each member of the Pensions Committee and Pension Board is required to declare any financial and non-financial interests they have in the items of business for consideration at each meeting, identifying the relevant agenda item and the nature of their interest.

During the period from 1 April 2018 to the date of issuing of these accounts, a number of employees of the City of Edinburgh Council and its wholly owned subsidiary, LPFE Limited, held key positions in the financial management of the Lothian Pension Fund. Total compensation paid in relation to key management personnel employed by LPFE Limited during the period was as follows:

| | 31 March 2018 £000 | 31 March 2019 £000 |
|-----------------------------------------------------------|-----------------------|-----------------------|
| Short-term employee benefits | 415 | 647 |
| Post-employment benefits - employer pension contributions | 85 | 111 |

Key management personnel employed by LPFE had accrued pensions totalling £120,245 (1 April 2018: £97,456) and lump sums totalling £132,375 (1 April 2018: £110,889) at the end of the period. Further details on senior management remuneration can be found within the remuneration report on page 134.

Remuneration of key management personnel employed by City of Edinburgh Council is disclosed separately in the Financial Statements of City of Edinburgh Council.

The Councillors, who are members of the Pensions Committee, are also remunerated by City of Edinburgh Council.

LPFE Limited & LPFI Limited- loan facility

LPFE & LPFI Limited are wholly owned by the City of Edinburgh Council as administrating authority of Lothian Pension Fund and have entered into a shareholder agreement with the Council to address governance matters. The companies have a loan facility agreement with the City of Edinburgh Council for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the companies return any cash not immediately required and this can result in short periods when the companies have returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Interest payable by LPFE Limited during the period was £1,434 of which £787 was due at the year end and for LPFI Limited there was no interest payable for the year. At 31 March 2019, there was zero balance on the loan facilities for both LPFE Limited and LPFI Limited.

LPFE Limited - staffing services

Staffing services are provided to Lothian Pension Fund for the purposes of administering the Funds under a intra-group resourcing agreement. The agreement also provides for the running costs of the company to be covered as part of a service charge and allows for the provision of staffing services to LPFI Limited. During the year to 31 March 2019, the Fund was invoiced £3,614k (2018 £1,450k) for the services of LPFE Limited staff.

Notes to the Financial Statements

29a Consolidated Lothian Pension Fund Group - LPFE Limited & LPFI Limited - deferred tax

| Movement in deferred tax asset (Non-current asset) | LPF | LPF |
|----------------------------------------------------|---------|---------|
| | Group | Group |
| | 2017/18 | 2018/19 |
| | £000 | £000 |
| At 1 April 2018 | 117 | 292 |
| Credit for year to Fund Account | 175 | 101 |
| At 31 March 2019 | 292 | 393 |

| Elements of closing deferred tax asset | LPF | LPF |
|----------------------------------------|----------|----------|
| | Group | Group |
| | 31 March | 31 March |
| | 2018 | 2019 |
| | £000 | £000 |
| Pension liability | 292 | 393 |
| | 292 | 393 |

29b Shares in group companies - LPFE Limited & LPFI Limited

| | 31 March 2018 | 31 March 2019 |
|-------------------------------------------------------------------------------|---------------|---------------|
| | £ | £ |
| Allotted, called up and fully paid Ordinary shares of £1 each - LPFE Limited* | 1 | 1 |
| Allotted, called up and fully paid Ordinary shares of £1 each - LPFI Limited | 60,000 | 60,000 |
| | 60,001 | 60,001 |

*One ordinary share of £1 was issued to Lothian Pension Fund at par value on incorporation. Due to the low value this does not show on the Net Assets Statement.

30 Retirement benefits obligation - group

The retirement benefit obligation described in this note relates only to the employees of LPFE. This is because obligation in respect of the staff employed by the City of Edinburgh Council is accounted for in the City of Edinburgh Council's Financial Statements.

On 1 May 2015 LPFE commenced trading and its staff transferred their employment from the City of Edinburgh Council to the Company on that date. At that time, the Company also entered into appropriate admission arrangements with the City of Edinburgh Council with respect to the transferring individuals continuing to be members of the Lothian Pension Fund and in relation to its obligations as an employer in that Fund.

The present value of the defined benefit obligation and related current and past service cost were measured using the Projected Unit Credit Method.

Fund assets

LPFE's share of the fair value of the Fund's assets which are not intended to be realised in the short term and may be subject to significant change before they are realised, was comprised as follows:

Notes to the Financial Statements

30 Retirement benefits obligation - group (cont)

| Asset | | Fair value at 31 | % of total | Fair value at 31 | % of total |
|------------------------------------------|------------------------|------------------|------------|------------------|------------|
| | | March 2018 | 31 March | March 2019 | 31 March |
| | | £000 | % | £000 | % |
| Equity securities: | Consumer | 1,185 | 14.0 | 1,094 | 14.0 |
| | Manufacturing | 1,288 | 15.0 | 1,265 | 15.0 |
| | Energy and utilities | 541 | 6.0 | 777 | 6.0 |
| | Financial institutions | 769 | 9.0 | 865 | 9.0 |
| | Health and care | 424 | 5.0 | 559 | 5.0 |
| | Information technology | 528 | 6.0 | 335 | 6.0 |
| | Other | 543 | 6.0 | 1,003 | 6.0 |
| Debt securities: | Corporate Bonds | 169 | 2.0 | - | 2.0 |
| | UK Government | 839 | 10.0 | 1,045 | 10.0 |
| | Other | - | 0.0 | - | 0.0 |
| Private equity: | All | 158 | 2.0 | 139 | 2.0 |
| Real property | UK property | 556 | 6.0 | 697 | 6.0 |
| | Overseas property | 9 | 0.0 | - | 0.0 |
| Investment funds and unit trusts: | Equities | 83 | 1.0 | 102 | 1.0 |
| | Commodities | - | 0.0 | - | 0.0 |
| | Bonds | - | 0.0 | 261 | 0.0 |
| | Infrastructure | 1,025 | 12.0 | 1,277 | 12.0 |
| | Other | 20 | 0.0 | - | 0.0 |
| Derivatives: | Foreign Exchange | 4 | 0.0 | 3 | 0.0 |
| Cash and cash equivalents: | All | 511 | 6.0 | 863 | 6.0 |
| | | 8,652 | 100.0 | 10,285 | 100.0 |

Amounts recognised in the Net Assets Statement

| | LPF | LPF |
|-----------------------------------|----------|----------|
| | Group | Group |
| | 31 March | 31 March |
| | 2018 | 2019 |
| | £000 | £000 |
| Fair value of Fund assets | 8,652 | 10,285 |
| Present value of Fund liabilities | (10,367) | (12,594) |
| | (1,715) | (2,309) |

Notes to the Financial Statements

30 Retirement benefits obligation - group (cont)

Movement in the defined benefit obligation during the period

| | LPF Group 2017/18 £000 | LPF Group 2018/19 £000 |
|------------------------------------------------------------------|---------------------------------|---------------------------------|
| Brought forward | 3,513 | 10,367 |
| Current service cost | 336 | 843 |
| Interest cost on obligation | 131 | 294 |
| Fund participants contributions | 7,175 | 186 |
| Benefits paid | - | - |
| Actuarial losses arising from changes in financial assumptions | (788) | 904 |
| Actuarial losses arising from changes in demographic assumptions | - | - |
| Other actuarial losses | - | - |
| Balance at year end | 10,367 | 12,594 |

After the Supreme Court denied the Government leave to appeal the McCloud and other associated cases on 27 June 2019, a written ministerial statement confirmed that as 'transitional protection' was offered to members of all the main public service pension schemes, the difference in treatment would need to be remedied across all those schemes, including the LGPS. The Fund therefore commissioned its actuary to produce a revised IAS19 statement for LPFE Limited to incorporate the potential implications of the McCloud judgement. The revised statement estimated an approximate £255k increase in LPFE's defined benefit obligation. This has not been incorporated in the above figures, which remain consistent with LPFE Limited's audited financial statements.

Movement in the fair value of Fund assets during the period

| | LPF Group 2017/18 £000 | LPF Group 2018/19 £000 |
|-------------------------------------------------------------|---------------------------------|---------------------------------|
| Brought forward | 2,828 | 8,652 |
| Benefits paid | - | - |
| Interest income on Fund assets | 104 | 244 |
| Contributions by employer | 204 | 567 |
| Contributions by member | 91 | 194 |
| Contributions in respect of unfunded benefits | - | - |
| Unfunded benefits paid | (4) | (8) |
| Effect of business combinations and disposals | 5,711 | - |
| Return on assets excluding amounts included in net interest | (282) | 636 |
| Balance at year end | 8,652 | 10,285 |

Amounts recognised in the Fund Account

| | LPF Group 2017/18 £000 | LPF Group 2018/19 £000 |
|--------------------------------------------------------------------|---------------------------------|---------------------------------|
| Interest received on Fund assets | (104) | (244) |
| Interest cost on Fund liabilities | 131 | 294 |
| Current service costs | 336 | 843 |
| Effect of business combinations and disposals | 1,377 | - |
| Employer contributions | (204) | (567) |
| Actuarial gain due to re-measurement of defined benefit obligation | (788) | 904 |
| Return on Fund assets (excluding interest above) | 282 | (636) |
| Net cost recognised in Fund account | 1,030 | 594 |

Notes to the Financial Statements

30 Retirement benefits obligation - group (cont)

Principal actuarial assumptions used in this valuation

| | 31 March 2018 | 31 March 2019 |
|------------------------------------|---------------|---------------|
| | % p.a. | % p.a. |
| Inflation / pensions increase rate | 2.3 | 2.4 |
| Salary increase rate | 4.0 | 4.1 |
| Discount rate | 2.7 | 2.5 |

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice. Best estimate has been interpreted to mean that the proposed assumptions are 'neutral' – there is an equal chance of actual experience being better or worse than the assumptions proposed.

The financial assumptions used for reporting in the financial statements are the responsibility of the employer. These assumptions are largely prescribed at any point and reflect market conditions at the reporting date. Changes in market conditions that result in changes in the net discount rate can have a significant effect on the value of the liabilities reported.

A reduction in the net discount rate will increase the assessed value of liabilities as a higher value is placed on benefits paid in the future. A rise in the net discount rate will have an opposite effect of a similar magnitude. There is also uncertainty around life expectancy of the UK population – the value of current and future pension benefits will depend on how long they are assumed to be in payment.

Life expectancy is based on Fund specific statistical analysis with improvements in line with the CMI 2012 model assuming current rates of improvements have peaked and will converge to a long term rate of 1.25% p.a.

Based on these assumptions, the average future life expectancies at age 65 are summarised below:

| | 31 March 2018 | | 31 March 2019 | |
|--------------------|---------------|------------|---------------|------------|
| | Males | Females | Males | Females |
| Current pensioners | 22.1 years | 23.7 years | 21.7 years | 24.3 years |
| Future pensioners | 24.2 years | 26.3 years | 24.7 years | 27.5 years |

Expected employer contributions to the defined benefit plan for the year ended 31 March 2020 are £643,000, based on a pensionable payroll cost of £2,374,000.

31 Contractual commitments

Investment commitments

The Fund has commitments relating to outstanding call payments due on unquoted funds held in the private equity, timber, property and infrastructure parts of the portfolio. The amounts 'called' by these funds are irregular in both size and timing, taking place over a number of years from the date of each original commitment. The outstanding commitments at the year end are as follows:

| | 31 March 2018* | 31 March 2019 |
|------------------------------------|----------------|---------------|
| | £000 | £000 |
| Outstanding investment commitments | 213,774 | 325,361 |
| | 213,774 | 325,361 |

Notes to the Financial Statements

31 Contractual commitments (cont)

Office accommodation - 144 Morrison Street, Edinburgh

The Fund is committed to making the following future payments.

| | 31 March 2018 | 31 March 2019 |
|------------------------------------------|---------------|---------------|
| | £000 | £000 |
| Within one year | 115 | 115 |
| Between one and five years | 345 | 345 |
| After five years | 762 | 647 |
| | 1,222 | 1,107 |
| Recognised as an expense during the year | 92 | 92 |

The above expense has been allocated across the two Funds, Lothian Pension Fund's share is £85.1k.

32 Contingent assets and liabilities

Contribution refunds

At 31st March 2019, Lothian Pension Fund had £909k (2018: £894k) in unclaimed refunds due to members.

Employer Cessations

a) Funding Agreements

As stated in note 24, "In accordance with the Funding Strategy Statement and in recognition of severe affordability constraints facing the charitable sector, "Funding Agreements" have been put in place with certain former employers to repay cessation valuation debt".... In exceptional circumstances, this includes "repayment of less than the cessation debt in order to avoid employer insolvency, with an appropriate agreement which allows the Fund to revisit the repayment of the remaining debt at a future date (i.e. the debt would be a contingent liability and hence not recognised on an employer's balance sheet); and seeking, where appropriate, suitable "anti-embarrassment" provisions in legal agreement covering future increase in employer asset values". At 31 March 2019, such contingent assets of the Fund totalled £1,635k.

b) Homeless Action Scotland

On 24 January 2019, the Chief Finance Officer, Lothian Pension Fund, made a request for direction by Scottish Ministers that the assets and liabilities of Homeless Action Scotland (HAS) should be transferred from Lothian Pension Fund (LPF) to the Scottish Homes Pension Fund. HAS became an "Admitted Body" of Lothian Pension Fund when its predecessor (The Scottish Council for Single Homeless) was admitted in 1978, pursuant to Regulation B4(4) of the Local Government Superannuation (Scotland) Regulations 1974, being 'a body to whom a grant is made out of moneys provided by Parliament'. Since 1978, HAS accrued pension liabilities for the ongoing pension entitlements of the HAS employees admitted to membership of LPF. Following confirmation by HAS that it would be unable to meet the minimum contribution rate assessed at the actuarial valuation of 31 March 2017 (certified by LPF's actuary), LPF terminated HAS's admission to LPF with effect from 12 July 2018 in accordance with LPF's Funding Strategy Statement. Upon HAS becoming an exiting employer, LPF's actuary was instructed to calculate the liabilities that remained with LPF on cessation and the final contribution due from HAS, as required under Regulation 62(2) of the 2018 Regulations. The Actuary's cessation valuation is £641,000.

A response to the request for such direction is awaited from Scottish Ministers.

Notes to the Financial Statements

32 Contingent assets and liabilities (cont)

EU Tax claims & income recovery

The Fund participates in various claims to recover withheld investment income. EU tax claims relate to the recovery of tax deducted from dividend payments prior to receipt or payable tax credits thereon. The claims can be divided into three main types – “Manninen” / Foreign Income Dividends (Fids), “Fokus Bank” and Manufactured Dividends. Given the high level of uncertainty as to the eventual success of such claims from EU tax authorities, no accrual of income is made in the financial statements. The value of these outstanding claims is approximately £11.4m. To date, the amount of tax recovered exceeds the cost of pursuing claims. Legal costs are shared across a pool of claimants and the Fund has the right to cease participation without incurring further costs. An annual progress report is provided to Pensions Audit Sub-Committee.

Variable pay arrangements

During the year, the company introduced three variable pay schemes, two of which have vesting periods. The Portfolio Manager and Senior Management schemes entitle staff to receive an assessed percentage of their salary as an additional variable pay award if they meet certain objectives during the year. The assessment year runs from 1 February 2018 to 31 January 2019. The award then vests over three years. The first part is payable at the end of the first year if the objectives are met and the remaining two parts are payable in the following two years if the requirement that the employee is still employed by the company at such time is met. Payment one has been made in January 2019. A liability has been raised at 31 March 2019 for the 2 months of service which the employees have delivered with regards to the second and third payments in the scheme.

In the event that all the staff involved in the arrangements at 31 January 2019 remain in the company’s employment there is a contingent liability of £319,900 in excess of the current and non-current liabilities, as recognised in these financial statements in accordance with IAS19. This amount would be payable over two years.

Guaranteed Minimum Pension (GMP) – Reconciliation to HMRC records

GMP is the minimum pension which a United Kingdom occupational pension scheme must provide for those employees who were contracted out of the State Earnings-Related Pension Scheme (SERPS) between 6 April 1978 and 5 April 1997.

The UK Government mandated a reconciliation of Guaranteed Minimum Pension details held on scheme pension administration records to those held by HMRC, this to be completed by a revised date of 31 March 2019. Whilst this reconciliation of GMP mismatches has been completed by the Fund, work is ongoing to calculate “lump sum” arrears of any pension underpayments arising, together with the correct pension now being put into payment. It is not anticipated, however, that such arrears should represent a material sum.

On 8 February 2018, SPPA published “Circular No.1/2018”, the purpose of which was to “Confirm how GMP related overpayments which arise from the current reconciliation exercise should be managed going forward...” This stated that “Scottish Minister have decided that as in 2008/2009 any LGPS pension in payment affected by the exercise should not be reduced going forward. Instead the identified GMP related overpayment should be converted as before into an Increased Pension Entitlement (IPE) allowing the pension to continue at its existing level.”

Guaranteed Minimum Pension (GMP)

Following The High Court ruling from 26 October 2016, all defined benefit pension schemes must equalise Guaranteed Minimum Pension (GMP) for men and women. There is insufficient basis to estimate reliably the amount to be recognised in the past service cost until actuaries complete their assessment of the impact and reflect it fully in the pension reports. The Funds actuary, Hymans Robertson LLP has advised that following discussions with the National Audit Office and other LGPS actuaries, the general expectation is that a ‘trigger event’ is yet to occur in the LGPS and their default approach is to ignore any GMP impact in the 31 March 2019 accounts.

Notes to the Financial Statements

32 Contingent assets and liabilities (cont)

Local Government Pension Scheme (Scotland) cost management update from Scottish Public Pensions Agency (SPPA)

In February 2019, the SPPA provided the Local Government Association (LGA) Secretariat with the following update for Scottish administering authorities:

"As you are aware, the Public Service Pensions Act 2013 requires all public service pension schemes to undergo regular valuations, in addition to the regular fund valuations undertaken by LGPS fund actuaries. At the October meeting of the LGPSAB (Scheme Advisory Board) (Scotland), Government Actuary's Department (GAD) presented demographic assumptions which have been agreed. The UK Government and Scottish Ministers chose to allow certain exceptions which were designed to protect those closest to retirement from the impact of those reforms. As you will be aware, the Court of Appeal handed down judgment in the cases of McCloud and Sargeant on 20 December 2018: these age-related transitional arrangements were held to be discriminatory. It is anticipated that other public service pension schemes across the UK may be affected by this decision, including LGPS Scotland, notwithstanding that the nature of the comparable transitional arrangements implemented for local government pension schemes [statutory underpin] was slightly different from those adopted for the unfunded schemes. The judgment therefore has implications for post-reform members' benefits, and the UK Government is seeking permission to appeal to the Supreme Court. Meantime, the substantial impact of the judgment is such that it is impossible to assess with certainty the value of current public service pension arrangements.

On 30 January 2019 HM Treasury therefore announced in a Written Ministerial Statement that the UK Government intends to pause the 'cost cap' mechanism under the current round of scheme valuations, pending the final outcome of the appeal. As noted in the Ministerial Statement, if the UK Government is successful in its appeal, the cost cap process will resume. If unsuccessful, steps will need to be taken to compensate members who have been unfairly disadvantaged in the post reform schemes. Accordingly, the nature, and the timescale for implementation, of changes to the provisions of LGPS Scotland flowing from the actuarial valuation of the scheme for cost cap purposes being undertaken by the Government Actuary's Department (GAD) is not currently clear. We understand that changes which were scheduled to come into force this April in the England & Wales LGPS have been put on hold. We are liaising closely with HM Treasury and MHCLG on this matter. Meanwhile, GAD is progressing its valuation calculations only to the extent necessary at this stage, pending greater clarity on the legal position and the UK Government's consequent policy intent".

The UK Government had sought leave to appeal that decision but, on 27 June 2019, the Supreme Court rejected that request, meaning the case will now refer back to the Employment Tribunal so that a remedy can be put in place for those affected. The UK Government must now propose rectification to compensate individuals for the difference in treatment.

The Fund requested revised IAS19 reporting from its actuary following the appeal decision. The actuary has estimated the impact of the ruling to be a £102m increase in the actuarial value of promised retirement benefits. This has been reflected in Note 23. As confirmed by the actuary, however, there remains significant uncertainty over the remedy to be applied and associated costs to Scottish LGPS funds.

33 Impairment losses

During the year the Fund recognised an increase in impairment losses in respect of specific benefit over payments for which reimbursement has been requested of £15k. This increased the impairment to £42.7k at the year end.

Lothian Pension Fund

Actuarial Statement for 2018/19

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The funding policy is set out in the Administering Authority's Funding Strategy (FSS), dated March 2018. In summary, the key funding principles are as follows:

- to ensure the long-term solvency of the overall Fund;
- to ensure the solvency of each individual employers' share of the Fund based on their expected term of participation in the Fund;
- to minimise the degree of short-term change in employer contribution rates;
- maximise the returns from investments within reasonable and considered risk parameters, and hence minimise the cost to the employer;
- to ensure that sufficient cash is available to meet all liabilities as they fall due for payment;
- to help employers manage their pension liabilities; and
- where practical and cost effective, to make allowance for the different characteristics of different employers and groups of employers.

The FSS sets out how the Administering Authority seeks to achieve these objectives.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2014 was as at 31 March 2017. This valuation revealed that the Fund's assets, which at 31 March 2017 were valued at £6,598 million, were sufficient to meet 98% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2017 valuation was £145 million. For the avoidance of doubt, these results are based on the assumptions that apply to the Fund's Primary investment strategy.

Each employer had contribution requirements set at the valuation with the aim of achieving full funding within a given time horizon. Contribution rates were set using one of two approaches depending on each employer's circumstances:

- Certain low risk and open employers participate in a contribution stability mechanism which limits annual changes in contribution rates. The mechanism is tested at each valuation to make sure it achieves the desired funding objectives.
- Other employers pay the contributions required to cover the cost of future service benefits and to recover the deficit/surplus identified as at 31 March 2017 over a given time period.

Individual employers' contributions for the period 1 April 2018 to 31 March 2021 were set in accordance with the Fund's funding policy as set out in its FSS, which includes further detail on the approaches mentioned above.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the 2017 valuation report.

Lothian Pension Fund

Actuarial Statement for 2018/19

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth and inflation to retirement or expected earlier date of leaving pensionable membership.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market value.

The key financial assumptions adopted under the Primary investment strategy for the 2017 valuation were as follows:

| Financial assumptions | 31 March 2017 % p.a. |
|-----------------------------------|-------------------------|
| Discount rate | 3.2% |
| Salary increase assumption | 4.1% |
| Benefit increase assumption (CPI) | 2.4% |

The key demographic assumption was the allowance made for longevity. The life expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2016 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.25% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

| | Males | Females |
|---------------------|------------|------------|
| Current Pensioners | 21.7 years | 24.3 years |
| Future Pensioners * | 24.7 years | 27.5 years |

*Aged 45 as at 31 March 2017

Copies of the 2017 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2017

Asset returns under the Primary investment strategy over the period have been higher than the valuation discount rate but real bond yields have fallen slightly since 31 March 2017. Combining the impact of these may mean that the overall funding level at 31 March 2019 is broadly similar to the last valuation.

The next actuarial valuation will be carried out as at 31 March 2020. The Funding Strategy Statement will also be reviewed at that time.

Richard Warden FFA

Fellow of the Institute and Faculty of Actuaries

For and on behalf of Hymans Robertson LLP

20 Waterloo Street, Glasgow, G2 6DB

26 April 2019

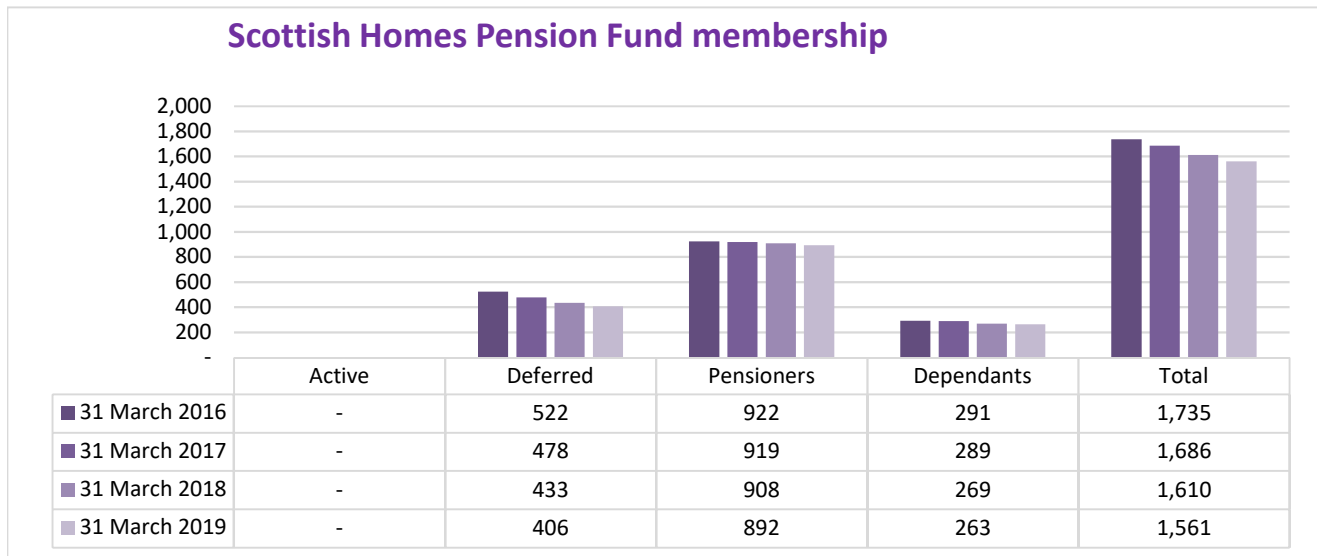
List of active employers at 31 March 2019

| Scheduled Bodies | |
|---------------------------------|----------------------------------|
| City of Edinburgh Council (The) | Scottish Fire and Rescue Service |
| East Lothian Council | Scottish Police Authority |
| Edinburgh College | Scottish Water |
| Heriot-Watt University | SESTRAN |
| Lothian Buses | Visit Scotland |
| Lothian Valuation Joint Board | West Lothian College |
| Midlothian Council | West Lothian Council |
| Scotland's Rural College (SRUC) | |

| Admitted Bodies | |
|-----------------------------------------------|----------------------------------------------------|
| Amey Services | Improvement Service (The) |
| Audit Scotland | Into Work |
| Barony Housing Association Ltd | ISS UK Ltd |
| Baxter Storey | LPFE Ltd |
| Bellrock Property and Facilities Management | Melville Housing Association |
| Canongate Youth Project | Mitie (Edinburgh College) |
| Capital City Partnership | Mitie PFI |
| CGI UK Ltd | Morrison Facilities Services Ltd |
| Children's Hearing Scotland | Museums Galleries Scotland |
| Children's Hospice Association Scotland | Newbattle Abbey College |
| Citadel Youth Centre | North Edinburgh Dementia Care |
| Compass Chartwell | NSL Services Ltd |
| Convention of Scottish Local Authorities | Penumbra |
| Cyrenians | Pilton Equalities Project |
| Dacoll Limited | Queen Margaret University |
| Edinburgh Business School | Royal Edinburgh Military Tattoo |
| Edinburgh Development Group | Royal Society of Edinburgh |
| Edinburgh International Festival Society | Scotland's Learning Partnership |
| Edinburgh Leisure | Scottish Adoption Agency |
| Edinburgh Napier University | Scottish Futures Trust |
| ELCAP | Scottish Legal Complaints Commission |
| Enjoy East Lothian | Scottish Schools Education Research Centre (SSERC) |
| Family Advice and Information Resource | Skanska UK |
| Family and Community Development West Lothian | Sodexo Ltd |
| First Step | St Andrew's Children's Society Limited |
| Forth and Oban Ltd | St Columba's Hospice |
| Four Square (Scotland) | Stepping Out Project |
| Freespace Housing Association | Waverley Care |
| Granton Information Centre | University of Edinburgh (Edinburgh College of Art) |
| Handicabs (Lothian) Ltd | Weslo Housing Management |
| Hanover (Scotland) Housing Association | West Granton Community Trust |
| Health in Mind | West Lothian Leisure |
| Homes for Life Housing Partnership | Young Scot Enterprise |
| HWU Students Association | Youthlink Scotland |

There are currently 13 ceased employers not included in the above list that are currently or in the process of setting up funding agreements to repay cessation debt over a number of years.

Scottish Homes Pension Fund



Investment strategy

The Fund's actuary estimated that the funding level of the Scottish Homes Pension Fund was 104.7% at 31 March 2017.

Achievement of full funding meant that the Fund no longer needed to take investment risk by investing in equities and property. Instead, the Fund was able to minimise risk by investing solely in bonds, specifically UK gilts. These financial instruments move proportionately with liability values.

After a year of significant change, the year to 31 March 2019 brought no change to the strategy allocation of 100% bonds and this should not change until at least the results of the next actuarial valuation (March 2020) are known. At that point in time, the actuary will amend financial and demographic estimates based on actual experience over the prior three years.

The strategic and actual asset allocations for the Fund at the end of the 2018 and 2019 financial years are shown in the table below.

| | Strategic Allocation 31 March 2018 % | Actual Allocation 31 March 2018 % | Strategic Allocation 31 March 2019 % | Actual Allocation 31 March 2019 % |
|--------------|--------------------------------------------|-----------------------------------------|--------------------------------------------|-----------------------------------------|
| Equities | - | - | - | - |
| Bonds | 100.0 | 91.9 | 100.0 | 97.8 |
| Property | - | 2.7 | - | - |
| Cash | - | 5.4 | - | 2.2 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 |

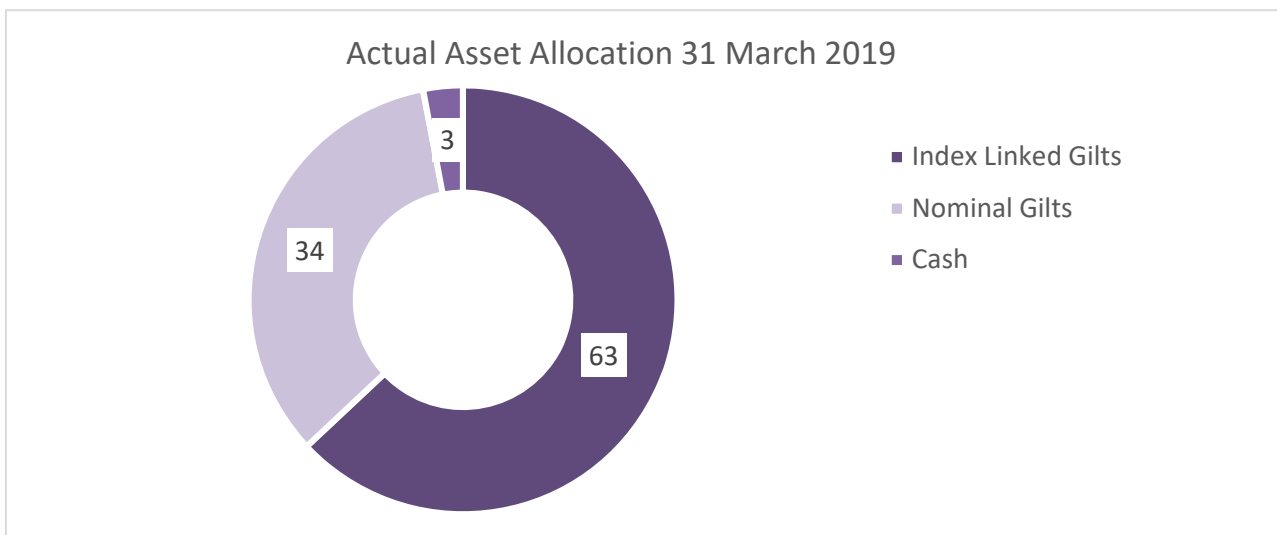
Shortly after the end of March 2018, the final sale of property assets was completed, leaving the Fund entirely invested in index-linked gilts and cash. The index linked gilts were structured to broadly match the expected liability payments as they fall due.

Given that the Fund had achieved full funding, the Pensions Committee approved a new investment objective in June 2018:

"to match the cash flow from gilt income and redemption payments as closely as possible with the expected liability payments of the fund"

Detailed analysis of the Scottish Homes liabilities was undertaken during 2018/19 to ensure that the invested assets are as closely matched with the liability profile as possible, taking into consideration the expected duration of liabilities and whether they are fixed or index-linked in nature.

This resulted in a portion of index-linked gilts being sold and reinvested in nominal gilts to achieve a closer asset-liability match. At 31 March 2019, the Fund is 'cash flow matched' up to one year beyond the next actuarial valuation expected at 31 March 2020, and 'duration matched' liabilities beyond that. This is because there is greater certainty in the earlier period - funding levels will continue to be subject to the actuary's financial or demographic assumptions of future experience, which will be reassessed during 2020/21.



Investment movements

As the Scottish Homes Pension Fund is mature, it must sell assets to pay pensions. Cash or cash equivalents are held to enable pensions to be paid in between the dates when gilts redeem.

The Fund's assets have increased in value by 4.6% over the year, adjusted for cash flow movements to pay pensions, while a proxy for the value of liabilities increased by 4.4%, which suggests that the asset-liability match is quite effective.

Scottish Homes Pension Fund

Fund Account for year ended 31 March 2019

This statement shows a summary of the income and expenditure that the Pension Fund has generated and consumed in delivering the Local Government Pension Scheme. Included is the income from investment dealings and as well as the cost of providing benefits and administration of the Fund.

| Restated 2017/18 £000 | | Note | 2018/19 £000 |
|-----------------------------|------------------------------------------------------------|---------------|-----------------|
| | Income | | |
| 575 | Contributions from the Scottish Government | 2, 4 | - |
| - | Transfers from other schemes | | - |
| 575 | | | - |
| | Less: expenditure | | |
| 6,666 | Pension payments including increases | | 6,572 |
| 767 | Lump sum retirement payments | | 591 |
| 4 | Lump sum death benefits | | 5 |
| 47 | Transfers to other schemes | 5 | 129 |
| (31) | Administrative expenses | 2, 6b | (19) |
| 7,453 | | | 7,278 |
| (6,878) | Net withdrawals from dealing with members | | (7,278) |
| | Returns on investments | | |
| 2,474 | Investment income | 7 | 1,824 |
| (1,615) | Change in market value of investments | 8, 11b | 5,767 |
| (165) | Investment management expenses | 6c | (84) |
| 694 | Net returns on investments | | 7,507 |
| (6,184) | Net increase/(decrease) in the Fund during the year | | 229 |
| 170,644 | Net assets of the Fund at 1 April 2018 | | 164,460 |
| 164,460 | Net assets of the Fund at 31 March 2019 | 11 | 164,689 |

Scottish Homes Pension Fund

Net Assets Statement as at 31 March 2019

This statement provides a breakdown of type and value of all net assets at the year end.

| 31 March 2018 £000 | Note | 31 March 2019 £000 |
|-------------------------------|------------------------------------------------|--------------------------|
| Investment Assets | | |
| 148,064 | Bonds - UK | 158,743 |
| 9,094 | Cash Deposits | 3,650 |
| 4,904 | Other investment assets | 618 |
| 162,062 | | 163,011 |
| Investment Liabilities | | |
| - | Other investment liabilities | - |
| - | | - |
| 162,062 | Net investment assets | 163,011 |
| | | |
| Current assets | | |
| 194 | The City of Edinburgh Council | 10 |
| 2,240 | Cash balances | 1,741 |
| 12 | Debtors | 1 |
| 2,446 | | 1,752 |
| Current liabilities | | |
| (48) | Creditors | (74) |
| (48) | | (74) |
| 2,398 | Net current assets | 1,678 |
| 164,460 | Net assets of the Fund at 31 March 2019 | 164,689 |

The unaudited accounts were issued on 26 June 2019 and the audited accounts were authorised for issue on 25 September 2019.

JOHN BURNS FCMA CGMA, PgC
Chief Finance Officer, Lothian Pension Fund
25 September 2019

Note to the net asset statement

The financial statements summarise the transactions of the Fund during the year and its net assets at the year end. They do not take account of the obligations to pay pensions and benefits which fall due after the end of the year. The actuarial position of the Fund, which does take account of such obligations, is discussed in the Actuarial Valuation section of this report and these financial statements should be read in conjunction with that information. In addition, as required by IAS26, the Actuarial Present Value of Promised Retirement Benefits is disclosed in the notes to these financial statements.

Notes to the Financial Statements

1 Statement of Accounting Policies

The statement of accounting policies for all Funds can be found on page 105.

2 Prior Year Adjustment

During the year, the Fund has changed its accounting policy in respect to the recognition of income received by the Fund from Scottish Government in relation to the administration of the Fund.

Previously this income was recognised within the employer contributions received by the Fund in relation to deficit funding. As the Scottish Homes Pension Fund now has a funding surplus no deficit funding is required and the Fund has reviewed its previous treatment. The administration charge is no longer recognised in employer contribution and is now recognised as income against the administrative expenses of the Fund.

| | 2017/18 Audited £000 | Adjustment £000 | 2017/18 Restated £000 |
|--------------------------------------------|----------------------------|--------------------|-----------------------------|
| Contributions from the Scottish Government | 675 | (100) | 575 |
| Administrative expenses | (69) | 100 | 31 |

3 Events after the Reporting Date

There have been no events since 31 March 2019, and up to the date when these Financial Statements were authorised, that require any adjustments to these Financial Statements.

4 Contributions from the Scottish Government

The Scottish Homes Pension Fund (SHPF) is a single employer pension fund for former employees of Scottish Homes (subsequently Communities Scotland) (and persons who were employed by the Scottish Special Housing Association, but who did not become employees of Scottish Homes). The City of Edinburgh Council was selected by the Scottish Executive to be the administering authority of a fund created prior to the wind up of the Scottish Homes Residuary Body and therefore became the administering authority of SHPF on 1 July 2005, pursuant to section 2(a)(1A) of The Local Government Pension Scheme (Scotland) Amendment (No. 2) Regulations 2005 (SSI 315/2005) (the 2005 Regs).

SHPF is a mature, non-active fund (that is, the fund has no contributions paid into it by active members but consists only of deferred and pensioner members and therefore only pays money out to the pensioners).

Section 2 (1C) of the 2005 Regs stipulates that:

Where the actuary determines, after having regard to the existing and prospective liabilities of the fund, that additional funding is necessary to maintain the solvency of the fund (SHPF), then Scottish Ministers will make payments to the administering authority to maintain that solvency.

In this way, the Scottish Government acts as the 'Guarantor' for SHPF's liabilities, as confirmed in the Funding agreement, signed on behalf of the Scottish Executive and dated 6 July 2005.

As at the latest triennial actuarial valuation date of 31 March 2017, SHPF showed a funding surplus of £7.7million with a funding level of 104.7%, derived from a market valuation of assets of £170.6million and liabilities of £162.9million.

Notes to the Financial Statements

4 Contributions from the Scottish Government (cont)

Having implemented the investment strategy as required by the Funding Agreement, the assets of SHPF are invested entirely in low risk, index-linked gilts. With a funding surplus, the Scottish Government is not required to provide any contribution, but as Guarantor has the responsibility to pay towards the administration expenses of the Fund estimated to be £70,000 per annum (for years 2018 to 31 March 2021).

In addition the Guarantor is responsible for meeting the cost of investment expenses. Given the Fund's surplus the Fund are comfortable that investment expenses can be met directly by the Fund until the next triannual valuation.

5 Transfers out to other pension schemes

| | 2017/18 £000 | 2018/19 £000 |
|----------------------|-----------------|-----------------|
| Group transfers | - | - |
| Individual transfers | 47 | 129 |
| | 47 | 129 |

6a Total Management expenses

| | Restated 2017/18 £000 | 2018/19 £000 |
|--------------------------------|-----------------------------|-----------------|
| Administrative costs | (31) | 15 |
| Investment management expenses | 107 | 19 |
| Oversight and governance costs | 58 | 31 |
| | 134 | 65 |

This analysis of costs for the Scottish Homes Pension Fund has been prepared in accordance with CIPFA guidance. The analysis looks at the combined administration and investment management expenses in note 6b and c and splits out the costs to include a third heading covering oversight and governance expenditure.

6b Administrative expenses

| | Restated 2017/18 £000 | 2018/19 £000 |
|---------------------------------|-----------------------------|-----------------|
| Employee costs | 24 | 28 |
| System costs | 8 | 8 |
| Actuarial fees | 30 | 8 |
| External audit fees | 1 | 1 |
| Printing and postage | 2 | 2 |
| Depreciation | 1 | 1 |
| Office costs | 2 | 2 |
| Sundry costs less sundry income | 1 | 1 |
| | 69 | 51 |
| Administration fee received | (100) | (70) |
| | (31) | (19) |

LPFE, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer the pension funds. The Fund has a service level agreement in place with the Council for certain support services. Costs directly attributable to a specific Fund are charged to the relevant Fund, costs that are common to the two Funds are allocated on a defined basis.

Notes to the Financial Statements

6c Investment management expenses

| | 2017/18 £000 | 2018/19 £000 |
|-----------------------------------------------------------|-----------------|-----------------|
| External management fees - deducted from capital (direct) | 54 | - |
| Transaction costs | 30 | 2 |
| Employee costs | 31 | 44 |
| Custody fees | 7 | 6 |
| Engagement and voting fees | 2 | 2 |
| Performance measurement fees | 10 | 3 |
| Consultancy fees | 16 | 3 |
| System costs | 7 | 9 |
| Legal fees | 1 | 2 |
| Office costs | 2 | 2 |
| Sundry costs less sundry income | 5 | 11 |
| | 165 | 84 |

The Fund has not incurred any performance-related investment management fees in 2018/19 or 2017/18.

7 Investment income

| | 2017/18 £000 | 2018/19 £000 |
|-------------------------------------------|-----------------|-----------------|
| Income from fixed interest securities | 1,449 | 1,749 |
| Dividends from equities | 799 | - |
| Income from pooled investments - property | 270 | - |
| Interest on cash deposits and sundries | 29 | 75 |
| | 2,547 | 1,824 |
| Irrecoverable withholding tax | (73) | - |
| | 2,474 | 1,824 |

8 Reconciliation of movement in investments

| | Market value at 31 March 2018 £000 | Purchases at cost £000 | Sales & proceeds £000 | Change in market value £000 | Market value at 31 March 2019 £000 |
|-----------------------------------------------|---------------------------------------|---------------------------|--------------------------|--------------------------------|---------------------------------------|
| Bonds | 148,064 | 54,948 | (50,036) | 5,767 | 158,743 |
| Equities | - | - | - | - | - |
| Pooled investment vehicles | - | - | - | - | - |
| | 148,064 | 54,948 | (50,036) | 5,767 | 158,743 |
| Other financial assets / (liabilities) | | | | | |
| Cash deposits* | 9,094 | | | - | 3,650 |
| Investment income due/amounts payable* | 4,904 | | | - | 618 |
| | 13,998 | | | - | 4,268 |
| Net financial assets | 162,062 | | | 5,767 | 163,011 |

The change in market value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are reflected in the cost of investment acquisitions and in the proceeds from sales and are therefore included in the tables above.

Notes to the Financial Statements

8 Reconciliation of movement in investments (cont)

| | Market value at 31 March 2017 £000 | Purchases at cost £000 | Sales & proceeds £000 | Change in market value £000 | Market value at 31 March 2018 £000 |
|-----------------------------------------------|---------------------------------------|---------------------------|--------------------------|--------------------------------|---------------------------------------|
| Bonds | 127,970 | 33,345 | (11,838) | (1,413) | 148,064 |
| Equities | 28,221 | 932 | (28,451) | (702) | - |
| Pooled investment vehicles | 7,998 | - | (8,621) | 623 | - |
| | 164,189 | 34,277 | (48,910) | (1,492) | 148,064 |
| Other financial assets / (liabilities) | | | | | |
| Cash deposits* | 3,602 | | | (123) | 9,094 |
| Investment income due/amounts payable* | 459 | | | - | 4,904 |
| | 4,061 | | | (123) | 13,998 |
| Net financial assets | 168,250 | | | (1,615) | 162,062 |

* Per CIPFA disclosure guidance the change in market value intentionally does not balance opening/closing market values

9 Investment managers and mandates

| Manager | Mandate | Market value at 31 March 2018 £000 | % of total 31 March 2018 % | Market value at 31 March 2019 £000 | % of total 31 March 2019 % |
|--------------------------------------------------------|-----------------------|---------------------------------------|-------------------------------|---------------------------------------|-------------------------------|
| In-house | High Div Equity | 87 | 0.1 | 31 | 0.0 |
| Total global equities | | 87 | 0.1 | 31 | 0.0 |
| In-house | UK Index linked gilts | 148,858 | 91.9 | 159,330 | 97.8 |
| Total fixed interest and inflation linked bonds | | 148,858 | 91.9 | 159,330 | 97.8 |
| Schroders | Property | 4,363 | 2.7 | - | - |
| Total property | | 4,363 | 2.7 | - | - |
| In-house | Cash | 8,754 | 5.4 | 3,650 | 2.2 |
| Total cash | | 8,754 | 5.4 | 3,650 | 2.2 |
| Net financial assets | | 162,062 | 100.0 | 163,011 | 100.0 |

10 Investments representing more than 5% of the net assets of the Fund

| | Market value at 31 March 2018 £000 | % of total 31 March 2018 % | Market value at 31 March 2019 £000 | % of total 31 March 2019 % |
|-------------------------------------|---------------------------------------|-------------------------------|---------------------------------------|-------------------------------|
| UK Gov 2.5% Index Linked 16/04/20 | 12,309 | 7.5 | 11,619 | 7.1 |
| UK Gov 4.25% 07/06/32 | - | - | 9,366 | 5.7 |
| UK Gov 4.125% Index Linked 22/07/30 | - | - | 9,124 | 5.5 |
| UK Gov 2.5% Index Linked 17/07/24 | 12,431 | 7.6 | 9,053 | 5.5 |
| UK Gov 1.25% Index Linked 22/11/27 | 11,149 | 6.8 | 8,914 | 5.4 |
| UK Gov 1.875% Index Linked 22/11/22 | 12,530 | 7.6 | 8,240 | 5.0 |
| UK Gov 4.125% Index Linked 22/11/17 | 21,410 | 13.0 | - | - |
| UK Gov 1.125% Index Linked 22/11/37 | 12,465 | 7.6 | - | - |

Notes to the Financial Statements

11 Financial Instruments

11a Classification of financial instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the fair value amounts of financial assets and liabilities by category and net assets statement heading. No financial assets were reclassified during the accounting period.

All financial instruments are marked to market (at fair value) in the Fund's accounting records hence there is no difference between the carrying value and fair value.

| | 31 March 2018 | | | 31 March 2019 | | |
|----------------------------------------|-----------------------------------------------|-----------------------|-----------------------------------------|-----------------------------------------------|-----------------------|-----------------------------------------|
| | Designated as fair value through fund account | Loans and receivables | Financial liabilities at amortised cost | Designated as fair value through fund account | Loans and receivables | Financial liabilities at amortised cost |
| | £000 | £000 | £000 | £000 | £000 | £000 |
| Financial assets | | | | | | |
| Investment assets | | | | | | |
| Bonds | 148,064 | - | - | 158,743 | - | - |
| Equities | - | - | - | - | - | - |
| Pooled investments | - | - | - | - | - | - |
| Cash | - | 9,094 | - | - | 3,650 | - |
| Other balances | - | 4,904 | - | - | 618 | - |
| | 148,064 | 13,998 | - | 158,743 | 4,268 | - |
| Other assets | | | | | | |
| City of Edinburgh Council | - | 194 | - | - | 10 | - |
| Cash | - | 2,240 | - | - | 1,741 | - |
| Debtors | - | 12 | - | - | 1 | - |
| | - | 2,446 | - | - | 1,752 | - |
| Assets total | 148,064 | 16,444 | - | 158,743 | 6,020 | - |
| Financial liabilities | | | | | | |
| Other liabilities | | | | | | |
| Creditors | - | - | (48) | - | - | (74) |
| Liabilities total | - | - | (48) | - | - | (74) |
| Total net assets | 148,064 | 16,444 | (48) | 158,743 | 6,020 | (74) |
| Total net financial instruments | | | 164,460 | | | 164,689 |

11b Net gains and losses on financial instruments

| | 2017/18 £000 | 2018/19 £000 |
|-----------------------------------------------|-----------------|-----------------|
| Designated as fair value through fund account | (1,492) | 5,767 |
| Loans and receivables | (123) | - |
| Financial liabilities at amortised cost | - | - |
| Total | (1,615) | 5,767 |

Notes to the Financial Statements

11c Valuation of financial instruments carried at fair value

The valuation of financial instruments has been classified into three levels, according to the quality and reliability of information used to determine fair values.

Level 1

Financial instruments at Level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities and unit trusts.

Quoted investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Level 2

Financial instruments at Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3

Financial instruments at Level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data. Such instruments would include unquoted equity investments, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investments in unquoted private equity, infrastructure, timber and real estate are based on valuations provided by the general partners to the funds in which the Fund has invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of International Financial Reporting Standards (IFRS). The valuations are typically undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

| | 31 March 2019 | | | Total £000 |
|-----------------------------------------------|-----------------|-----------------|-----------------|---------------|
| | Level 1 £000 | Level 2 £000 | Level 3 £000 | |
| Investment assets | | | | |
| Designated as fair value through fund account | - | 158,743 | - | 158,743 |
| Total investment assets | - | 158,743 | - | 158,743 |
| Investment liabilities | | | | |
| Designated as fair value through fund account | - | - | - | - |
| Total investment liabilities | - | - | - | - |
| Net investment assets | - | 158,743 | - | 158,743 |

Notes to the Financial Statements

11c Valuation of financial instruments carried at fair value (cont)

| | 31 March 2018 | | | Total £000 |
|-----------------------------------------------|-----------------|-----------------|-----------------|---------------|
| | Level 1 £000 | Level 2 £000 | Level 3 £000 | |
| Investment assets | | | | |
| Designated as fair value through fund account | - | 148,064 | - | 148,064 |
| Total financial assets | - | 148,064 | - | 148,064 |
| Investment liabilities | | | | |
| Designated as fair value through fund account | - | - | - | - |
| Total financial liabilities | - | - | - | - |
| Net investment assets | - | 148,064 | - | 148,064 |

12 Nature and extent of risk arising from financial instruments

Risk and risk management

The Fund's primary aim is to ensure that all members and their dependants receive their benefits when they become payable. As directed by Scottish Government, after 31 March 2017 triennial valuation showed a funding level of 104.7%, the assets of the Fund were invested entirely in low risk gilts. In addition, the Fund ensures that sufficient cash is available to meet all liabilities when they are due to be paid.

Responsibility for the Fund's overall investment strategy rests with the Pensions Committee. The Investment Strategy Panel and the internal investment team monitor investment risks on a regular basis. Investment risk management tools are used to identify and analyse risks faced by the Fund's investments.

Types of investment risk

There are various ways of considering investment risks for pension funds. For the purposes of this note, market risk is the potential for an investor to experience losses from falls in the prices of investments. All financial instruments, including cash deposits, present a risk of loss of capital and risks vary depending on different asset classes.

Market risk also changes over time as economic conditions and investor sentiment change. The market risk of Scottish Homes Pension Fund has to some extent been mitigated. The Fund's assets have been matched to its liabilities as at the 31 March 2017 triennial valuation so interest rate risk has been minimised and as all assets held are valued in Pound Sterling no exchange risk occurs. A review of the asset matching of the Fund will next take place to coincide with the results of 31 March 2020 triennial valuation.

Sensitivity analysis

Asset prices have a tendency to fluctuate. The degree of such fluctuation is known as "volatility" and it differs by asset class. The table sets out the long-term volatility assumptions used by the Fund's investment adviser KPMG:

| Asset type | Potential price movement (+ or -) |
|--------------------|-----------------------------------|
| Index-Linked Gilts | 11.2% |
| Cash | 0.9% |

Notes to the Financial Statements

12 Nature and extent of risk arising from financial instruments (cont)

Volatility is the standard deviation of annual returns. Broadly speaking, in two years out of three, the asset's change in value (which could be a gain or a loss) is expected to be lower than the volatility figure, but in one year out of three, the change in value is expected to be higher than the volatility figure.

Asset classes don't always move in line with each other. The extent to which assets move together is known as their "correlation". A lower correlation means that there is less risk of assets losing value at the same time. The overall Fund benefits from "diversification" because it invests in numerous different asset classes, which don't all move in line with each other. Consequently, the aggregate risk at the Fund level is less than the total risk from all the individual assets in which the Fund invests.

The following table shows the risks at the asset class level and the overall Fund level.

| | Value at 31 March 2019 £000 | % of fund % | Potential Change +/- % | Value on increase £000 | Value on decrease £000 |
|--------------------|--------------------------------------|----------------|---------------------------------|------------------------------|------------------------------|
| Index-Linked Gilts | 159,329 | 97.7 | 11.2 | 177,174 | 141,484 |
| Cash | 3,681 | 2.3 | 0.9 | 3,714 | 3,648 |
| Total [1] | 163,010 | 100.0 | 11.0 | 180,888 | 145,132 |
| Total [2] | | | 11.0 | 180,892 | 145,128 |
| Total [3] | | | 4.8 | 170,834 | n/a |

[1] No allowance for correlations between assets

[2] Including allowance for correlations between assets

[3] Including allowance for correlation between assets and liabilities.

The value on increase/decrease columns illustrate the monetary effect of the percentage change in the volatility column. The actual annual change in value is expected to be lower than this in two years out of three, but higher in one year out of three.

It can be seen that the risk to the overall Fund assets [2] is lower than the total of the risks to the individual assets [1].

However, because the purpose of a pension scheme is to make payments to scheme beneficiaries, the true risk of a pension scheme is not measured in absolute terms, but relative to its liabilities [3]. The risk is lower than the absolute asset risk, due to the impact of correlation with the discount rate used to value the liabilities.

This risk analysis incorporates volatility from market, interest rate, foreign exchange, credit, and all other sources of risk, and, importantly, makes allowance for how these risks may offset each other.

Credit risk

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit risk in their pricing and consequently the risk of loss is implicitly provided for in the value of the Fund's assets and liabilities (as outlined in Market Risk above).

In essence, the Fund's entire investment portfolio is exposed to some sort of credit risk. However, through the selection of counterparties, brokers and financial institutions the Fund reduces the credit risk that may occur through the failure to settle a transaction in a timely manner.

Notes to the Financial Statements

12 Nature and extent of risk arising from financial instruments (cont)

Cash deposits are the major areas of credit exposure where credit risk is not reflected in market prices.

Cash deposits

At 31 March 2019, cash deposits represented £9m, 5.5% of total net assets. This was held with the following institutions:

| | Moody's Credit Rating at 31 March 2019 | Balances at 31 March 2018 £000 | Balances at 31 March 2019 £000 |
|-----------------------------------------------------|----------------------------------------|-----------------------------------|-----------------------------------|
| Held for investment purposes | | | |
| Northern Trust Company - cash deposits | A2 | 1,077 | 580 |
| The City of Edinburgh Council - treasury management | See below | 8,017 | 3,070 |
| | | 9,094 | 3,650 |
| Held for other purposes | | | |
| The City of Edinburgh Council - treasury management | See below | 2,240 | 1,741 |
| Total cash | | 11,334 | 5,391 |

The majority of Sterling cash deposits of the Fund are managed along with those of the administering authority (the City of Edinburgh Council) and other related organisations which are pooled for investment purposes as a treasury cash fund. Management of the cash fund is on a low risk basis, with security of the investments the key consideration. The Council has in place counterparty criteria.

The Council has in place institutional restrictions on investments and counterparty criteria. These include -

- (a) UK Government and other UK local Authorities with no limit, other public bodies up to £20 million per organisation.
- (b) Money market funds (MMFs) no more than £30 million or 15% with any one Fund.
- (c) Financial Institutions: Banks and Building Societies with multiple criteria based on a range of short and long term credit ratings, as well as any security provided, from maximum of £60 million / 20% of assets under management (AUM) for institutions with the highest criteria to £10 million / 5% of AUM for institutions with the lowest acceptable criteria.

Notes to the Financial Statements

12 Nature and extent of risk arising from financial instruments (cont)

| | Moody's Credit Rating at 31 March 2019 | Balances at 31 March 2018 £000 | Balances at 31 March 2019 £000 |
|---------------------------------------------|----------------------------------------|-----------------------------------|-----------------------------------|
| Money market funds | | | |
| Deutsche Bank AG, London | Aaa-mf | 44 | 129 |
| Goldman Sachs | Aaa-mf | - | 2 |
| Aberdeen Standard Sterling Liquidity Fund | Aaa-mf | - | 706 |
| Standard Life Investments | Aaa-mf | 1,520 | - |
| Bank call accounts | | | |
| Bank of Scotland | Aa3 | 1,013 | 473 |
| Royal Bank of Scotland | A3 | 37 | 19 |
| Santander UK | Aa3 | 27 | - |
| Barclays Bank | A1 | 1 | - |
| Svenska Handelsbanken | Aa2 | 50 | - |
| HSBC Bank PLC | Aa3 | 4 | - |
| Notice accounts | | | |
| HSBC Bank PLC | Aa3 | - | 569 |
| UK Pseudo-Sovereign risk instruments | | | |
| Other Local Authorities [1] | Aa1 | 7,561 | 2,913 |
| | | 10,257 | 4,811 |

[1] Very few Local Authorities have their own credit rating but they are generally assumed to have a pseudo-sovereign credit rating (which in the UK at 31 March 2018 was 'Aa1').

No breaches of the Council's counterparty criteria occurred during the reporting period and the Fund does not expect any losses from non-performance by any of its counterparties in relation to deposits.

Refinancing risk

Refinancing risk is the risk that the Fund will be bound to replenish a significant proportion of its pension fund financial instruments at a time of unfavourable interest rates. The Fund is not bound by any obligation to replenish its investments and hence is not exposed to refinancing risk.

Liquidity risk

Liquidity risk reflects the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund therefore ensures that there is adequate cash and liquid resources to meet its commitments. Cash flow projections are prepared on a regular basis to understand and manage the timing of the Fund's cash flows.

All of the Fund's investments could be converted to cash within three months in a normal trading environment.

13 Actuarial statement

The Scheme Actuary has provided a statement describing the funding arrangements of the Fund. This can be found at the end of this section.

Notes to the Financial Statements

14 Actuarial present value of promised retirement benefits

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standard 19 (IAS19) assumptions, is estimated to be £135m (2018 £134m). This figure is used for statutory accounting purposes by Scottish Homes Pension Fund and complies with the requirements of IAS26. The assumptions underlying the figure match those adopted for the Administering Authority's IAS19 reports at each year end.

The figure is only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

| | 31 March 2018 % p.a. | 31 March 2019 % p.a. |
|----------------------------------|-------------------------|-------------------------|
| Inflation/pensions increase rate | 2.4% | 2.5% |
| Discount rate | 2.7% | 2.4% |

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2016 model, assuming that the current rate of improvements has reached a peak and will converge to a long term rate of 1.75% p.a.. Based on these assumptions, the average future life expectancies, in years, at age 65 are summarised below:

| | 31 March 2018 | | 31 March 2019 | |
|------------------------------------------------|---------------|------------|---------------|------------|
| | Males | Females | Males | Females |
| Current pensioners | 22.4 years | 24.8 years | 22.4 years | 24.8 years |
| Future pensioners (assumed to be currently 45) | 24.8 years | 27.8 years | 24.8 years | 27.8 years |

Commutation assumption

An allowance is included for future retirements to elect to take 50% of the maximum additional tax-free cash up to HMRC limits for pre-April 2009 service and 75% of the maximum tax-free cash for post-April 2009 service.

15 Debtors

| | 31 March 2018 £000 | 31 March 2019 £000 |
|----------------|-----------------------|-----------------------|
| Sundry debtors | 12 | 1 |
| | 12 | 1 |

16 Creditors

| | 31 March 2018 £000 | 31 March 2019 £000 |
|----------------------------------------------|-----------------------|-----------------------|
| Benefits payable | 3 | 73 |
| Miscellaneous creditors and accrued expenses | 45 | 1 |
| | 48 | 74 |

17 Related party transactions

The City of Edinburgh Council

The Lothian Pension Fund and the Scottish Homes Pension Fund are administered by the City of Edinburgh Council. Consequently there is a strong relationship between the Council and the Pension Funds.

Notes to the Financial Statements

17 Related party transactions (cont)

LPFE, which is a wholly owned subsidiary of the Council, is responsible for providing the staffing resource to administer the pension funds. The Fund has a service level agreement in place with the Council for certain support services. Costs directly attributable to a specific Fund are charged to the relevant Fund, costs that are common to the two Funds are allocated on a defined basis.

Transactions between the Council and the Fund are managed via a holding account. Each month the Fund is paid a cash sum leaving a working balance in the account to cover the month's pension payroll costs and other expected costs.

| | 31 March 2018 £000 | 31 March 2019 £000 |
|-------------------------------------|-----------------------|-----------------------|
| Year end balance of holding account | 194 | 10 |
| | 194 | 10 |

Part of the Fund's cash holdings are invested on the money markets by the treasury management operations of the Council, through a service level agreement. During the year to 31 March 2019, the fund had an average investment balance of £10.6m (2018 £6.3m). Interest earned was £74k (2018 £29k).

| Year end balance on treasury management account | 31 March 2018 £000 | 31 March 2019 £000 |
|-------------------------------------------------|-----------------------|-----------------------|
| Held for investment purposes | 8,011 | 3,070 |
| Held for other purposes | 2,240 | 1,741 |
| | 10,251 | 4,811 |

Fund Guarantor

The Fund guarantor (by definition) is a related party to the scheme. The Scottish Government's contributions to the Fund can be found in note 4 (page 89) of the notes to the Financial Statements.

LPFE Limited - staffing services

Staffing services are provided to Lothian Pension Fund for the purposes of administering the Funds under a intra-group resourcing agreement. The agreement also provides for the running costs of the company to be covered as part of a service charge and allows for the provision of staffing services to LPFI Limited. During the year to 31 March 2019, the Fund was invoiced £3,614k (2018 £1,450k) for the services of LPFE Limited staff.

Governance

As at 31 March 2019, all members of the Pensions Committee, with the exception of Richard Lamont, and all members of the Pension Board, were members of the Lothian Pension Fund. One member of both the Pensions Committee and the Pension Board are in receipt of pension benefits from Lothian Pension Fund.

Each member of the Pensions Committee and Pensions Board is required to declare any financial and non-financial interests they have in the items of business for consideration at each meeting, identifying the relevant agenda item and the nature of their interest.

Notes to the Financial Statements

17 Related party transactions (cont)

During the period from 1 April 2018 to the date of issuing of these accounts, the Fund was charged by City Of Edinburgh Councils via its service level agreement for time spent by its Executive Management team on pension fund issues. All other staff that held key positions in the financial management of Lothian Pension Fund were employed by LPFE Limited. Total compensation paid in relation to key management personnel employed by LPFE Limited during the period was as follows:

| | 31 March 2018 | 31 March 2019 |
|-----------------------------------------------------------|---------------|---------------|
| | £000 | £000 |
| Short-term employee benefits | 415 | 567 |
| Post-employment benefits - employer pension contributions | 85 | 111 |

Key management personnel employed by LPFE, had accrued pensions totalling £120,245 (1 April 2018: £97,456) and lump sums totalling £132,375 (1 April 2018: £110,889) at the end of the period.

Staff are either employed by City of Edinburgh Council or LPFE Limited, and their costs reimbursed by the Pension Funds. The Councillors, who are members of the Pensions Committee, are also remunerated by City of Edinburgh Council.

18 Contingent assets/liabilities

Request for direction by Scottish Ministers to transfer the assets and liabilities of Homeless Action Scotland from the Lothian Pension Fund to the Scottish Homes Pension Fund

On 24 January 2019, the Chief Finance Officer, Lothian Pension Fund, made a request for direction by Scottish Ministers that the assets and liabilities of Homeless Action Scotland (HAS) should be transferred from Lothian Pension Fund (LPF) to the Scottish Homes Pension Fund. HAS became an "Admitted Body" of Lothian Pension Fund when its predecessor (The Scottish Council for Single Homeless) was admitted in 1978, pursuant to Regulation B4(4) of the Local Government Superannuation (Scotland) Regulations 1974, being 'a body to whom a grant is made out of moneys provided by Parliament'. Since 1978, HAS accrued pension liabilities for the ongoing pension entitlements of the HAS employees admitted to membership of LPF. Following confirmation by HAS that it would be unable to meet the minimum contribution rate assessed at the actuarial valuation of 31 March 2017 (certified by LPF's actuary), LPF terminated HAS's admission to LPF with effect from 12 July 2018 in accordance with LPF's Funding Strategy Statement. Upon HAS becoming an exiting employer, LPF's actuary was instructed to calculate the liabilities that remained with LPF on cessation and the final contribution due from HAS, as required under Regulation 62(2) of the 2018 Regulations. The Actuary's cessation valuation is £641,000.

A response to the request for such direction is awaited from Scottish Ministers.

Guaranteed Minimum Pension (GMP)

Following The High Court ruling from 26 October 2016, all defined benefit pension schemes must equalise Guaranteed Minimum Pension (GMP) for men and women. There is insufficient basis to estimate reliably the amount to be recognised in the past service cost until actuaries complete their assessment of the impact and reflect it fully in the pension reports. The Funds actuary, Hymans Robertson LLP has advised that following discussions with the National Audit Office and other LGPS actuaries, the general expectation is that a 'trigger event' is yet to occur in the LGPS and their default approach is to ignore any GMP impact in the 31 March 2019 accounts.

Notes to the Financial Statements

18 Contingent assets/liabilities (cont)

Local Government Pension Scheme (Scotland) cost management update from Scottish Public Pensions Agency (SPPA)

In February 2019, the SPPA provided the Local Government Association (LGA) Secretariat with the following update for Scottish administering authorities:

As you are aware, the Public Service Pensions Act 2013 requires all public service pension schemes to undergo regular valuations, in addition to the regular fund valuations undertaken by LGPS fund actuaries. At the October meeting of the LGPSAB (Scheme Advisory Board) (Scotland), Government Actuary's Department (GAD) presented demographic assumptions which have been agreed. The UK Government and Scottish Ministers chose to allow certain exceptions which were designed to protect those closest to retirement from the impact of those reforms. As you will be aware, the Court of Appeal handed down judgment in the cases of McCloud and Sargeant on 20 December 2018: these age-related transitional arrangements were held to be discriminatory. It is anticipated that other public service pension schemes across the UK may be affected by this decision, including LGPS Scotland, notwithstanding that the nature of the comparable transitional arrangements implemented for local government pension schemes [statutory underpin] was slightly different from those adopted for the unfunded schemes. The judgment therefore has implications for post-reform members' benefits, and the UK Government is seeking permission to appeal to the Supreme Court. Meantime, the substantial impact of the judgment is such that it is impossible to assess with certainty the value of current public service pension arrangements.

On 30 January 2019 HM Treasury therefore announced in a Written Ministerial Statement that the UK Government intends to pause the 'cost cap' mechanism under the current round of scheme valuations, pending the final outcome of the appeal. As noted in the Ministerial Statement, if the UK Government is successful in its appeal, the cost cap process will resume. If unsuccessful, steps will need to be taken to compensate members who have been unfairly disadvantaged in the post reform schemes. Accordingly, the nature, and the timescale for implementation, of changes to the provisions of LGPS Scotland flowing from the actuarial valuation of the scheme for cost cap purposes being undertaken by the Government Actuary's Department (GAD) is not currently clear. We understand that changes which were scheduled to come into force this April in the England & Wales LGPS have been put on hold. We are liaising closely with HM Treasury and MHCLG on this matter. Meanwhile, GAD is progressing its valuation calculations only to the extent necessary at this stage, pending greater clarity on the legal position and the UK Government's consequent policy intent".

19 Contractual commitments

The Fund had no contractual commitments at the year end.

20 Impairment losses

No impairment losses have been identified during the year.

Scottish Homes Pension Fund

Actuarial Statement for 2018/19

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The Administering Authority's Funding Strategy Statement (FSS), dated March 2018, states that a bespoke funding strategy has been adopted for the Fund.

The strategy aims for the Fund to be 100% solvent by 2044 using a discount rate based on government bonds. It includes target funding levels at each actuarial valuation. Contributions from the Scottish Government are determined by reference to the target funding levels. The deficit recovery period is 8 years.

As the Fund was well ahead of its Target Funding Level at the 2017 valuation, it took the decision to derisk its investment strategy and now invests 100% of its assets in index-linked gilts.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2014 was as at 31 March 2017. This valuation revealed that the Fund's assets, which at 31 March 2017 were valued at £170.6 million, were sufficient to meet 104.7% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting surplus at the 2017 valuation was £7.7 million.

The Guarantor's contributions for the period 1 April 2018 to 31 March 2021 were set in accordance with the Fund's funding policy as set out in its FSS.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the 2017 valuation report.

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund's assets at their market value.

The key financial assumptions adopted for the 2017 valuation were as follows:

| Financial assumptions | 31 March 2017 |
|-----------------------------------|----------------------------------------------------|
| Discount Rate | Bank of England nominal yield curve |
| Benefit increase assumption (CPI) | Bank of England implied (RPI) curve less 1.0% p.a. |

Scottish Homes Pension Fund

Actuarial Statement for 2018/19

The key demographic assumption was the allowance made for longevity. The life expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2016 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.75% p.a.

Based on these assumptions, the average future life expectancies at age 65 are as follows:

| | Males | Females |
|---------------------|-------|---------|
| Current Pensioners | 22.4 | 24.8 |
| Future Pensioners * | 24.8 | 27.8 |

*Aged 45 as at 31 March 2017

Copies of the 2017 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2017

Since the last formal valuation, real bond yields have fallen placing a higher value on the liabilities but there have been positive asset returns over the 2 years. Both events are of broadly similar magnitude with regards to the impact on the funding position.

The next actuarial valuation will be carried out as at 31 March 2020. The Funding Strategy Statement will also be reviewed at that time.

Richard Warden FFA
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
20 Waterloo Street
Glasgow
G2 6DB

26 April 2019



Statement of Accounting Policies and General Notes

1 Basis of preparation

The Financial Statements have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

The Financial Statements summarise the transactions of the funds for the 2018/19 financial year and report on the net assets available to pay pension benefits as at 31 March 2019. The Financial Statements do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present values of promised retirement benefits, valued on an International Accounting Standard (IAS) 19 basis, are disclosed in the Notes to the Financial Statements.

2 Summary of significant accounting policies

General

a) Basis of consolidation

i) Group accounts

Commencing with the year ended 31 March 2016, Consolidated Financial Statements have been prepared for Lothian Pension Fund. The Financial Statements of Scottish Homes Pension Fund continue to be prepared on a single entity basis.

The Consolidated Financial Statements for Lothian Pension Fund are prepared by combining the Financial Statements of the Fund (the parent entity) and its controlled entities (LPFE Limited and LPFI Limited) as defined in accounting standard IAS27 - Consolidated and Separate Financial Statements. Consistent accounting policies are employed in the preparation and presentation of the Consolidated Financial Statements. All inter-entity balances and transactions between entities, including any unrealised profits or losses, have been eliminated on consolidation.

Further details of the consolidation are provided in the Notes to the Financial Statements of Lothian Pension Fund.

LPFE Limited (LPFE) and LPFI Limited (LPFI) are wholly owned by the City of Edinburgh Council in its capacity as administering authority for the Local Government Pension Scheme in the Lothian area.



The purpose of LPFE is to provide staff services in respect of management of the Fund. LPFI's purpose is to provide FCA regulated services to the Fund and other Local Government Pension Scheme funds. It is considered appropriate to consolidate the Financial Statements of the two companies with those of Lothian Pension Fund.

ii) Lothian Buses Pension Fund merger

At its meeting on 26 March 2018, the Pensions Committee approved the merger of the assets and liabilities of the Lothian Buses Pension Fund into the Lothian Pension Fund, subject to the satisfactory completion of a revised admission agreement and shareholder guarantee. Having received the necessary admission agreement and shareholder guarantees the Lothian Buses Pension Fund assets were merged into Lothian Pension Fund on 1 February 2019.

Section 2.5 of the Code states that 'The combination of two or more local authorities into one new authority, or the transfer of functions from the responsibility of one authority to another, shall be accounted for under the principles that apply to group reconstructions and shall be accounted for as either a transfer by absorption or a transfer by merger.' 'Transfers by merger are rare transactions but may occur when legal transfers take place and management of the local government entity consider that in substance for a true and fair presentation of the local government entity the financial statements would be best presented as if the entity had always existed in its newly combined form.

The results and cash flows of all of the combining bodies (or functions) should be brought into the financial statements of the combined body from the beginning of the financial year in which the combination occurred.....'.

Specialist legal opinion had been sought prior to the merger of Lothian Buses Pension Fund. This concluded that "...Lothian Buses Pension Fund was set up as a 'further fund', within the meaning of the Local Government Superannuation (Funds) (Scotland) Regulations 1986 (the 'Funds Regulations')....At the time when the Admission Agreement was entered into, there was a clear mechanism under legislation whereby a 'further fund' could be dissolved and transferred back into the Main Fund." Also, "It is worth noting that, under the Admission Agreement..., Lothian Buses was admitted first of all to the Main Fund (immediately following which) the further Fund was set up".

Accordingly, with such assurance that "the newly combined body or functions has always existed", the consolidation of Lothian Buses Pension Fund "sub-fund" into Lothian Pension Fund has been accounted for by the 'transfer by merger'.



Fund account - revenue recognition

b) Contribution income

Normal contributions, both from the members and from employers, are accounted for on an accruals basis at the rate certified by the Scheme Actuary in the payroll period to which they relate.

Similarly, employer deficit funding contributions are accounted for on the due date on which they are payable as certified by the Scheme Actuary.

Employers' pensions strain contributions are accounted for in the period in which the liability arises. Any amount due but unpaid will be classed as a current financial asset. Amounts not due until future years are classed as long-term financial assets.

c) Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the Local Government Pension Scheme Regulations.

Individual transfers in/out are accounted for when received/paid, which is normally when the member liability is accepted or discharged.

Transfers in from members wishing to use the proceeds of their additional voluntary contributions to purchase scheme benefits are accounted for on a receipts basis and are included in transfers in.

Bulk (group) transfers are accounted for on an accruals basis in accordance with the terms of the transfer agreement.

d) Investment income

i) Interest income

Interest income is recognised in the Fund accounts as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination. Income includes the amortisation of any discount or premium, transaction costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

ii) Dividend income

Dividend income is recognised on the date the shares are quoted ex-dividend. Any amount not received by the end of the reporting period is disclosed in the Net Assets Statement as a current financial asset.



iii) Distributions from pooled funds

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the Net Assets Statement as a current financial asset.

iv) Income from unquoted private equity and infrastructure investments

Income from the above sources is recognised when it is notified by the manager. Distributions are split into capital and income elements with the latter being included under investment income in the Fund Account.

v) Property related income

Property-related income consists primarily of rental income. Rental income from operating leases on properties owned by Lothian Pension Fund is recognised on a straight-line basis over the term of the lease. Any lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

Rental income is reported gross with the operational costs of the properties included in investment management expenses.

Contingent rents based on the future amount of a factor that changes other than with the passage of time, such as turnover rents, are only recognised when contractually due.

vi) Movement in the net market value of investments

Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during the year.

Fund Account - expense items

e) Benefits payable

Pensions and lump sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the Net Assets Statement as current liabilities.

f) Taxation

i) Pension Funds

The Local Government Pension Scheme is a registered public service scheme under section 1(1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax is accounted for as a fund expense as it arises.



ii) Controlled entities - LPFE and LPFI

The Companies are mutual traders and are therefore not liable to corporation tax on any surpluses generated from services provided in respect of the Fund. The tax charges for the period are based on any profit for the period from non-mutual trade, adjusted for any non-assessable or disallowed items. They are calculated using tax rates that have been enacted or are substantively enacted by the period end date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Financial Statements. No deferred tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

g) Administrative expenses

All administrative expenses are accounted for on an accruals basis. The Lothian Pension Fund is responsible for administering the two Funds. The costs include charges from LPFE and LPFI for services rendered. The Fund receives an allocation of the overheads of the Council, this is based on the amount of central services consumed. In turn, these costs are allocated to the two Funds.

Costs directly attributable to a specific fund are charged to the relevant Fund. Investment management costs that are common to all funds are allocated in proportion to the value of each Fund as at the end of the year. Other administration costs are allocated in proportion to the number of members in each of the Funds at the end of the year.

h) Investment management expenses

All investment management expenses are accounted for on an accruals basis.

Fees of the external investment managers and custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.



For some investment managers, an element of their fee is performance related. The amount of any performance related fees paid is disclosed in the note to the accounts on investment management expenses provided for each Fund.

The cost of administering the Local Government Pension Scheme in the UK has come under increasing scrutiny in recent years. As a result, it has been decided to recognise investment management costs that are deducted from the value of an investment and recognised this as a cost in the Fund Account rather than as a reduction in the change in market value of investments. Investment transaction costs that are added to an investment purchase price or deducted from the proceeds of a sale are also recognised as a cost in the Fund Account rather than as a reduction in the change in market value of investments.

In June 2016, CIPFA revised and updated its guidance "Accounting for Local Government Pension Scheme Management Costs". Whilst the underlying principle of transparency of investment costs remains unchanged, there has been a degree of relaxation to full cost disclosure. Specifically, for complex "fund of funds" structures, the new guidance states that "Investment costs incurred by a separate legal entity, or in respect of investment decisions over which the pension fund has no control, should not be included in the (Pension) Fund Account.....If pension funds wish to provide information about the total cost of "fund of fund" investments, this should be included as part of the Investments section in the Annual Report".

The impact of this is that investment management costs deducted from any underlying fund in a "fund of funds" investment would not be included in the costs disclosed in the Fund Account. As this would significantly under-report investment management costs the decision has been made not to adopt this element of the CIPFA guidance. However, this type of cost is separately identified as "external management fees - deducted from capital (indirect)" in the notes on investment management expenses.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are not treated as an expense. Such costs are accounted for as part of the acquisition costs or sale proceeds.

The cost of obtaining investment advice from external consultants is included in investment management charges.

The costs of the in-house investment management team are charged to the Fund. The basis of allocation is as described in section g.

Securities lending revenue is reported gross and their fees are disclosed in investment management expenses.

i) Operating lease

Lease payments under an operating lease are recognised as an expense on a straight-line basis over the term of the lease. In accordance with Standard Interpretations Committee (SIC) 15, subsequently endorsed by the International Accounting Standards Board (IASB), lease incentives are recognised as a reduction in the lease expense over the term of the lease on a straight-line basis.



Net Assets Statement

j) Financial assets

Financial assets are included in the Net Assets Statement on a fair value basis as at the reporting date. A financial asset is recognised in the Net Assets Statement on the date the Fund becomes party to the contractual acquisition of the asset. From this date, any gains or losses arising from changes in the fair value of asset are recognised by the Fund.

The values of investments as shown in the Net Assets Statement have been determined at fair value in accordance with the requirements of the Code and IFRS13. For the purposes of disclosing levels of fair value hierarchy, the Fund has adopted the classification guidelines recommended in Practical Guidance on Investment Disclosures (PRAG/Investment Association, 2016).

The basis of the valuation of each class of investment assets is set out below. There has been no change in the valuation techniques used during the year. All assets have been valued using fair value techniques which represent the highest and best price available at the reporting date.

| Description of asset | Valuation hierarchy | Basis of valuation | Observable and unobservable inputs | Key sensitivity affecting the valuations provided |
|--------------------------------------|---------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------|---------------------------------------------------|
| Market quoted investments - Equities | Level 1 | Closing bid value on published exchanges | Not required | Not required |
| Exchange traded pooled investments | Level 1 | Closing bid value on published exchanges | Not required | Not required |
| Future derivative contracts | Level 1 | Determined using exchange prices at the reporting date. Amounts due from or owed to the broker are the amounts outstanding in respect of the initial margin and variation margin. | Not required | Not required |



| Description of asset | Valuation hierarchy | Basis of valuation | Observable and unobservable inputs | Key sensitivity affecting the valuations provided |
|--------------------------------------------------------------------------------------------------------|---------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Forward foreign exchange derivatives | Level 1 | Based on market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year-end with an equal and opposite contract. | Not required | Not required |
| Government bonds - fixed interest / index linked gilts | Level 2 | Recorded at net market value based on their current yields. | Evaluated price feeds | Not required |
| Freehold and leasehold properties | Level 3 | Valued at fair value at the year-end using the investment method of valuation by John Symes-Thompson FRICS of independent valuers, CBRE Ltd in accordance with RICS Valuation – Global Standards 2017 | Existing lease terms and rentals. Independent market research. Nature of tenancies. Covenant strength for existing tenants. Assumed vacancy levels. Estimated rental growth. Discount rate | Significant changes in rental growth, vacancy levels or the discount rate could affect valuations as could more general changes to market price |
| Unquoted Pooled investments – Private Equity, Infrastructure, Timber, Private Secured Loans & Property | Level 3 | Comparable valuation of similar companies in accordance with International Private Equity and Venture Capital Guidelines (2015) | EBITDA multiple Revenue multiple. Discount for lack of marketability. Control premium. | Valuations could be affected by material events occurring between the date of the financial statements provided and the Fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts. |



Sensitivity of assets valued at level 3

Having analysed historical data and current market trends, and consulted with independent investment advisers, the Fund has determined that the valuation methods described above are likely to be accurate to within the following ranges, and has set out below the consequent potential impact on the closing value of investments held at 31 March 2019.

| Lothian Pension Fund | Assessed Valuation range (+ or -) | Value at 31 March 2019 | Value on increase | Value on decrease |
|-----------------------|-----------------------------------|------------------------|-------------------|-------------------|
| <u>Unquoted</u> | | £m | £m | £m |
| Private Equity | 30% | 76.1 | 98.9 | 53.3 |
| Infrastructure | 12% | 844.9 | 946.3 | 743.5 |
| Timber | 18% | 124.0 | 146.3 | 101.7 |
| Private Secured Loans | 7.5% | 205.0 | 220.4 | 189.6 |
| Property | 13% | 461.0 | 520.9 | 401.1 |
| | | 1,711.0 | 1,932.8 | 1,489.2 |

Scottish Homes Pension Fund has no assets valued at Level 3.

k) Foreign currency transactions and balances

Dividends, interest and purchases and sales of investments in foreign currencies have been accounted for at the spot market rates at the date of the transaction. End-of-year spot market exchange rates are used to value cash balances held in foreign currency bank accounts, market values of overseas investments and purchases and sales outstanding at the end of the reporting period.

l) Cash and cash equivalents

Cash comprises cash in hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal risk of changes in value.

m) Financial liabilities

The Fund recognise financial liabilities at fair value as at the reporting date. A financial liability is recognised in the Net Assets Statement on the date the Fund becomes party to the liability. From this date, any gains or losses arising from changes in the fair value of the liability are recognised.



n) Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits of each of the Fund is assessed on an annual basis by the Scheme Actuary in accordance with the requirements of IAS 19 and relevant actuarial standards.

As permitted under IAS26, the Fund have opted to disclose the actuarial present value of promised retirement benefits by way of a note to the Net Assets Statements.

o) Additional voluntary contributions

The Lothian Pension Fund and Lothian Buses Pension Fund provide an additional voluntary contributions (AVC) scheme for their members, the assets of which are invested separately from those of the Fund. The Fund has appointed Standard Life and Prudential as their AVC providers. AVCs are paid to the AVC providers by employers and are specifically for providing additional benefits for individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and the movements in the year.

In accordance with regulation 5(2)(b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 1998, AVCs are not included in pension fund financial statements. Details of contributions paid and the total value of funds invested are disclosed by way of note.

p) Contingent assets and contingent liabilities

A contingent liability arises where an event has taken place prior to the year-end giving rise to a possible financial obligation whose existence will only be confirmed or otherwise by the occurrence of future events. Contingent liabilities can also arise in circumstances where a provision would be made, except that it is not possible at the balance sheet date to measure the value of the financial obligation reliably.

A contingent asset arises where an event has taken place giving rise to a possible asset whose existence will only be confirmed or otherwise by the occurrence of future events.

Contingent assets and liabilities are not recognised in the Net Assets Statement but are disclosed by way of narrative in the notes.

q) Employee benefits

The employees of LPFE are eligible to participate in Lothian Pension Fund.

In the Consolidated Financial Statements, the current service cost for the period is charged to the Fund Account. The assets of Lothian Pension Fund are held separately from those of the Company. The Company has fully adopted the accounting principles as required by IAS19 – Employee Benefits.

The liability recognised in the Net Asset Statement in respect of the defined benefit pension plan is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs.



The defined benefit obligation is calculated annually, by the Scheme Actuary, using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in a currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to the Fund Account in the period in which they arise.

Past-service costs are recognised immediately in the Fund Account, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

3 Accounting Standards that have been issued but not yet adopted

The Code requires the disclosure of information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted. This applies to the adoption of the following new or amended standards within the 2019/20 Code:

The Code requires implementation from 1 April 2019 and there is therefore no impact on the 2018/19 financial statements.

- Amendments to IAS 40 Investment Property: Transfers to Investment Property
- Annual Improvements to IFRS Standards 2014-2016 Cycle
- IFRIC 22 Foreign Currency Transactions and Advance Consideration
- IFRIC 23 Uncertainty over Income Tax Treatments
- Amendments to IAS 9 Financial Instruments

The amendments are generally minor or principally providing clarification. Overall, these new or amended standards are not expected to have a significant impact on the financial statements.

4 Critical judgements in applying accounting policies

Unquoted private equity and infrastructure investments

It is important to recognise the highly subjective nature of determining the fair value of private equity and infrastructure investments.

They are inherently based on forward-looking estimates and judgements involving many factors. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of IFRS.



For the Lothian Pension Fund, the value of unquoted private equity, infrastructure, timber and secured loan investments at 31 March 2019 was £1,250.0m (2018 £1,125.1m).

Actuarial present value of promised retirement benefits

Each Fund is required to disclose the estimated actuarial present value of promised retirement benefits as at the end of the financial year. These estimates are prepared by the Fund Actuary. These values are calculated in line with International Accounting Standard 19 (IAS19) assumptions and comply with the requirements of IAS26. However, the results are subject to significant variances based on changes to the underlying assumptions.

The figures are only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

5 Assumptions made about the future and other major sources of estimation uncertainty

The Financial Statements contain estimated figures that are based on assumptions made by the Council; private equity and infrastructure managers; other providers of valuation information; and the Scheme Actuary about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because amounts cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

The items in the Net Assets Statement at 31 March 2019 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

a) Actuarial present value of promised retirement benefits

Uncertainties

Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on the Fund's assets. The Fund Actuary advises on the assumptions to be applied and prepares the estimates.



Effect if actual results differ from assumptions - Lothian Pension Fund

The effects on the net pension liability of changes in individual assumptions can be illustrated as follows:

| Change in assumptions - year ended 31 March 2019 | Approx % increase in liabilities % | Approx monetary amount £m |
|--------------------------------------------------|---------------------------------------|------------------------------|
| 0.5% decrease in the real discount rate | 11 | 1,017 |
| 1 year increase in member life expectancy | 4 | 330 |
| 0.5% increase in salary increase rate | 2 | 166 |
| 0.5% increase in pensions increase rate | 8 | 782 |

Effect if actual results differ from assumptions - Scottish Homes Pension Fund

The effects on the net pension liability of changes in individual assumptions can be illustrated as follows:

| Change in assumptions - year ended 31 March 2019 | Approx % increase in liabilities % | Approx monetary amount £m |
|--------------------------------------------------|---------------------------------------|------------------------------|
| 0.5% decrease in the real discount rate | 5 | 7 |
| 1 year increase in member life expectancy | 4 | 6 |
| 0.5% increase in pensions increase rate | 5 | 7 |

b) Valuation of unquoted private equity and infrastructure investments

Uncertainties

These investments are not publicly listed and therefore there is a degree of estimation involved in their valuation, see 2j above for more details on the valuation methodology.



Effect if actual results differ from assumptions

There is a risk that these investments may be under or overstated in the accounts at any point in time. The actual financial return of this type of investment is only known with certainty when they reach the end of their lifecycles and the final distributions are made to investors. A sensitivity analysis can be found in note 2j above.

c) Quantifying the cost of investment fees deducted from capital

Uncertainties

Section 2 h) describes the accounting policy for investment management expenses in relation to expenses deducted from the capital value of investments. Quantification of these costs involves asking the relevant managers for information and only some of this information can be independently verified. In cases where the charges relate to an investment as a whole, an estimate needs to be made of the costs applicable to the holding owned by the relevant Fund.

Effect if actual results differ from assumptions

There is a risk that the cost of investment fees deducted from capital may be under or overstated. However, as the costs are included in the Fund Account by adjusting the change in market value of investments, any inaccuracy in the cost estimate will not change the reported net change in the Fund for the year.



Statement of responsibilities for the Annual Accounts

The responsibilities of the Administering Authority

The Administering Authority's responsibilities require it to:

- Make arrangements for the proper administration of the financial affairs of the Fund in its charge and to secure that one of its officers has the responsibility for the administration of those affairs. The Head of Finance serves as the Section 95 Officer for all the Council's accounting arrangements, including those of Lothian Pension Fund and Scottish Homes Pension Fund. For the Fund, this Section 95 responsibility has been delegated to the Chief Finance Officer, Lothian Pension Fund.
- Manage its affairs to secure economic, efficient and effective use of its resources and safeguard its assets.
- Ensure the Annual Accounts are prepared in accordance with legislation (The Local Authority Accounts (Scotland) Regulations 2014) and, so far as is compatible with that legislation, in accordance with proper accounting practices (section 12 of the Local Government in Scotland Act 2003).
- Approve the Audited Annual Accounts for signature.

HUGH DUNN
Head of Finance
The City of Edinburgh Council
25 September 2019

The responsibilities of the Chief Finance Officer, Lothian Pension Fund

The Chief Finance Officer, Lothian Pension Fund, is responsible for the preparation of the Fund's Financial Statements which, in terms of the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 (the Code of Practice), is required to present a true and fair view of the financial position of the Fund at the accounting date and their income and expenditure for the year (ended 31 March 2019).

In preparing this statement of accounts, the Chief Finance Officer, Lothian Pension Fund, has:

- Selected suitable accounting policies and then applied them consistently
- Made judgements and estimates that were reasonable and prudent
- Complied with the Code of Practice.



The Chief Finance Officer, Lothian Pension Fund, has also:

- Kept proper accounting records which were up to date
- Taken reasonable steps for the prevention and detection of fraud and other irregularities.

The Statement of Accounts presents a true and fair view of the financial position of the Fund as at 31 March 2019, and their income and expenditure for the year ended 31 March 2019.

JOHN BURNS, FCMA CGMA PgC
Chief Finance Officer
Lothian Pension Fund
25 September 2019



Independent auditor's report

to the members of City of Edinburgh Council as administering authority for Lothian Pension Fund and Scottish Homes Pension Fund and the Accounts Commission

Report on the audit of the financial statements

Opinion on financial statements

We certify that we have audited the financial statements in the annual report of Lothian Pension Fund and its group and Scottish Homes Pension Fund (the funds) for the year ended 31 March 2019 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Lothian Pension Fund Fund Account, the Lothian Pension Fund Net Assets Statement, the Scottish Homes Pension Fund Fund Account, the Scottish Homes Pension Fund Net Assets Statement and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 (the 2018/19 Code).

In our opinion the accompanying financial statements:

- give a true and fair view in accordance with applicable law and the 2018/19 Code of the financial transactions of the funds during the year ended 31 March 2019 and of the amount and disposition at that date of their assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2018/19 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Basis for opinion

We conducted our audit in accordance with applicable law and International Standards on Auditing (UK) (ISAs (UK)) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report. We were appointed by the Accounts Commission on 31 May 2016. The period of total uninterrupted appointment is three years. We are independent of the funds in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. Non-audit services prohibited by the Ethical Standard were not provided to the council. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.



Conclusions relating to going concern basis of accounting

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Chief Finance Officer has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the funds' ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Risks of material misstatement

We have reported in a separate Annual Audit Report, which is available from the Audit Scotland website, the most significant assessed risks of material misstatement that we identified and our conclusions thereon.

Responsibilities of the Chief Finance Officer and the City of Edinburgh Council for the financial statements

As explained more fully in the Statement of Responsibilities for the Annual Accounts, the Chief Finance Officer is responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Chief Finance Officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Chief Finance Officer is responsible for assessing the funds' ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless deemed inappropriate.

The City of Edinburgh Council is responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of the auditor's responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.



Other information in the annual report

The Chief Finance Officer is responsible for the other information in the annual report. The other information comprises the information other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except on matters prescribed by the Accounts Commission to the extent explicitly stated later in this report.

In connection with our audit of the financial statements, our responsibility is to read all the other information in the annual report and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Report on other requirements

Opinions on matters prescribed by the Accounts Commission

In our opinion, the audited part of the Remuneration Report has been properly prepared in accordance with The Local Authority Accounts (Scotland) Regulations 2014.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with statutory guidance issued under the Local Government in Scotland Act 2003;
- the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016); and
- the information given in the Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations 2018.

Matters on which we are required to report by exception

We are required by the Accounts Commission to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.



Conclusions on wider scope responsibilities

In addition to our responsibilities for the annual accounts, our conclusions on the wider scope responsibilities specified in the Code of Audit Practice, including those in respect of Best Value, are set out in our Annual Audit Report.

Use of our report

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 120 of the Code of Audit Practice, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Nick Bennett (for and on behalf of Scott-Moncrieff Audit Services)

Exchange Place 3

Semple Street

Edinburgh

EH3 8BL

25 September 2019



Annual Governance Statement

Roles and responsibilities

The City of Edinburgh Council (the Council) has statutory responsibility for the administration of the Local Government Pension Scheme (LGPS) in the Lothian area of Scotland. This responsibility is for two separate funds: the Lothian Pension Fund and Scottish Homes Pension Fund (the Fund). The Lothian Pension Fund group comprises the investment and pensions team employed by LPFE Limited (LPFE) supporting the Council in its separate statutory capacity as the administering authority of the Fund (Administering Authority) and LPFI Limited (LPFI), the Group's regulated investment vehicle (together the LPF Group).

The main functions of the Administering Authority are administration of scheme benefits and the investment of the assets of the Fund. These functions are conducted in accordance with the Local Government Pension Scheme (Scotland) Regulations which are statutory instruments made under the Superannuation Act 1972. The role of Administering Authority is carried out via:

- the Pensions Committee and the Pensions Audit Sub-Committee
- the Pension Board
- the Joint Investment Strategy Panel; and
- the LPF Group.

Further details on the above arrangements can be found in the Governance section of the Management Commentary towards the front of this document.

Scope of responsibility

As the Administering Authority of the Fund, the Council is responsible for ensuring that its business in administering the Fund, is conducted in accordance with the law and appropriate standards, and that monies are safeguarded, properly accounted for, and used economically, efficiently and effectively. The Council also has a statutory duty under the Local Government in Scotland Act 2003, to make arrangements to secure best value, which is defined as continuous improvement in the way its functions are carried out.

In discharging these overall responsibilities, elected members, senior officers and external representatives are responsible for implementing effective arrangements for governing the affairs of the LPF Group, and facilitating the effective exercise of its functions, including arrangements for the management of risk. The Pensions Committee oversees the operational administration of the Fund by the LPF Group.

The LPF Group has adopted a Local Code of Corporate Governance that is consistent with the principles of the Chartered Institute of Public Finance and Accountancy (CIPFA) and Society of Local Authority Chief Executives (SOLACE) framework 'Delivering Good Governance in Local Government'.

This statement explains how the LPF Group has complied with the Local Code of Corporate Governance and how it meets the CIPFA Code of Practice on Local Authority Accounting in the United Kingdom.



The governance framework

The LPF Group operates within the wider governance framework of the Council but within specific ringfenced governance structures focused on the Fund themselves. The governance framework comprises the systems, controls, processes, cultures and values by which the LPF Group directs and controls the Fund. It also describes the way the LPF Group engages with and accounts to its stakeholders in relation to the management of the administration of the Fund. It enables the LPF Group to monitor the achievement of its objectives and consider whether those objectives have led to the delivery of appropriate, cost-effective services. The framework also applies to any subsidiary companies which are members of the LPF Group, namely LPFI and LPFE. The LPF Group is also directly regulated by The Pensions Regulator, the Financial Conduct Authority (regarding its regulated investment activity), the Scottish Information Commissioner and is subject to other corporate and public sector rules and regulations.

The LPF Group's ongoing compliance with its governance framework and regulatory obligations is monitored on an ongoing basis by the Pensions Committee, the Audit Sub-Committee and the Pension Board and the respective boards of LPFI and LPFE.

The wider Council's Local Code of Corporate Governance is regularly reviewed and considered by the Governance, Risk & Best Value Committee. It has implemented arrangements for monitoring each element of the framework and providing evidence of compliance. The Council's Democracy, Governance and Resilience Senior Manager reviewed the arrangements and is satisfied that the Code continues to be adequate and effective. Internal Audit has also reviewed the annual assurance questionnaire process in relation to Arms-Length Companies and has found that this provides the Chief Executive Officer with a level of assurance on the adequacy of the governance arrangements. The Council's Corporate governance framework meets the principles of effective governance.

The LPF Group places reliance upon certain of the internal financial controls within the Council's financial systems and the monitoring in place to ensure the effectiveness of these controls. The relevant key elements of the LPF Group and the Fund governance framework within the Council, include:

- Identifying the objectives of the Fund in the Funding Strategy Statement, Statement of Investment Principles, Pension Administration Strategy and Service Plan.
- Since April 2015, The Pensions Regulator has been responsible for setting standards of governance and administration for the Local Government Pension Scheme. The LPF Group has taken steps to fully integrate compliance with these standards within the overall governance framework.
- A systematic approach to monitoring service performance by the Pensions Committee, Pensions Audit Sub-Committee, Pension Board (each including external stakeholder representation), Independent Professional Observer and senior officers.
- A structured programme to ensure that Pensions Committee and Pension Board members have the required standard of knowledge and understanding of Local Government Pension Scheme matters.
- Operating within clearly established investment guidelines defined by the Local Government Pension Scheme Investment Regulations and the Fund's Statement of Investment Principles.



- Compliance with the CIPFA Principles for Investment Decision Making and Disclosure in the Local Government Pension Scheme.
- With the exception of managed funds, unlisted investments and property, all investments are held under custody by a global custodian. The Fund benefits from the custodian's extensive internal control framework.
- Benchmarking of services in terms of standards and cost against other pension funds.
- LPFE and LPFI operating within their respective constitutional documentation and the relevant companies regulations.
- LPFI operating within the relevant governance policies and procedures to ensure compliance with the Financial Conduct Authority's rules, regulations and guidance.
- For LPF Group and Fund matters, the Pensions Committee, Pensions Audit Sub-Committee and Pension Board are responsible for scrutiny and challenge and a quarterly risk reporting process is in place to ensure full consideration of such matters.
- Officers of the LPF Group are managed separately through the processes and procedures of LPFE, overseen by its board of directors, with terms and conditions and a human resources performance review and management strategy tailored to the express needs of the Fund and their stakeholders.
- The directors of LPFE and LPFI have obligations to report to the Pensions Committee as the governing body for the Fund and Council in being the sole shareholder. In addition, the board and staff of LPFI are each individually regulated by the Financial Conduct Authority and so bound by the associated Principles and Standards of governance best practice.

Elements of the governance framework of the Council that are relevant to the LPF Group and Fund include:

- The Council is embedding a culture of commercial excellence to ensure that its services always deliver Best Value. That is ongoing and seeks to improve standards in buying practices and processes across the Council including, to the extent applicable, the LPF Group and the Fund which bear the cost of its operation and administration
- The submission of reports, findings and recommendations from the external auditor, other inspectorates and internal audit, to the Pensions Committee, Pensions Audit Sub-Committee for all matters affecting the LPF Group and Fund and, in certain circumstances strictly for Council wide oversight purposes, the Corporate Leadership Team, Governance, Risk and Best Value Committee and wider Council.
- The roles and responsibilities of Elected Members and Officers are defined in Procedural Standing Orders, Committee Terms of Reference and Delegated Functions, Contract Standing Orders, Scheme of Delegation to Officers, the Member/officer protocol and Financial Regulations. These are subject to annual review.
- The Chief Executive Officer has overall accountability to Council, for all aspects of operational management and overall responsibility for ensuring the continued development and improvement of systems and processes concerned with ensuring appropriate direction, accountability and control.
- The Section 95 Officer has overall responsibility for ensuring appropriate advice is given to the Council and the LPF Group on all financial matters, keeping proper financial records of accounts and maintaining an effective system of internal financial control. For the Fund, the Section 95 officer responsibility has been sub-delegated to the Chief Finance Officer of the LPF Group.



- The Chief Internal Auditor has overall responsibility to review, appraise and report to management and the Governance, Risk and Best Value Committee, and for matters relating to the LPF Group and Fund to the Pensions Committee and Pensions Audit Sub-Committee, on the adequacy of relevant internal control and corporate governance arrangements and on risks relating to approved policies, programmes and projects.
- The Council's Democracy, Governance and Resilience Manager, reporting to the Head of Strategy and Communications, has responsibility for advising the Council on corporate governance arrangements and supports the LPF Group on certain aspects of its governance arrangements.
- The Governance, Risk and Best Value Committee, and for LPF Group and Fund matters the Pensions Committee and Pensions Audit Sub-Committee, provides the Council with independent assurance of the adequacy of the governance and risk management frameworks and internal control environment. Also providing independent scrutiny of financial and non-financial performance, approving and monitoring the progress of the Internal Audit risk-based plan, and monitoring performance of the internal audit service.
- The risk management policy and framework set out the responsibilities of elected members, Governance, Risk and Best Value Committee, and for LPF Group and Fund matters the Pensions Committee and Pensions Audit Sub-Committee, management and staff for the identification and management of risks to corporate and service related priorities;
 - The Resources and Chief Executive's Risk Register and Council Risk Register all identify risks and proposed treatment and actions. These registers are regularly reviewed, updated and reported to the Corporate Leadership Team, which reviews Council-wide risk and reports to the Governance, Risk and Best Value Committee for scrutiny and challenge.
 - Resilience and business continuity plans are in place for all essential Council services. These set out arrangements for continuing to deliver essential services in the event of an emergency or other disruption.
 - Senior management and Heads of Service have formal objectives, with performance reviewed by the appropriate chief officer. Officers have personal work objectives and receive feedback on their performance through the Council-wide performance review and development process.
 - An Elected Members remuneration and expenses scheme is in place and is consistent with the Scottish Government's 'Councillors Remuneration: allowances and expenses – Guidance'. Information on the amounts and composition of elected members salaries, allowances and expenses is published on the Council's website.
 - The Council's Democracy, Governance and Resilience Senior Manager ensures that induction training on roles and responsibilities, and ongoing development opportunities, are provided for Elected Members. A separate policy on Pensions Committee and Pension Board member training has been adopted and is overseen by the LPF Group's officers.
 - Mandatory training for Councillors newly appointed to the Pensions Committee is programmed within the Induction and Training programme for Elected Members. This focuses on governance, investment management and strategy and how the LPF Group and Fund work. Committee members are reminded of the requirement to undertake a minimum of 21 hours of training per financial year to fulfil their role on the Pensions Committee.
 - Codes of Conduct, that set out the standards of behaviour expected from Elected Members and officers, are in place.



- The Employee Code of Conduct, Anti Bribery Policy and Policy on Fraud Prevention set out the responsibilities of officers and Elected Members in relation to fraud and corruption, and are reinforced by the Councillors' Code of Conduct, the Code of Ethical Standards and the Financial Regulations. The LPF Group has adapted policies to take into account the specific nature of its business and regulation.
- The Whistleblowing policy provides a process for disclosure in the public interest about the Council and its activities by officers, Elected Members and others. The LPF Group has an adapted policy to take into account the specific nature of its business and regulation.
- A Register of Members' Interests and Registers of Officers' interests are maintained and available for public inspection.

A significant element of the governance framework is the system of internal controls, which is based on an ongoing process to identify and prioritise risks to the achievement of the Council's objectives, including those relevant to the LPG Group and Fund. Following the establishment of the wholly-owned subsidiary companies, LPFE and LPFI, the Council continues to have appropriate assurance processes and procedures in relation to the responsible officers involved in the administration of those companies and so the wider LPF Group administering the Fund.

Review of Effectiveness

The Local Code of Governance details the Council's arrangements for monitoring each element of the framework and providing evidence of compliance. The Council's Governance and Democratic Services Manager has reviewed the effectiveness of the Code.

The Chief Internal Auditor has also provided an assurance statement on the effectiveness of the system of internal control. The opinion in the assurance statement states: "Internal Audit considers that the LPF control environment and governance and risk management frameworks are generally adequate but with enhancements required and is therefore reporting a 'amber' rated opinion, with our assessment towards the middle of this category."

In compliance with standard accounting practice, the Head of Finance, of the City of Edinburgh Council has provided the Chief Executive Officer with a statement of the effectiveness of the Group's internal financial control system for the year ended 31st March 2019. It is the Head of Finance's opinion that "... that although a degree of assurance can be placed upon the adequacy and effectiveness of the Group's systems of internal financial control, further improvements, including embedding of actions taken in response to previous recommendations, are still required.

In this context, I would particularly highlight improvements in train to address a number of systemic weaknesses in respect of payroll-related controls, including those to address historic, and prevent recurring, overpayments."

The Chief Finance Officer of the LPF Group has provided a statement of the effectiveness of the internal financial control system for the year ended 31st March 2019 for the Fund. It is the Chief Finance Officer's opinion "that reasonable assurance can be placed upon the adequacy and effectiveness of the system of internal financial control for the LPF Group in administering the Lothian Pension Fund and Scottish Homes Pension Fund".



Certification

It is our opinion, in light of the foregoing, that reasonable assurance can be placed upon the adequacy and effectiveness of the systems of governance that operate within the LPF Group in its administration of the Fund. We consider the governance and internal control environment operating during the financial year from 1 April 2017 to 31 March 2019 to provide reasonable and objective assurance that any significant risks impacting on the LPF Group and its ability to achieve its objectives in properly administering the Fund have and will continue to be identified and suitably proportionate actions have and will be taken to avoid or mitigate the impact of any such risks.

The LPF Group has identified certain key areas for improvement, summarised as follows:

- ICT: Continuing to engage with ICT service provider and the City of Edinburgh Council to monitor and drive improvements in the ICT services which the LPF Group receives, whilst in tandem continuing to assess the position around the LPF Group procuring a separate ICT provider to solely and independently service its specific ICT requirements in support of its strategic business plan.
- Human resources: To continue to implement the new human resources strategy specific to LPF Group's requirements.
- Pension Board: To ensure that vacancies in the Pension Board are filled timeously and by suitable candidates and that this body of external stakeholder representatives receives the training and support that it requires on an ongoing basis.
- Business continuity: To continue to assess and refresh the business continuity plan on an ongoing basis ensuring sufficient engagement with staff.
- Information governance: Having completed a full information governance compliance project prior to the implementation of new data protection laws on 25 May 2018, to continue to implement ongoing actions to ensure continuing best practice information governance and security within the LPF Group, including monitoring and engaging with third party suppliers where appropriate.
- Financial services regulatory compliance: To continue to instruct external compliance audits on the operations and governance of LPFI in order to ensure best practice compliance and assurance around its existing operations (and in preparation for its extended collaborative business model) and take action to address the recommendations from those audits on an ongoing basis.
- Wider governance: To continue to maintain and reinforce separate governance and controls specific to the needs of the LPF Group, the pensions funds it administers and its distinct duties to employer and member stakeholders; consistently throughout the LPF Group's governance structures. To ensure that oversight by the City of Edinburgh Council is supported in a manner consistent with these duties.



The LPF Group will continue to ensure that these are treated as a priority and that progress towards implementation will be reviewed through the governance structures and processes established for the LPF Group and summarised herein.

ANDREW KERR
Chief Executive Officer
The City of Edinburgh Council
25 September 2019

DR STEPHEN S MOIR
Executive Director of Resources
The City of Edinburgh Council
25 September 2019

DOUG HERON
Chief Executive Officer
Lothian Pension Fund
25 September 2019



Governance Compliance Statement

The Regulations that govern the management of Local Government Pension Scheme in Scotland require that a Governance Compliance Statement is published. This statement sets out the extent to which governance arrangements comply with best practice.

The statement below describes arrangements at 31 March 2019 and over the financial year.

| Principle | | Full Compliance | Comments |
|-----------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Structure | The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing Council. | Yes | The City of Edinburgh Council acts as administering authority and delegates all pension scheme matters to a committee of seven members (Pensions Committee) made up as follows: <ul style="list-style-type: none"> - Five City of Edinburgh Council elected members - Two external members, one drawn from the membership of the Fund and one drawn from the employers that participate in the Fund. |
| | That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee. | Yes | The Pensions Committee includes two external places for pension fund stakeholders i.e. one each from the employer and member representatives. <p>Fund members and employers are also represented within the Fund's Pension Board. Membership includes five employer representatives and five member representatives.</p> <p>All members of the Pension Board are invited to attend the meeting of the Pensions Committee and receive the relevant papers prior to those meetings.</p> <p>Two members of the Pension Board attend the Pensions Audit Sub-Committee.</p> |



| Principle | | Full Compliance | Comments |
|----------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Structure | That where a secondary committee or board has been established, the structure ensures effective communication across both levels. | Yes | <p>The Pensions Audit Sub-Committee, consisting of three members of the Pensions Committee, report to the Pensions Committee on their findings and recommendations. Two members of the Pension Board attend the Pensions Audit Sub-Committee in a non-voting capacity. The Pension Board attends the Pensions Committee meetings and takes part in training events.</p> <p>Implementation of investment strategy is delegated to the Executive Director of Resources who then delegates to the Head of Finance, who takes advice from the Joint Investment Strategy Panel. The Panel meets quarterly and reports to the Pensions Committee annually.</p> <p>The advisers on the Joint Investment Strategy Panel consists of the Chief Investment Officer and on other portfolio manager of LPFI plus two experienced independent external industry advisers.</p> <p>The Pensions Committee receives annual updates from LPFE and LPFI.</p> |
| Representation | That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include employing authorities (including non-scheme employers, e.g. admitted bodies) and scheme members (including deferred and pensioner scheme members). | Yes | <p>The Pension Board consists of a mix of representatives:</p> <ul style="list-style-type: none"> - Five employer representatives from non-administering authority employers; - Five member representatives appointed by the Trade Unions in accordance with the approach required under Scottish statute. |
| | Where appropriate, independent professional observers, and expert advisers (on an ad-hoc basis). | Yes | <p>An Independent Professional Observer was appointed in March 2013 to help Committee scrutinise advice. This contract expired in February 2018 and a new Observer was appointed in September 2018.</p> |



| Principle | | Full Compliance | Comments |
|-----------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Representation | Where appropriate, independent professional observers, and expert advisers (on an ad-hoc basis). | Yes | <p>As mentioned previously, external investment advisers sit on the Joint Investment Strategy Panel.</p> <p>A separate specialist Pensions Audit Sub-Committee consisting of three members (including at least two elected members from the City of Edinburgh Council) undertake the audit scrutiny of the funds.</p> <p>A non-executive director was appointed to the board of LPFI on 7 February 2017 and LPFE on 19 March 2018.</p> <p>An external compliance consultant supports the LPF Group on its ongoing compliance with the Financial Conduct Authority rules, regulations and guidance.</p> |
| | That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision-making process, with or without voting rights. | Yes | <p>The Pension Board attends the Pensions Committee meetings to help ensure that the operation of the pension funds is in accordance with the applicable law and regulation. The Pension Board takes part in all Committee training events.</p> <p>The Pensions Committee takes account of the views of the Pension Board when making decisions.</p> |
| Selection and Role of Lay Members | That committee or board members are made fully aware of the status, role and function that they are required to perform on either a main or secondary committee. | Yes | <p>A comprehensive training programme including induction is in place. Members of the Pensions Committee and Pension Board are expected to attend no less than three days of training (21 hours) per year.</p> <p>The non-elected members confirm that they have read, signed and will abide by a Code of Conduct (specifically tailored for the Pensions Committee and Pension Board) prior to their appointment to those bodies.</p> <p>The elected members are required to read, sign and abide by the Councillors' Code of Conduct.</p> |



| Principle | | Full Compliance | Comments |
|-------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Selection and Role of Lay Members | That at the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda. | Yes | <p>The declaration of members' interests is a standard item on the agenda for meetings of the Pensions Committee, Pensions Audit Sub-Committee and Pension Board.</p> <p>A Code of Conduct also applies to all members of the Pensions Committee and the Pension Board. The declaration of board members interest is a standard item on the agenda for the meetings for the LPFE and LPFI board meetings.</p> |
| Voting | The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees. | Yes | <p>Five of the seven places of the Pensions Committee are held by elected members of the City of Edinburgh Council, which is required to retain a 2/3 majority in line with the Local Government (Scotland) Act 1973.</p> <p>The LPF Group's Nomination and Appointments Policy clearly documents how employer and member representatives will be elected to the Pensions Committee and Pension Board.</p> <p>LPFI and LPFE board members conduct meetings and other matters in accordance with their respective articles of association and shareholders' agreements.</p> |
| Training / Facility Time / Expenses | a) That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process. | Yes | <p>A Training and Attendance Policy is in place covering training requirements and reimbursement of expenses. The policy is available on the LPF Group's website www.lpf.org.uk.</p> <p>Board members and staff working for LPFI and LPFE also attend separate training for the purposes of their knowledge, understanding and (where appropriate) compliance with Financial Conduct Authority regulations.</p> |
| | b) That where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum. | Yes | <p>The Training and Attendance Policy applies to both the Pensions Committee and the Pension Board. Advisers have their own professional development obligations.</p> |



| Principle | | Full Compliance | Comments |
|-------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Training / Facility Time / Expenses | c) That the administering authority considers the adoption of annual training plans for committee and board members and maintains a log of all such training. | Yes | Each Pensions Committee and Pension Board member is expected to attend no less than three days training per year (21 hours) per year. Attendance at meetings and training is monitored and reported. |
| Meetings frequency | a) That an administering authority's main committee or committees meet at least quarterly. | Yes | The Pensions Committee meets at least four times a year. |
| | b) That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committees sits. | Yes | The Pensions Audit Sub-Committee is held before the Pensions Committee at least three times a year with further meetings held if necessary. The Joint Investment Strategy Panel meets quarterly or more frequently as required. The Pension Board attends all the Pensions Committee meetings and separately meets in advance of such meetings. Further meetings are held if necessary. The LPFE board now meet five time a year (in February, May, August, October and December) and the LPFI board at least quarterly. |
| | c) That an administering authority who does not include lay members in their formal governance arrangements must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented. | Not applicable | |
| Access | That subject to any rules in the council's constitution, all members of main and secondary committees or boards have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee. | Yes | Pensions Committee papers and minutes are publicly available on the Council's website and all Pensions Committee and Pension Board members have equal access. Members of the Pensions Committee and Pension Board have equal access to the Independent Professional Observer who holds surgeries ahead of Committee meetings. |



| Principle | | Full Compliance | Comments |
|-----------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Scope | That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements. | Yes | <p>The Pensions Committee deals with all matters relating to both the administration and investment of the Fund and the LPF Group.</p> <p>A separate specialist Pensions Audit Sub-Committee consisting of three members (including at least two elected members from the City of Edinburgh Council) undertake the audit scrutiny of the Fund.</p> |
| Publicity | That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express an interest in wanting to be part of those arrangements. | Yes | Governance documents, policies and details of Pension Board membership are on the LPF Group's website. The LPF Group also communicates regularly with employers and scheme members. |

ANDREW KERR
Chief Executive Officer
The City of Edinburgh Council
25 September 2019

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The City of Edinburgh Council
25 September 2019

DOUG HERON
Chief Executive Officer
Lothian Pension Fund
25 September 2019



REMUNERATION REPORT

Remuneration Policy for Employees

Officers and employees of Lothian Pension Fund are employed by LPFE, an arms-length organisation owned by the City of Edinburgh Council, the administering authority for the Lothian Pension Fund. In recent years LPFE has been incorporated as a standalone entity to allow the Fund to compete with private sector investment management firms for recruitment and retention of skilled and experienced investment managers and analysts.

Operating this model allows Lothian Pension Fund to achieve significantly lower costs, and therefore improved net returns or lower investment risk, than would be possible by appointing private sector asset managers to invest the Fund's assets. The LPFE Board acts as a Remuneration Committee for officers and employees determining pay arrangements based on comparison to well-researched market benchmarks and performance against pre-agreed performance targets, and always linked to the principle of delivering value-for-money for the members of the Fund and their sponsoring employers.

Each year the Fund participates in a range of benchmarking exercises to measure operating costs and net investment returns against peers and indices relevant to the investment strategy, and this information is reported to the oversight bodies who review pay arrangements and terms of appointments of officers. Pay arrangements in LPFE reflect the market for investment expertise and recognise the qualifications and experience levels required to perform the roles and, more fundamentally, represent value-for-money for employee members and their sponsoring employers who bear the costs of operating the pension fund and securing retirement benefits.

Number of Employees by Pay Band

The numbers of employees whose remuneration during the year exceeded £50,000 were as follows:

| Remuneration Bands | 2017/18 | 2018/19 | Remuneration Bands | 2017/18 | 2018/19 |
|--------------------|---------|---------|-------------------------------|---------|---------|
| £50,000 - £54,999 | 1 | 1 | £95,000 - £99,999 | 1 | 1 |
| £55,000 - £59,999 | 3 | 3 | £100,000 - £104,999 | 1 | 2 |
| £60,000 - £64,999 | 1 | 1 | £105,000 - £109,999 | - | 2 |
| £65,000 - £69,999 | 1 | - | £110,000 - £114,999 | - | - |
| £70,000 - £74,999 | 2 | - | £115,000 - £119,999 | - | - |
| £75,000 - £79,999 | 2 | 1 | £120,000 - £124,999 | - | - |
| £80,000 - £84,999 | 1 | 1 | £125,000 - £129,999 | - | 1 |
| £85,000 - £89,999 | 3 | - | £130,000 - £134,999 | - | 4 |
| £90,000 - £94,999 | - | - | | | |
| | | | Total No. of Employees | 16 | 17 |

During the year, the company introduced three variable pay schemes, two of which have vesting periods. The Portfolio Manager and Senior Management schemes entitle staff to receive an assessed percentage of their salary as an additional variable pay award if they meet certain objectives during the year. The assessment year runs from 1 February 2018 to 31 January 2019. The award then vests over three years.



The first part is payable at the end of the first year if the objectives are met and the remaining two parts are payable in the following two years if the requirement that the employee is still employed by the company at such time is met. Payment one has been made in January 2019. A liability has been raised at 31 March 2019 for the 2 months of service which the employees have delivered with regards to the second and third payments in the scheme.

Senior Employees Remuneration

The remuneration paid to the Fund's senior employees is as follows:

| | Total Remuneration 2017/18 | Salary, Fees and Allowances | Variable Remuneration | Total Remuneration 2018/19 |
|---------------------------------------------------------------------------|----------------------------|-----------------------------|-----------------------|----------------------------|
| Name and Post Title | £000 | £000 | £000 | £000 |
| Doug Heron, Chief Executive Officer (from February 2019)* | - | 18 | - | 18 |
| Clare Scott, Chief Executive Officer (to December 2018)** | 101 | 80 | - | 80 |
| Bruce Miller, Chief Investment Officer | 96 | 106 | 26 | 132 |
| John Burns, Chief Finance Officer | 76 | 82 | 20 | 102 |
| Struan Fairbairn, Chief Risk Officer (Head of Legal, Risk and Compliance) | 76 | 81 | 19 | 100 |
| | 349 | 367 | 65 | 432 |

* Full time equivalent for 2018/19 £108,000

** Full time equivalent for 2018/19 £108,000

The senior employees detailed above have responsibility for management of the LPF group to the extent that they have power to direct or control the major activities of the group (including activities involving the expenditure of money), during the year to which the Remuneration Report relates, whether solely or collectively with other persons.

Senior officers of the City of Edinburgh Council are also fully remunerated via the Council and no additional remuneration is paid by the Fund. This remuneration is disclosed in the Financial Statements of the City of Edinburgh Council.

Senior Employees Pension Entitlement

Pension benefits for employees are provided through the Local Government Pension Scheme.

For employees the Local Government Pension Scheme became a career average pay scheme on 1 April 2015. Benefits built up to 31 March 2015 are protected and based on final salary. Accrued benefits from 1 April 2015 will be based on career average salary.



The Scheme's normal retirement age for employees is linked to the State Pension Age (with a minimum of age 65).

From 1 April 2009, a five-tier contribution system was introduced with contributions from Scheme members being based on how much pay falls into each tier. This is designed to give more equality between the cost and benefits of scheme membership. Prior to 2009, contributions rates were set at 6% for all non-manual employees.

The tiers and members' contribution rates for 2018/19 were as follows:

| Pensionable Pay (2018/2019) | Rate (%) |
|----------------------------------------------------------------------------|----------|
| On earnings up to and including £21,300 (2017/2018 £20,700) | 5.5% |
| On earnings above £21,300 and up to £26,100 (2017/2018 £20,700 to £25,300) | 7.25% |
| On earnings above £26,100 and up to £35,700 (2017/2018 £25,300 to £34,700) | 8.5% |
| On earnings above £35,700 and up to £47,600 (2017/2018 £34,700 to £46,300) | 9.5% |
| On earnings of £47,600 and above (2017/2018 £46,300) | 12% |

If a person works part-time, their contribution rate is worked out on the whole-time pay rate for the job, with actual contributions paid on actual pay earned.

There is no automatic entitlement to a lump sum. Members may opt to give up (commute) pension for lump sum up to the limit set by the Finance Act 2004.

The value of the accrued benefits has been calculated on the basis of the age at which the person will first become entitled to receive a pension on retirement without reduction on account of its payment at that age; without exercising any option to commute pension entitlement into a lump sum; and without any adjustment for the effects of future inflation.

The pension figures shown relate to the benefits that the person has accrued as consequence of their total local government service, and not just their current appointment.



The pension entitlement of the LPF Group's senior employees is as follows:

| | In-year Pension Contributions | | | Accrued Pension Benefits | |
|------------------------------------------------------------------------------|-------------------------------|-----------|----------|--------------------------|-----------------------------|
| | 2017/18 | 2018/19 | | As at 31 March 2019 | Increase from 31 March 2018 |
| Name and post title | £000 | £000 | | £000 | £000 |
| Doug Heron, Chief Executive Officer (from February 2019) | - | 4 | Pension | - | - |
| | | | Lump Sum | - | - |
| Clare Scott, Chief Executive Officer (to December 2018) | 21 | 19 | Pension | 23 | 3 |
| | | | Lump Sum | 14 | 1 |
| Bruce Miller, Chief Investment Officer | 20 | 27 | Pension | 29 | 7 |
| | | | Lump Sum | 28 | 7 |
| John Burns, Chief Finance Officer | 16 | 21 | Pension | 41 | 7 |
| | | | Lump Sum | 78 | 12 |
| Struan Fairbairn, Chief Risk Officer (Head of Legal, Risk and Compliance) | 16 | 21 | Pension | 10 | 2 |
| | | | Lump Sum | - | - |
| Total | 73 | 92 | | | |

Exit Packages

Exit packages include compulsory and voluntary redundancy costs, pension contributions in respect of added years, ex-gratia payments and other departure costs. There was no payment of any exit packages in 2018/19 or in the previous year.

All information disclosed in the above tables at paragraphs in this Remuneration Report has been audited. The other sections of the Remuneration Report have been reviewed by the appointed auditor to ensure that they are consistent with the annual accounts.

Remuneration for Councillors on the Pensions Committee

Councillors on the Pensions Committee are remunerated by the City of Edinburgh Council, no additional remuneration is paid by the Fund.

ANDREW KERR
Chief Executive Officer
The City of Edinburgh Council
25 September 2019

DR STEPHEN S MOIR
Executive Director of Resources
The City of Edinburgh Council
25 September 2019

JOHN BURNS
Chief Finance Officer
Lothian Pension Fund
25 September 2019



Additional information

Key documents online

You can find further information on what we do and how we do it, on our website at www.lpf.org.uk. To view individual policy documents, click on the links below if viewing online or visit www.lpf.org.uk/publications.

- [Actuarial Valuation reports](#)
- [Pension Board constitution](#)
- [Annual Report and Accounts](#)
- [Statement of Investment Principles](#)
- [Pension Administration Strategy](#)
- [Communications strategy](#)
- [Funding Strategy Statement](#)
- [Service Plan](#)
- [Training and attendance policy](#)

Fund advisers

| | |
|----------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------|
| Actuaries: | Hymans Robertson LLP, Exchange Place One, 1 Semple Street, Edinburgh, EH3 8BL |
| Bankers: | Royal Bank of Scotland, 36 St Andrew Square, Edinburgh, EH2 2YB |
| Investment consultancy: | Gordon Bagot and Scott Jamieson |
| Investment custodians: | The Northern Trust Company, 50 Bank Street, Canary Wharf, London, E14 5NT |
| Investment managers: | Details can be found in the notes to the accounts. |
| Additional Voluntary Contributions (AVC) managers: | Standard Life, Standard Life House, 30 Lothian Road, Edinburgh, EH1 2DH Prudential plc, 1 Angel Court, London, EC2R 7AG |
| Property valuations: | CB Richard Ellis Limited, St Martin's Court, 10 Paternoster Row, London, EC4M 7HP |
| Solicitors: | Lothian Pension Fund In-house |



Comments and suggestions

We appreciate your comments and suggestions on this report. Please let us know which sections you found useful and if you have any suggestions for items to be included in the future. Please email your comments to pensions@lpf.org.uk.

Accessibility

You can get this document on tape, in Braille, large print and various computer formats on request. Please contact the Interpretation and Translation Service (ITS) on 0131 242 8181 and quote reference number 00819. The ITS can also give information on community language translations.

Contact details

If you would like further information about Lothian Pension Fund and Scottish Home Pension Fund, please contact us the details on the back page of this report.

LOTHIAN PENSION FUND

pensions@lpf.org.uk

0131 529 4638

www.lpf.org.uk

Lothian Pension Fund, Atria One, 144 Morrison Street, Edinburgh EH3 8EX

LPFE Limited

Financial Statements

For the year ended 31 March 2019

Registered number SC497543

LPFE LIMITED

Financial statements

For the year ended 31 March 2019

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LPFE LIMITED

Company information

Board of Directors:

Chairman

Stephen Moir

Executive Directors

Hugh Dunn
Alasdair Rankin
Katy Miller
Douglas Heron

Non-executive Director

Leslie Robb

Company Secretary:

Struan Fairbairn

Registered office

4th Floor Saltire Court
20 Castle Terrace
Edinburgh
Lothian
EH1 2EN

Bankers:

The Royal Bank of Scotland plc

Auditor:

Scott-Moncrieff
Chartered Accountants
Exchange Place 3
Sempole Street
Edinburgh
EH3 8BL

LPFE LIMITED

Directors' Report

For the year ended 31 March 2019

The directors present their report and audited financial statements for the year ending 31 March 2019.

Principal activity

The principal activity of the company is the provision of seconded staff to the City of Edinburgh Council acting in its capacity as the administering authority of the Lothian Pension Fund ("LPF") and LPFI Limited in support of the administration of the Lothian Pension Fund and the Scottish Homes Pension Fund ("the Funds") and separately (on a limited basis) to Falkirk Council in its capacity as the administering authority of the Falkirk Council Pension Fund. All pension funds are part of the Local Government Pension Scheme in Scotland (LGPS).

Results, dividends and mutual trading surplus

The loss for the year after tax was £306,388 (2018 - £1,535,060 loss) and after allowing for items included under "Other comprehensive income" a loss of £473,408 (2018 - £853,960 loss). The directors do not recommend payment of dividend.

The company's aim is to make a modest trading surplus before adjustments required under IFRS. After allowing for an addition to costs of £69,314 (2018 - £40,112) in respect of accrued holiday and variable pay and £326,000 (2018 - £1,536,000) for adjustments to pension costs under IAS19, the underlying trading profit is £88,926 (2018 - £41,052). The additional costs recognised under "Other comprehensive income" amounting to £167,020 (2018: £681,100 additional gains) all relates to further adjustments required by IAS19 and the related deferred tax.

Under the mutual trading agreement with LPF, the company is required to consider if any of the profit arising from the mutual trade can be returned to the Council. Although there was an underlying trading profit of £88,926 (2018: £41,052, Company Law requires that only "distributable profits" are available for distribution. The company's auditor has confirmed that the various adjustments required under IFRS must be taken into account when determining if profits are distributable. As a result, there are no distributable profits available for return to LPF in respect of the period.

Business review

The company is wholly owned by LPF and has entered into a shareholder agreement with LPF to appropriately address certain governance matters. The company also has a loan facility provided by LPF for the purpose of the provision of short-term working capital.

Staffing services are provided to LPF for the purposes of administering the Funds under an intra-group resourcing agreement. The agreement also provides for the running costs of the company to be covered as part of a service charge and the provision of staffing services to LPFI Limited (also wholly owned by LPF).

The company also has a secondment agreement with Falkirk Council to provide legal staff to assist with certain aspects of the administration of the Falkirk Council Pension Fund as part of a mutually beneficial collaboration between those LGPS funds.

LPFE LIMITED

Directors' Report (continued)

For the year ended 31 March 2019

Future prospects

The company's future prospects are primarily linked to the needs of LPF. The company is securely funded by LPF, which means that it is in a position to adapt to any future staffing requirements. Arrangements are in hand to increase the number of investment staff to extend LPF's ability to manage investments (including direct property) in-house.

The directors are of the view that the current "Brexit" uncertainty and its outcome is unlikely to directly impact the prospects of the company. This is because LPF will still have a need for investment management and pension administration services.

Directors

The directors who served during the period were:

| | |
|-----------------|---------------------------|
| Hugh Dunn | |
| Clare Scott | Resigned 26 December 2018 |
| Alasdair Rankin | |
| Katy Miller | |
| Stephen Moir | |
| Leslie Robb | |
| Douglas Heron | Appointed 1 February 2019 |

Statement of directors' responsibilities

The directors are responsible for preparing the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. The directors have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law, the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of its results for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Disclosure of information to auditor

As far as each of the directors at the time the report is approved are aware:

- a) there is no relevant information of which the company's auditor is unaware, and
- b) the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of the information.

LPFE LIMITED

Directors' Report (continued)

For the year ended 31 March 2019

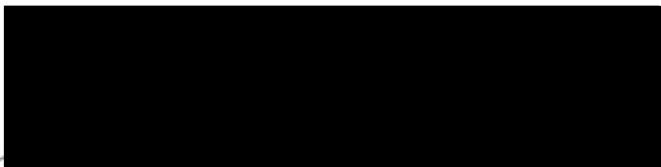
Auditor

The auditor, Scott-Moncrieff, is deemed to be reappointed under Section 487 (2) of the Companies Act 2006.

Small company provisions

This report has been prepared in accordance with the special provisions for small companies under Part 15 of the Companies Act 2006.

This report was approved by the board and signed on its behalf by:



Stephen Moir
Chairman

Date: 21 May 2019

LPFE LIMITED

Independent Auditor's Report to the Members of LPFE Limited

For the year ended 31 March 2019

Opinion

We have audited the financial statements of LPFE Limited ('the company') for the year ended 31 March 2019 which comprise the Statement of Profit or Loss and Other Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows and related notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2019 and its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the United Kingdom, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate, or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

LPFE LIMITED

Independent Auditor's Report to the Members of LPFE Limited (continued)

For the year ended 31 March 2019

Opinion on Other Matter(s) Prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Directors' Report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the directors' report.

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not exempt from the requirement to prepare a strategic report.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 3, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs(UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Councils website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our Auditor's report.

LPFE LIMITED

Independent Auditor's Report to the Members of LPFE Limited (continued)

For the year ended 31 March 2019

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an Auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.



**Nick Bennett, Senior Statutory Auditor
For and on behalf of Scott-Moncrieff, Statutory Auditor
Chartered Accountants
Exchange Place 3
Sempie Street
Edinburgh
EH3 8BL**

Date: *21 June* 2019

LPFE LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2019

| | Note | 2019 £ | 2018 £ |
|--------------------------------------------------------|-------------|-------------------------|-------------------------|
| Continuing Operations | | | |
| Revenue | 1e | 3,915,842 | 1,592,314 |
| Gross profit | | <u>3,915,842</u> | <u>1,592,314</u> |
| Administrative expenses | | (4,155,957) | (3,099,188) |
| Loss from operations | 2 | <u>(240,115)</u> | <u>(1,056,874)</u> |
| Finance costs | 3 | (51,434) | (28,380) |
| Loss before tax | | <u>(291,549)</u> | <u>(1,535,254)</u> |
| Corporation tax (charge)/credit | 4 | (14,839) | 194 |
| Loss for the year | | <u>(306,388)</u> | <u>(1,535,060)</u> |
| Other comprehensive income: | | | |
| Those that are not recyclable net of tax: | | | |
| Actuarial (loss)/gain on retirement benefit obligation | 15 | (268,000) | 506,000 |
| Deferred tax charge thereon | 10 | 100,980 | 175,100 |
| Total comprehensive loss for the year | | <u>(473,408)</u> | <u>(853,960)</u> |

The accompanying notes on pages 12 to 29 form part of these financial statements

LPFE LIMITED

Statement of Financial Position

As at 31 March 2019

| | Note | As at 31 March 2019 £ | As at 31 March 2018 £ |
|------------------------------------------------------------|------|-----------------------------|-----------------------------|
| Non-current assets | | | |
| Deferred tax asset | 10 | 392,530 | 291,550 |
| Total non-current assets | | 392,530 | 291,550 |
| Current assets | | | |
| Trade and other receivables | 7 | 396,240 | 340,881 |
| Cash and cash equivalents | 8 | 213,773 | 10,450 |
| Total current assets | | 610,013 | 351,331 |
| Total assets | | 1,002,543 | 642,881 |
| Equity and Liabilities | | | |
| Equity attributable to equity holders of the parent | | | |
| Share capital | 11 | 1 | 1 |
| Retained earnings | 12 | (1,866,097) | (1,392,689) |
| | | (1,866,096) | (1,392,688) |
| Liabilities | | | |
| Non-current liabilities | | | |
| Retirement benefits obligation | 15 | 2,309,000 | 1,715,000 |
| Trade and other payables | 9 | 12,551 | - |
| Total non-current liabilities | | 2,321,551 | 1,715,000 |
| Current liabilities | | | |
| Trade and other payables | 9 | 547,088 | 320,569 |
| Total current liabilities | | 547,088 | 320,569 |
| Total liabilities | | 2,868,639 | 2,035,569 |
| Total equity and liabilities | | 1,002,543 | 642,881 |

The financial statements were authorised for issue by the Board of Directors on
and were signed on its behalf by:

21 Mar 2019

Stephan Iron
Chairman

Registered number: SC497543

The accompanying notes on pages 12 to 29 form part of these financial statements

LPFE Limited
Statement of Changes in Equity
As at 31 March 2019

| | Note | Share Capital £ | Retained Earnings £ | Total £ |
|----------------------------------------------------------|------|-----------------------|---------------------------|--------------------|
| Balance at 1 April 2017 | | 1 | (538,729) | (538,728) |
| Comprehensive income | | | | |
| Loss for the year | | - | (1,535,060) | (1,535,060) |
| Other comprehensive income | | | | |
| Actuarial gains on retirement benefit obligation in year | 15 | - | 506,000 | 506,000 |
| Deferred tax on retirement benefit obligation | 10 | - | 175,100 | 175,100 |
| Balance at 31 March 2018 | | <u>1</u> | <u>(1,392,689)</u> | <u>(1,392,688)</u> |

| | Note | Share Capital £ | Retained Earnings £ | Total £ |
|-----------------------------------------------------------|------|-----------------------|---------------------------|--------------------|
| Balance at 1 April 2018 | | 1 | (1,392,689) | (1,392,688) |
| Comprehensive income | | | | |
| Loss for the year | | - | (306,388) | (306,388) |
| Other comprehensive income | | | | |
| Actuarial losses on retirement benefit obligation in year | 15 | - | (268,000) | (268,000) |
| Deferred tax on retirement benefit obligation | 10 | - | 100,980 | 100,980 |
| Balance at 31 March 2019 | | <u>1</u> | <u>(1,866,097)</u> | <u>(1,866,096)</u> |

The accompanying notes on pages 12 to 29 form part of these financial statements

LPFE LIMITED
Statement of Cash Flows

For the year ended 31 March 2019

| | 2019 | 2018 |
|------------------------------------------------------|-------------|-------------|
| | £ | £ |
| Cash flow from operating activities | | |
| Loss for the year | (306,388) | (1,535,060) |
| Adjustments for: | | |
| Defined benefit pension – current service cost | 843,000 | 336,000 |
| Defined benefit pension – employer contribution | (567,000) | (204,000) |
| Defined benefit pension – business combinations | - | 1,377,000 |
| Defined benefit pension – finance costs | 50,000 | 27,000 |
| Other finance costs | 1,434 | 1,380 |
| Corporation tax charge / (credit) | 14,839 | (194) |
| Changes in assets and liabilities: | | |
| Increase in receivables and other financial assets | (55,574) | (199,476) |
| Increase in payables | 234,112 | 159,5545 |
| Cash flows from operations | 214,423 | (37,796) |
| Interest paid | (845) | (1,195) |
| Corporation tax credit received | 215 | 1,321 |
| Net cash flows from operating activities | 213,793 | (37,670) |
| Cash flow from investing activities | - | - |
| Net cash flows from investing activities | - | - |
| Cash flow from financing activities | | |
| Movement in loan facility | (10,470) | 34,739 |
| Net cash flows from financing activities | (10,470) | 34,739 |
| Net increase/(decrease) in cash and cash equivalents | 203,323 | (2,931) |
| Cash and cash equivalents at beginning of year | 10,450 | 13,381 |
| Cash and cash equivalents at end of year | 213,773 | 10,450 |
| Cash at bank and in hand | 213,773 | 10,450 |

The accompanying notes on pages 12 to 29 form part of these financial statements

LPFE LIMITED

Notes to the Financial Statements

For the year ended 31 March 2019

1. Statement of significant accounting policies

LPFE Limited ('the company') is a limited company incorporated in Scotland. The address of its registered office and principal place of business are disclosed on page 1. The principal activities of the company are described within the directors' report on pages 2 to 4.

The financial statements of LPFE Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS), IFRIC Interpretation and the Companies Act 2006 applicable to companies reporting under IFRS.

Adoption of new and revised standards

The company has adopted the following new and amended IFRSs as of 1 April 2018:

- IAS 1 Presentation of Financial Statements
- IAS 39 Financial Instruments: Recognition and Measurement
- IFRS 7 Financial Instruments: Disclosures
- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IAS 1 has been amended after the issue of IFRS 9 with the main effect on the company being to amend the presentation and disclosure of assets held at amortised cost. Given the nature of the company's financial assets this standard has not had a material impact on the company's financial statements in the period of initial application.

IAS 39 requirements were replaced by IFRS 9 on Financial Instruments, with the main effect on the company being to re-categorise financial assets and liabilities together with IFRS 7 on Financial Instruments Disclosures. On initial application there has been no material impact or significant disclosure changes. The new impairment treatment required under IFRS 9 with impairment provisions for trade and other receivables based on expected credit losses has had no material impact on the company's financial statements.

IFRS 15 deals with contracts to provide goods or services. In recording income from service contracts the company currently recognises costs, particularly staff costs, when incurred. The service contract has one performance obligation and there is little ambiguity surrounding the transaction price as services are charged purely to cover costs incurred. Therefore the directors consider the company is already compliant with IFRS 15 and there have been no changes.

Guidance in issue but not in force

IAS 8 requires disclosure of guidance in issue but not in force. The minimum disclosure relates to guidance issued by 31 March 2018, and with potential effect.

| International Accounting Standards and Interpretations | Effective for annual periods beginning on or after |
|---------------------------------------------------------------|-----------------------------------------------------------|
| IFRS 16 Leases | 1 January 2019 |
| IFRIC 23 Uncertainty over Income Tax Treatments | 1 January 2019 |
| IAS 12 Income Taxes* | 1 January 2019 |

*Not yet adopted for use in the European Union.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

Guidance in issue but not in force (continued)

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IAS 12 on Income Taxes states that all tax consequences of a dividend should be recognised at the time the liability to pay the dividend is recorded or paid if no liability is recorded prior. All income tax consequences of the dividend will be recorded in profit or loss, other comprehensive income or equity according to where the distributable profits were created.

Basis of preparation

The financial statements are presented in Sterling (£) as that is the company's functional currency and the currency in which the majority of the company's transactions are denominated. The financial statements have been prepared on the historical cost basis.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the company's accounting policies.

The following significant accounting policies, which are consistent with the previous period unless otherwise stated, have been adopted in the preparation of this report:

a. Going concern

The directors are of the opinion that the company has adequate resources to enable it to undertake its planned activities for a period of at least one year from the date that the financial statements are approved.

b. Current and deferred income tax

The company is a mutual trader and is therefore not liable to corporation tax on surpluses generated from mutual trade. The tax charge for the period is based on the profit for the year from non-mutual trade, adjusted for any non-assessable or disallowed items. It is calculated using tax rates that have been enacted or are substantively enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

b. Current and deferred income tax (continued)

Deferred income tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

c. Impairment

The carrying value of all assets are reviewed for impairment at each reporting date, with the recoverable amount being estimated when events or changes in circumstances indicate that the carrying value may be impaired.

The recoverable amount of all assets is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which it belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of the asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

d. Cash and cash equivalents

For the purposes of the statement of cash flows, cash includes cash on hand and at call deposits with banks or financial institutions, investments in money market instruments maturing within less than two months and is net of bank overdrafts.

e. Revenue

Revenue is recognised to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty.

Revenue is derived wholly from the provision of seconded staff in the United Kingdom. Revenue is recognised upon the delivery of the service to the customer.

All revenue is stated net of the amount of value added tax (VAT).

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

f. Value added tax

Revenues, expenses and assets are recognised net of the amount of value added tax (VAT), except:

- i. Where the amount of VAT incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
- ii. For receivables and payables, which are recognised inclusive of VAT.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Cash flows are included in the statement of cash flows on a gross basis. The VAT component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

g. Share capital

Ordinary shares are classified as equity.

h. Employee benefits

Lothian Pension Fund

The company contributes to a defined benefits scheme operated on behalf of its employees.

The employees of LPFE Limited participate in the Lothian Pension Fund, which is part of the Local Government Pension Scheme in Scotland and is administered by the City of Edinburgh Council.

The current service cost for the period is charged to the statement of profit or loss and other comprehensive income. The assets of the scheme are held separately from those of the company in independently administered funds. The company has fully adopted the accounting principles as required by International Accounting Standard 19 – Employee Benefits.

The liability recognised in the balance sheet in respect of defined benefit pension plan is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in a currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity through other comprehensive income in the period in which they arise.

Past-service costs are recognised immediately in income, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

h. Employee benefits (continued)

Variable pay arrangements

During the year, the company introduced three variable pay schemes, two of which have vesting periods. The Portfolio Manager and Senior Management schemes entitle staff to receive an assessed percentage of their salary as an additional variable pay award if they meet certain objectives during the year. The assessment year runs from 1 February to 31 January each year. This award then vests over the following three years. The first part is payable at the end of the first year if the objectives are met and the remaining two parts are payable in the following two years if the requirement that the employee is still employed by the company at such time is met. In line with IAS19 the payment is recognised when made and the liability has been accrued accordingly for the services which the employees have delivered with regards to the second and third payments in the scheme.

i. Financial instruments

Financial assets and financial liabilities are recognised when the company has become party to the contractual provisions of the instrument.

Trade receivables

Trade receivables are recognised initially at cost and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the company will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is recognised in the statement of profit or loss and other comprehensive income.

Trade payables

Trade payables are initially recognised at cost and subsequently at amortised cost using the effective interest method.

Financial liabilities

Financial liabilities are classified according to the substance of the contractual arrangements entered into.

An instrument will be classified as a financial liability when there is a contractual obligation to deliver cash or another financial asset to another enterprise.

Loans

All interest bearing loans and other borrowings are initially recorded at fair value, which represents the fair value of the consideration received, net of any issue costs associated with other borrowings. Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs.

Finance charges, including premiums payable on settlement or redemption, are accounted for on an amortised cost basis to the statement of comprehensive income using the effective interest method, being recognised in the statement of profit or loss and other comprehensive income over the term of such instruments at a constant rate on the carrying amount of the instrument to the extent that they are not settled in the year in which they arise.

Borrowings are classified as current liabilities unless the company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

j. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

k. Critical accounting estimates and judgements

The directors evaluate estimates and judgements incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the company.

Key estimates – defined benefit pension obligation

IAS 19 Employee Benefits, requires that certain assumptions are made in order to determine the amount to be recorded for retirement benefit obligations and pension plan assets. These are mainly actuarial assumptions such as expected inflation rates, long-term increase in health care costs, employee turnover, expected return on plan assets and discount rates. Substantial changes from the assumptions listed in any one of these variables may significantly change the group's retirement benefit obligation and pension assets (see note 15 for further details).

2. Loss from operations

| | 2019 £ | 2018 £ |
|-----------------------------------------------------------|---------------|---------------|
| Loss from operations has been determined after deducting: | | |
| Auditor's remuneration: | | |
| Audit services | 5,500 | 4,900 |
| Non-Audit services | 12,775 | 8,100 |
| | <u>18,275</u> | <u>13,000</u> |

3. Finance costs

| | 2019 £ | 2018 £ |
|---------------------------------------------------|---------------|---------------|
| Loan interest payable to group entities (note 14) | 1,434 | 1,380 |
| Pension interest costs (note 15) | 50,000 | 27,000 |
| | <u>51,434</u> | <u>28,380</u> |

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

4. Corporation tax charge/(credit)

| | 2019 £ | 2018 £ |
|---------------------------------|-----------|-----------|
| Current tax: | | |
| Corporation tax charge/(credit) | 14,839 | (194) |
| Tax on profits for the year | 14,839 | (194) |

Corporation tax credit is calculated at 19% (2018: 19%) of the assessable profits for the year.

The charge for the year can be reconciled to the loss per the income statement as follows:

| | 2019 £ | 2018 £ |
|--------------------------------------------------------------------------------|-----------|-------------|
| Loss for the year before taxation | (291,549) | (1,535,254) |
| Loss for the year at the effective rate of corporation tax of 19% (2018 – 19%) | (55,394) | (291,698) |
| Effects of: | | |
| Mutual trade adjustment | 66,407 | 265,242 |
| Expenses not deductible for tax purposes | 3,866 | 26,262 |
| Trading losses carried forward | - | - |
| Other adjustments | (40) | - |
| Current tax charge/(credit) | 14,839 | (194) |

5. Employee benefits expense

The average number of persons employed by the company (including directors) during the year was 62 (2018: 20).

The aggregate payroll costs were as follows:

| | 2019 £ | 2018 £ |
|------------------------------------------------|-----------|-----------|
| Wages, salaries and variable pay | 2,817,553 | 1,136,832 |
| Social security costs | 305,148 | 134,079 |
| Defined benefit pension - current service cost | 843,000 | 336,000 |
| | 3,965,701 | 1,606,911 |

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

5. Employee benefits expense (continued)

Variable Pay

During the year, the company introduced three variable pay schemes, two of which have vesting periods. The Portfolio Manager and Senior Management schemes entitle staff to receive an assessed percentage of their salary as an additional variable pay award if they meet certain objectives during the year. The assessment year runs from 1 February 2018 to 31 January 2019. The award then vests over three years. The first part is payable at the end of the first year if the objectives are met and the remaining two parts are payable in the following two years if the requirement that the employee is still employed by the company at such time is met. Payment one has been made in January 2019. A liability has been raised at 31 March 2019 for the 2 months of service which the employees have delivered with regards to the second and third payments in the scheme.

Deferred variable pay

| | 2019 | 2018 |
|-----------------------|--------|------|
| | £ | £ |
| Brought forward | - | - |
| Current service cost | 38,261 | - |
| | 38,261 | - |
| | 38,261 | - |
| | 2019 | 2018 |
| | £ | £ |
| Current liability | 25,710 | - |
| Non-current liability | 12,551 | - |
| | 38,261 | - |
| | 38,261 | - |

6. Directors' remuneration

Three (2018: two) directors received emoluments from the company during the period. The directors' emoluments for the period were as follows:

| | 2019 | 2018 |
|--------------------------------|---------|---------|
| | £ | £ |
| Aggregate emoluments | 106,308 | 102,801 |
| Employer pension contributions | 23,397 | 20,685 |
| | 129,705 | 123,486 |
| | 129,705 | 123,486 |

One director had an accrued pension entitlement of £22,829 (2018: £20,225) and a lump sum entitlement of £13,636 (2018: £12,938) at the end of the year. The other two directors do not have any accrued pension provision provided by the company.

All other directors are employed by the City of Edinburgh Council.

7. Trade and other receivables

| | 2019 | 2018 |
|---------------------------------|---------|---------|
| | £ | £ |
| Trade receivables | 53,577 | 35,927 |
| Amounts due from group entities | 333,412 | 295,304 |
| Prepayments and accrued income | 9,251 | 9,650 |
| | 396,240 | 340,881 |
| | 396,240 | 340,881 |

The directors consider the fair value of receivables to be in line with carrying values.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

8. Cash and cash equivalents

| | 2019 | 2018 |
|--------------------------|----------------|---------------|
| | £ | £ |
| Cash at bank and in hand | 213,773 | 10,450 |
| | <u>213,773</u> | <u>10,450</u> |

9. Trade and other payables

| Current liabilities | 2019 | 2018 |
|---------------------------------|----------------|----------------|
| | £ | £ |
| Trade payables | 3,053 | 13,315 |
| Accruals and deferred income | 144,658 | 140,782 |
| Social security and other taxes | 383,751 | 155,804 |
| Amounts due to group entities | 787 | 10,668 |
| Corporation tax | 14,839 | - |
| | <u>547,088</u> | <u>320,569</u> |

| Non-current liabilities | 2019 | 2018 |
|--------------------------------|---------------|-------------|
| | £ | £ |
| Accruals and deferred income | 12,551 | - |
| | <u>12,551</u> | <u>-</u> |

10. Deferred tax

| | 2019 | 2018 |
|---------------------------------------------------|----------------|----------------|
| | £ | £ |
| At 31 March 2018 | 291,550 | 116,450 |
| Charge for the year to other comprehensive income | 100,980 | 175,100 |
| | <u>392,530</u> | <u>291,550</u> |
| At 31 March 2019 | 392,530 | 291,550 |
| The elements of deferred tax are as follows: | | |
| Defined benefit pension scheme liability | 392,530 | 291,550 |
| | <u>392,530</u> | <u>291,550</u> |

11. Share Capital

| | 2019 | 2018 |
|-------------------------------------------|-------------|-------------|
| | £ | £ |
| <i>Allotted, called up and fully paid</i> | | |
| Ordinary shares of £1 each | 1 | 1 |
| | <u>1</u> | <u>1</u> |

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

12. Reserves

| | Retained Earnings £ |
|-------------------------------------------------|---------------------------|
| At 31 March 2017 | (538,729) |
| Loss for the year | (1,535,060) |
| Actuarial gain on retirement benefit obligation | 506,000 |
| Deferred tax on retirement benefit obligation | 175,100 |
| | <hr/> |
| At 31 March 2018 | (1,392,689) |
| Loss for the year | (306,388) |
| Actuarial loss on pension plan | (268,000) |
| Deferred tax on retirement benefit obligation | 100,980 |
| | <hr/> |
| At 31 March 2019 | <u>(1,866,097)</u> |

13. Controlling interest

The City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) owns all the issued share capital of the company. The company itself has been established to support the administration of the Lothian Pension Fund. Administering authorities are required to prepare separate financial statements for the Local Government Pension Scheme funds that they administer and so it is considered appropriate to consolidate the company's individual financial statements into Lothian Pension Fund's consolidated financial statements.

Group accounts are available to the public from the following address and will also be made available through the pension scheme website at www.lpf.org.uk:

Company Secretary
Lothian Pension Fund
Atria One
144 Morrison Street
Edinburgh
EH3 8EX

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

14. Related party transactions

| | 2019 £ | 2018 £ |
|--------------------------------------------------------------------------------------|-----------|-----------|
| Lothian Pension Fund (pension fund administered by City of Edinburgh Council) | | |
| Sale of services during the period | 3,616,093 | 1,449,997 |
| Receivables at the period end | 222,584 | 287,782 |
| Loan facility balance payable at the period end | - | 10,470 |
| Interest payable during the period | 1,434 | 1,380 |
| Interest payable but still accruing at the period end | 787 | 198 |
| LPFI Limited (company under common control) | | |
| Sale of services during the period | 119,279 | 20,236 |
| Receivables at the period end | 110,828 | 7,306 |
| Balance receivable for group tax losses surrendered | - | 215 |

The company has a loan facility agreement with Lothian Pension Fund for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the company returns any cash not immediately required and this can result in short periods when the company has returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Total compensation paid in relation to key management personnel during the period was as follows:

| | 2019 £ | 2018 £ |
|-----------------------------------------------------------|-----------|-----------|
| Short-term employee benefits | 647,017 | 472,188 |
| Post-employment benefits - employer pension contributions | 110,543 | 84,962 |
| | 757,560 | 557,150 |
| | 757,560 | 557,150 |

Key management personnel had accrued pensions totalling £120,245 (2018: £97,456) and lump sums totalling £132,375 (2018: £110,889) at the end of the period.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

15. Retirement benefits obligation

The Lothian Pension Fund, which is administered by the City of Edinburgh Council, is part of the Local Government Pension Scheme in Scotland. This is a pension scheme providing benefits based on pensionable pay, contributions being charged to the profit or loss so to spread the cost of pensions over employees' working lives. The contributions are determined by a qualified actuary.

The valuation of the pension fund is carried out triennially. The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at 31 March 2017 by Hymans Robertson LLP. The present value of the defined benefit obligation, and related current service cost and past service cost, were measured using the Projected Unit Credit Method.

Scheme assets

The company's share of the fair value of the scheme's assets which are not intended to be realised in the short term and may be subject to significant change before they are realised, were comprised as follows:

| | % | 2019 £'000 | % | 2018 £'000 |
|------------------------------------------|-------------|---------------|-------------|---------------|
| Equity Securities: | | | | |
| Consumer | 11% | 1,094 | 14% | 1,187 |
| Manufacturing | 12% | 1,265 | 15% | 1,288 |
| Energy and Utilities | 8% | 777 | 6% | 542 |
| Financial Institutions | 8% | 865 | 9% | 769 |
| Health and Care | 5% | 559 | 5% | 425 |
| Information Technology | 3% | 335 | 6% | 528 |
| Other | 10% | 1,003 | 6% | 543 |
| Debt Securities: | | | | |
| Corporate Bonds (investment grade) | 0% | - | 0% | - |
| Corporate Bonds (non-investment grade) | 0% | - | 2% | 169 |
| UK Government | 10% | 1,045 | 10% | 839 |
| Other | 0% | - | 0% | - |
| Private Equity: | | | | |
| All | 1% | 139 | 2% | 158 |
| Real Estate | | | | |
| UK Property | 7% | 697 | 6% | 556 |
| Overseas property | 0% | - | 0% | 9 |
| Investment Funds and Unit Trusts: | | | | |
| Equities | 1% | 102 | 1% | 83 |
| Bonds | 3% | 261 | 0% | - |
| Infrastructure | 12% | 1277 | 12% | 1,025 |
| Other | 0% | - | 0% | 20 |
| Derivatives: | | | | |
| Foreign Exchange | 0% | 3 | 0% | - |
| Cash and Cash Equivalents: | | | | |
| All | 8% | 863 | 6% | 511 |
| | <u>100%</u> | <u>10,285</u> | <u>100%</u> | <u>8,652</u> |

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

15. Retirement benefits obligation (continued)

| | | |
|------------------------------------------------------------------------------------------|-------------------|-------------------|
| The amounts recognised in the statement of financial position are determined as follows: | | |
| | 2019 | 2018 |
| | £'000 | £'000 |
| Fair value of plan assets | 10,285 | 8,652 |
| Present value of scheme liabilities | (12,594) | (10,367) |
| | <u> </u> | <u> </u> |
| Net pension liability | <u>(2,309)</u> | <u>(1,715)</u> |

The movement in the defined benefit obligation over the year is as follows:

| | | |
|------------------------------------------------------------------------|-------------------|-------------------|
| | 2019 | 2018 |
| | £'000 | £'000 |
| Brought forward | 10,367 | 3,513 |
| Current service cost | 843 | 336 |
| Interest cost on obligation | 294 | 131 |
| Plan participants contributions | 194 | 91 |
| Benefits paid | (8) | (4) |
| Effects of business combinations | - | 7,088 |
| Actuarial losses/(gains) arising from changes in financial assumptions | 904 | (536) |
| Actuarial losses arising from changes in demographic assumptions | - | 120 |
| Other actuarial gains | - | (372) |
| | <u> </u> | <u> </u> |
| Balance at year end | <u>12,594</u> | <u>10,367</u> |

The movement in the fair value of plan assets of the year is as follows:

| | | |
|-------------------------------------------------------------|-------------------|-------------------|
| | 2019 | 2018 |
| | £'000 | £'000 |
| Brought forward | 8,652 | 2,828 |
| Benefits paid | (8) | (4) |
| Effect of business combinations | - | 5,711 |
| Interest income on plan assets | 244 | 104 |
| Contributions by employer | 567 | 204 |
| Contributions by member | 194 | 91 |
| Return on assets excluding amounts included in net interest | 636 | (282) |
| | <u> </u> | <u> </u> |
| Balance at year end | <u>10,285</u> | <u>8,652</u> |

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

15. Retirement benefits obligation (continued)

The amounts recognised in the Statement of Profit or Loss are as follows:

| | 2019 £'000 | 2018 £'000 |
|---------------------------------------------|---------------|---------------|
| Interest received on pension scheme assets | (244) | (104) |
| Interest cost on pension scheme liabilities | 294 | 131 |
| | <hr/> | <hr/> |
| Finance cost | 50 | 27 |
| Current service cost | 843 | 336 |
| Effect of business combinations | - | 1,377 |
| | <hr/> | <hr/> |
| | 893 | 1,740 |
| | <hr/> <hr/> | <hr/> <hr/> |

Amounts recognised in other comprehensive income:

| | 2019 £'000 | 2018 £'000 |
|----------------------------------------------------------------------|---------------|---------------|
| Actuarial (losses)/gains in the defined benefit obligation | (904) | 788 |
| Actuarial gains/(losses) in the fair value of defined benefit assets | 636 | (282) |
| | <hr/> | <hr/> |
| | (268) | 506 |
| | <hr/> <hr/> | <hr/> <hr/> |

The principal actuarial assumptions used in this valuation were:

| | 2019 | 2018 |
|---------------------------------|------|------|
| Inflation/pension increase rate | 2.4% | 2.3% |
| Salary increase rate | 4.1% | 4.0% |
| Discount rate | 2.5% | 2.7% |

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice. Best estimate has been interpreted to mean that the proposed assumptions are 'neutral' – there is an equal chance of actual experience being better or worse than the assumptions proposed.

The financial assumptions used for reporting in the financial statements are the responsibility of the employer. These assumptions are largely prescribed at any point and reflect market conditions at the reporting date. Changes in market conditions that result in changes in the net discount rate can have a significant effect on the value of the liabilities reported.

A reduction in the net discount rate will increase the assessed value of liabilities as a higher value is placed on benefits paid in the future. A rise in the net discount rate will have the opposite effect of a similar magnitude. There is also uncertainty around life expectancy of the UK population – the value of current and future pension benefits will depend on how long they are assumed to be in payment.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

15. Retirement benefits obligation (continued)

The sensitivity of the overall pension liability to changes in the weighted principal assumptions is:

| Change in assumption | Approximate % increase to employer liability | | Approximate increase to employer liability (£'000) | |
|--------------------------------------------|----------------------------------------------|------|----------------------------------------------------|-------|
| | 2019 | 2018 | 2019 | 2018 |
| 0.5% decrease in real discount rate | 13% | 13% | 1,666 | 1,354 |
| 0.5% increase in the salary increase rate | 4% | 4% | 499 | 455 |
| 0.5% increase in the pension increase rate | 9% | 8% | 1,118 | 859 |

Mortality rates:

Life expectancy is based on the Fund's Vita Curves with improvements in line with the CMI 2012 model assuming current rates of improvements have peaked and will converge at to a long term rate of 1.25% p.a.

Based on these assumptions, the average future life expectancy at age 65 are summarised below:

| | Male | Female |
|--------------------|------|--------|
| Current pensioners | 21.7 | 24.3 |
| Future pensioners | 24.7 | 27.5 |

Expected employer contributions to the benefit plans for the year ended 31 March 2020 are £643,000, based on a pensionable payroll cost of £2,374,000.

Contingent Liabilities

Following The High Court ruling from 26 October 2016, all defined benefit pension schemes must equalise Guaranteed Minimum Pension (GMP) for men and women. In the directors' opinion, there is insufficient basis to estimate reliably the amount to be recognised in the past service cost until actuaries complete their assessment of the impact and reflect it fully in the pension reports. LPF's actuary, Hymans Robertson LLP has advised that following discussions with the National Audit Office and other LGPS actuaries, the general expectation is that a 'trigger event' is yet to occur in the LGPS and their default approach is to ignore any GMP impact in the 31 March 2019 accounts.

As a result of a ruling in The Court of Appeal (the McCloud judgement) in December 2018, which relates to age discrimination arising from public sector pension scheme transition arrangements, there is the potential for an impact on employer pension liabilities for LPF. Hymans Robertson LLP has advised that given the uncertainty around this judgement, with the government awaiting news of its right to an appeal, it is too early to know what the likely effect may be on LGPS members' benefits.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

16. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable. Financial instruments do not include prepayments, VAT, taxation, social security and deferred income.

The company did not enter into any transactions that would be classed derivative financial instruments during the period.

The totals for each category of financial instruments, measured in accordance with IAS 39 and detailed in the accounting policies, are as follows:

| | 2019 £ | 2018 £ |
|------------------------------------|----------------|----------------|
| Financial Assets | | |
| Cash and cash equivalents | 213,773 | 10,450 |
| Trade and other receivables | 389,372 | 333,531 |
| Total Financial Assets | <u>603,145</u> | <u>343,981</u> |
| Financial Liabilities | | |
| Trade and other payables | 161,049 | 164,765 |
| Total Financial Liabilities | <u>161,049</u> | <u>164,765</u> |

Financial Risk Management Policies

The company aims to manage its overall capital structure to ensure it continues to operate as a going concern. The company's capital structure represents the equity attributable to the shareholders of the company together with cash equivalents.

The Board is charged with the overall responsibility of establishing and monitoring the company's risk management policies and processes in order to identify, analyse and monitor the risks that are faced by the company. The company does not enter into or trade financial instruments for speculative purposes.

The main risks that the company is exposed to through its financial instruments are credit risk, liquidity risk and market risk. These are managed as follows:

a. Credit risk

Exposure to credit risk relating to financial assets arises from the potential non-performance by counterparties of contractual obligations that could lead to a financial loss to the company.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance sheet date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the statement of financial position and notes to the financial statements. As at 31 March 2019 none of the company's financial assets were past due or impaired.

Credit risk is managed and reviewed regularly by senior management. It mainly arises from amounts owed by customers.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

16. Financial Risk Management (continued)

Financial Risk Management Policies (continued)

a. Credit risk (continued)

The nature of the company's business means that it currently only has three customers. By far the largest customer is the City of Edinburgh Council and the company is securely funded by the Council. Falkirk Council is a smaller customer. The third customer is LPFI Limited which is a related party. Given the financial stature of both Councils and LPFI Limited the credit risk faced by the company is considered to be very small.

b. Liquidity Risk

Liquidity risk arises from the possibility that the company might encounter difficulty in settling its debts or otherwise meeting its financial obligations as they fall due. The company manages this risk through the following mechanisms:

- preparing forward-looking cash flow analysis in relation to its operational, investing and financing activities; and
- ensuring that adequate unutilised borrowing facilities are maintained.

The tables below reflect an undiscounted contractual maturity analysis for financial liabilities.

Financial liability and financial asset maturity analysis

| Note | Within 1 Year 2019 £ | 1 to 5 Years 2018 £ | Total 2019 £ |
|-------------------------------------------------|-------------------------------|---------------------------|--------------------|
| Financial liabilities due for payment | | | |
| Trade and other payables | (148,498) | (12,551) | (161,049) |
| Total expected outflows | (148,498) | (12,551) | (161,049) |
| Financial assets — cash flows realisable | | | |
| Cash and cash equivalents | 213,773 | - | 213,773 |
| Trade and other receivables | 389,372 | - | 389,372 |
| Total anticipated inflows | 603,145 | - | 603,145 |
| Net inflow of financial instruments | 454,647 | (12,551) | 442,096 |

Cash flows realised from financial assets reflect management's expectation as to the timing of realisation. Actual timing may therefore differ from that disclosed. The timing of cash flows as presented in the table (to settle financial liabilities) reflects the earliest contractual settlement dates.

The company has been granted a £385,000 unsecured revolving loan facility by its parent, The City of Edinburgh Council. The ceiling of the facility has been set at a level to ensure sufficient cash is available to meet the company's short-term cash flow needs, should there be a delay in the City of Edinburgh Council settling invoices for seconded staff.

LPFE LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

16. Financial Risk Management (continued)

Financial Risk Management Policies (continued)

c. Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the company's financial position. The company has no direct exposure to movements in foreign exchange or equity prices, and has very little exposure to interest rate movements, due to the low level of borrowing. The company monitors this risk but the directors are of the opinion that it is very unlikely to have a significant effect on the company's financial position.

17. Movements in financing (assets)/liabilities arising from financing activities

| | Current loans & borrowings |
|-----------------------------------------------|---------------------------------------|
| At 1 April 2017 | (24,269) |
| Cash flows | |
| Financing loans from group companies drawdown | 34,739 |
| | 10,470 |
| At 31 March 2018 | 10,470 |
| Current loans & borrowings | |
| At 1 April 2018 | 10,470 |
| Cash flows | |
| Payment of group company financing loan | (10,470) |
| | - |
| At 31 March 2019 | - |

18. Contingent Liabilities

The company's variable pay arrangements are described in note 5 above. In the event that all the staff involved in the arrangements at 31 January 2019 remain in the company's employment there is a contingent liability of £319,900 in excess of the current and non-current liabilities, as recognised in these financial statements in accordance with IAS19. This amount would be payable over two years.

LPFI Limited

Financial Statements

For the year ended 31 March 2019

Registered number SC497542

LPFI LIMITED

Financial statements

For the year ended 31 March 2019

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LPFI LIMITED

Company information

Board of Directors:

Chairman

Hugh Dunn

Executive Directors

Struan Fairbairn
John Burns
William Bruce Miller
Douglas Heron

Non-executive Director

Leslie Robb

Registered office:

4th Floor Saltire Court
20 Castle Terrace
Edinburgh
Lothian
EH1 2EN

Bankers:

The Royal Bank of Scotland plc

Auditor:

Scott-Moncrieff
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

LPFI LIMITED

Directors' Report

For the year ended 31 March 2019

The directors present their report and audited financial statements for the year ended 31 March 2019.

Principal activity

The current principal activity of the company is the provision of Financial Conduct Authority ("FCA") regulated investment services to the City of Edinburgh Council acting in its capacity as the administering authority of the Lothian Pension Fund) ("LPF") and other Local Government Pension Scheme funds in Scotland and Northern Ireland .

Results, dividends and mutual trading surplus

The profit for the year after tax was £59,396 (2017: £34,619). The directors do not recommend payment of a dividend.

The company's aim is to make a modest trading surplus.

Under the mutual trading agreement with LPF, the company is required to consider if any of the profit arising from the mutual trade can be returned to LPF. Company Law requires that only "distributable profits" are available for distribution. None of the profit for the year is attributable to the mutual trade.

Business review

The company is wholly owned by LPF and has entered into a shareholder agreement with LPF to appropriately address certain governance matters. The company also has a loan facility provided by LPF for the provision of short term working capital.

LPFI Limited does not employ staff directly. Staffing and business support services are provided to the company under separate intra-group agreements with LPFE Limited and LPF respectively. LPFE Limited is also wholly owned by LPF. The company provides certain investment services to LPF via an intra-group investment services agreement and has appropriate terms of engagement with its external collaborative partners. During the year Fife Council Pension Fund was added as a new collaborative partner.

HMRC has agreed that any profits arising from trade between the company and LPF will be covered by the "Mutual Trading" rules and so not subject to Corporation Tax.

The company was granted authorised status by the FCA on 24 June 2016. During the year the company provided investment advising and transaction arranging services in relation to a broad scope of matters.

Future prospects

The company's prospects are linked to LPF's requirement for FCA regulated investment services and the LPF's strategy to work with other LGPS funds in the collaborative provision of such services. The company is securely funded by LPF which means that it can adapt to future trading needs.

The directors are of the view that the current "Brexit" uncertainty and its outcome is unlikely to directly impact the prospects of the company. This is because LPF and its external collaborative partners will still have a need for investment management services.

LPFI LIMITED

Directors' Report (continued)

For the year ended 31 March 2019

Directors

The directors who served during the year were:

| | |
|----------------------|------------------------------|
| Hugh Dunn | |
| Struan Fairbairn | |
| John Burns | |
| William Bruce Miller | |
| Clare Scott | Resigned on 26 December 2018 |
| Leslie Robb | |
| Douglas Heron | Appointed on 1 February 2019 |

Statement of directors' responsibilities

The directors are responsible for preparing the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of its results for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Disclosure of information to auditor

As far as each of the directors at the time the report is approved are aware:

- a) there is no relevant information of which the company's auditor is unaware, and
- b) the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of the information.

Auditor

The auditor, Scott-Moncrieff, is deemed to be reappointed under Section 487 (2) of the Companies Act 2006.

LPFI LIMITED

Directors' Report (continued)

For the year ended 31 March 2019

Small company provisions

This report has been prepared in accordance with the special provisions for small companies under Part 15 of the Companies Act 2006.

This report was approved by the board and signed on its behalf by:



Date: *23 May* 2019

**Hugh Dunn
Chairman**

LPFI LIMITED

Independent Auditor's Report to the Members of LPFI Limited

For the year ended 31 March 2019

Opinion

We have audited the financial statements of LPFI Limited ("the company") for the year ended 31 March 2019 which comprise the Statement of Profit or Loss and Other Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows and related notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2019 and its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the United Kingdom, including the FRC's Ethical Standard, and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate, or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our Auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

LPFI LIMITED

Independent Auditor's Report to the Members of LPFI Limited (continued)

For the year ended 31 March 2019

Opinion on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Directors' Report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the directors' report.

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not exempt from the requirement to prepare a strategic report.

Responsibilities of the directors

As explained more fully in the directors' responsibilities statement set out on page 3, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an Auditor's Report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Councils website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

LPFI LIMITED

Independent Auditor's Report to the Members of LPFE Limited (continued)

For the year ended 31 March 2019

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.



Nick Bennett, Senior Statutory Auditor
For and on behalf of Scott-Moncrieff, Statutory Auditor
Chartered Accountants
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

Date: *21 June* 2019

LPFI LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2019

| | Note | 2019 £ | 2018 £ |
|------------------------------------------------|-------------|-------------------------|-------------------------|
| Continuing Operations | | | |
| Revenue | 1e | 256,939 | 130,212 |
| | | <hr/> | <hr/> |
| Gross profit | | 256,939 | 130,212 |
| Administrative expenses | | (183,610) | (87,305) |
| | | <hr/> | <hr/> |
| Profit from operations | 2 | 73,329 | 42,907 |
| Finance costs | 3 | - | (168) |
| | | <hr/> | <hr/> |
| Profit before income tax expense | | 73,329 | 42,739 |
| Corporation tax charge | 4 | (13,933) | (8,120) |
| | | <hr/> | <hr/> |
| Profit for the year | | 59,396 | 34,619 |
| | | <hr/> | <hr/> |
| Other comprehensive income | | - | - |
| | | <hr/> | <hr/> |
| Total comprehensive income for the year | | 59,396 | 34,619 |
| | | <hr/> <hr/> | <hr/> <hr/> |

The accompanying notes on pages 12 to 23 form part of these financial statements

LPMI LIMITED

Statement of Financial Position

As at 31 March 2019

| | Note | As at 31 March 2019 £ | As at 31 March 2018 £ |
|------------------------------------------------------------|------|-----------------------------|-----------------------------|
| Current assets | | | |
| Trade and other receivables | 6 | 160,593 | 58,965 |
| Cash and cash equivalents | 7 | 126,624 | 83,209 |
| Total current assets | | 287,217 | 142,174 |
| Total assets | | 287,217 | 142,174 |
| Equity and Liabilities | | | |
| Equity attributable to equity holders of the parent | | | |
| Share capital | 9 | 60,000 | 60,000 |
| Retained earnings | 10 | 94,447 | 35,051 |
| | | 154,447 | 95,051 |
| Liabilities | | | |
| Current liabilities | | | |
| Trade and other payables | 8 | 132,770 | 47,123 |
| Total current liabilities | | 132,770 | 47,123 |
| Total equity and liabilities | | 287,217 | 142,174 |

The financial statements were authorised for issue by the Board of Directors on 23 May 2019 and were signed on its behalf by:

.....
Hugh Dunn
Chairman

Registered number: SC497542

The accompanying notes on pages 12 to 23 form part of these financial statements

LPFI LIMITED
Statement of Changes in Equity
As at 31 March 2019

| | Note | Share Capital £ | Retained Earnings £ | Total £ |
|---------------------------------|------|-----------------------|---------------------------|------------|
| Balance at 1 April 2017 | | 50,000 | 432 | 50,432 |
| Comprehensive income | | | | |
| Profit for the year | | - | 34,619 | 34,619 |
| Share movements | | | | |
| Shares allotted during the year | | 10,000 | - | 10,000 |
| Balance at 31 March 2018 | 10 | 60,000 | 35,051 | 95,051 |
| Balance at 1 April 2018 | | 60,000 | 35,051 | 95,051 |
| Comprehensive income | | | | |
| Profit for the year | | - | 59,396 | 59,396 |
| Balance at 31 March 2019 | 10 | 60,000 | 94,447 | 154,447 |

The accompanying notes on pages 12 to 23 form part of these financial statements

LPFI LIMITED

Statement of Cash Flows

For the year ended 31 March 2019

| | 2019 | 2018 |
|----------------------------------------------------|-------------|-------------|
| | £ | £ |
| Cash flow from operating activities: | | |
| Profit for the year | 59,396 | 34,619 |
| Adjustments for: | | |
| Finance costs | - | 168 |
| Corporation tax charge | 13,933 | 8,120 |
| Changes in assets and liabilities: | | |
| Increase in receivables and other financial assets | (101,628) | (45,719) |
| Increase in payables | 79,640 | 21,898 |
| Cash flows from operations | 51,341 | 19,086 |
| Interest paid | - | (257) |
| Corporation tax paid | (7,926) | (281) |
| Net Cash flows from operating activities | 43,415 | 18,548 |
| Cash flow from financing activities: | | |
| Loans repaid to group entities | - | (16,000) |
| Share capital issued | - | 10,000 |
| Net cash flows from financing activities | - | (6,000) |
| Net increase in cash and cash equivalents | 43,415 | 12,548 |
| Cash and cash equivalents at beginning of year | 83,209 | 70,661 |
| Cash and cash equivalents at end of year | 126,624 | 83,209 |
| Cash at bank and in hand | 126,624 | 83,209 |

The accompanying notes on pages 12 to 23 form part of these financial statements

LPMI LIMITED

Notes to the Financial Statements

For the year ended 31 March 2019

1. Statement of significant accounting policies

LPMI Limited ('the company') is a limited company incorporated in Scotland. The address of its registered office and principal place of business are disclosed on page 1. The principal activities of the company are described within the directors' report on pages 2 to 4.

The financial statements of LPMI Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS), IFRIC Interpretation and the Companies Act 2006 applicable to companies reporting under IFRS.

Adoption of new and revised standards

The company has adopted the following new and amended IFRSs as of 1 April 2018:

- IAS 1 Presentation of Financial Statements
- IAS 39 Financial Instruments: Recognition and Measurement
- IFRS 7 Financial Instruments: Disclosures
- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IAS 1 has been amended after the issue of IFRS 9 with the main effect on the company being to amend the presentation and disclosure of assets held at amortised cost. Given the nature of the company's financial assets this standard has not had a material impact on the company's financial statements in the period of initial application.

IAS 39 requirements were replaced by IFRS 9 on Financial Instruments, with the main effect on the company being to re-categorise financial assets and liabilities together with IFRS 7 on Financial Instruments Disclosures. On initial application there has been no material impact or significant disclosure changes. The new impairment treatment required under IFRS 9 with impairment provisions for trade and other receivables based on expected credit losses has had no material impact on the company's financial statements.

IFRS 15 deals with contracts to provide goods or services. In recording income from service contracts the company currently recognises costs, particularly staff costs, when incurred. The service contract has one performance obligations and there is little ambiguity surrounding the transaction price as services are charged for purely to cover costs incurred. Therefore the directors consider the company is already compliant with IFRS 15 and there have been no changes.

Guidance in issue but not in force

IAS 8 requires disclosure of guidance in issue but not in force. The minimum disclosure relates to guidance issued by 31 March 2018, and with potential effect.

| International Accounting Standards and Interpretations | Effective for annual periods beginning on or after |
|--------------------------------------------------------|----------------------------------------------------|
| IFRS 16 Leases | 1 January 2019 |
| IFRIC 23 Uncertainty over Income Tax Treatments | 1 January 2019 |
| IAS 12 Income Taxes* | 1 January 2019 |

*Not yet adopted for use in the European Union.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

Guidance in issue but not in force (continued)

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IFRS 16 on leases is not expected to have a material impact on the financial statements as the company currently has no material lessee or lessor transactions.

IAS 12 on Income Taxes states that all tax consequences of a dividend should be recognised at the time the liability to pay the dividend is recorded or paid if no liability is recorded prior. All income tax consequences of the dividend will be recorded in profit or loss, other comprehensive income or equity according to where the distributable profits were created.

Basis of preparation

The financial statements are presented in Sterling (£) as that is the company's functional currency and the currency in which the majority of the company's transactions are denominated. The financial statements have been prepared on the historical cost basis.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the company's accounting policies.

The following significant accounting policies, which are consistent with the previous period unless otherwise stated, have been adopted in the preparation of this report:

a. Going concern

The directors are of the opinion that the company has adequate resources to enable it to undertake its planned activities for a period of at least one year from the date that the financial statements are approved.

b. Current and deferred income tax

The charge for income tax expense for the year is based on the profit for the year adjusted for any non-assessable or disallowed items. It is calculated using tax rates that have been enacted or are substantively enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

b. Current and deferred tax (continued)

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred income tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

c. Impairment

The carrying value of all assets are reviewed for impairment at each reporting date, with the recoverable amount being estimated when events or changes in circumstances indicate that the carrying value may be impaired.

The recoverable amount of all assets is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which it belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of the asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

d. Cash and cash equivalents

For the purposes of the statement of cash flows, cash includes cash on hand and at call deposits with banks or financial institutions, investments in money market instruments maturing within less than two months and is net of bank overdrafts.

e. Revenue

Revenue is recognised to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty.

Revenue is derived wholly from the provision of FCA-regulated service in the United Kingdom. Revenue from a contract to provide services is recognised by reference to the stage of completion of the contract. The stage of completion of the contract is determined with reference to contractual rates as labour hours and direct expenses are incurred.

All revenue is stated net of the amount of value added tax (VAT).

LPMI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

f. Value added tax

Revenues, expenses and assets are recognised net of the amount of value added tax (VAT), except:

- i. Where the amount of VAT incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
- ii. For receivables and payables, which are recognised inclusive of VAT.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Cash flows are included in the statement of cash flows on a gross basis. The VAT component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

g. Share capital

Ordinary shares are classified as equity.

h. Financial instruments

Financial assets and financial liabilities are recognised when the company has become party to the contractual provisions of the instrument.

Trade receivables

Trade receivables are recognised initially at cost and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the company will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is recognised in the statement of profit or loss and other comprehensive income.

Trade payables

Trade payables are initially recognised at cost and subsequently at amortised cost using the effective interest method.

Financial liabilities

Financial liabilities are classified according to the substance of the contractual arrangements entered into.

An instrument will be classified as a financial liability when there is a contractual obligation to deliver cash or another financial asset to another enterprise.

Finance charges, including premiums payable on settlement or redemption, are accounted for on an amortised cost basis to the profit or loss and other statement of comprehensive income using the effective interest method, being recognised in the statement of comprehensive income over the term of such instruments at a constant rate on the carrying amount of the instrument to the extent that they are not settled in the year in which they arise.

Borrowings are classified as current liabilities unless the company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

1. Statement of significant accounting policies (continued)

h. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

i. Critical accounting estimates and judgements

The directors evaluate estimates and judgements incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the company. The directors are satisfied that the accounting policies are appropriate and that there are no significant estimates or judgements used in the preparation of the financial statements.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

2. Profit from operations

| | 2019 | 2018 |
|-------------------------------------------------------------|-------------|-------------|
| | £ | £ |
| Profit from operations has been determined after deducting: | | |
| Auditor's remuneration: | | |
| Audit services | 4,000 | 3,400 |
| Non-Audit services | 5,555 | 6,470 |
| | 5,555 | 6,470 |

3. Finance costs

| | 2019 | 2018 |
|---------------------------------------------------|-------------|-------------|
| | £ | £ |
| Loan interest payable to group entities (note 12) | - | 168 |
| | - | 168 |

4. Corporation tax charge

| | 2019 | 2018 |
|-----------------------------|-------------|-------------|
| | £ | £ |
| Current tax: | | |
| Corporation tax charge | 13,933 | 7,926 |
| Inter-company tax | - | 194 |
| Tax on profits for the year | 13,933 | 8,120 |

Corporation tax expense is calculated at 19% (2018: 19%) of the assessable profits for the year.

The charge for the year can be reconciled to the profit per the income statement as follows:

| | 2019 | 2019 |
|----------------------------------------------------------------------------------|-------------|-------------|
| | £ | £ |
| Profit for the year before taxation | 73,329 | 42,739 |
| Profit for the year at the effective rate of corporation tax of 19% (2018 – 19%) | 13,933 | 8,120 |

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

5. Directors' remuneration

The aggregate payroll costs for the year consisted of fees paid to a non-executive director. These were as follows:

| | 2019 | 2018 |
|-----------------------|--------|--------|
| | £ | £ |
| Wages and salaries | 12,000 | 12,000 |
| Social security costs | 958 | 651 |
| | 12,958 | 12,651 |
| | 12,958 | 12,651 |

No pension benefits were accrued by the director during the year. All other staff and directors are employed by LPFE Limited, a company under common control, and an appropriate portion of their employment costs recharged. LPFE Limited is a company under the control of Lothian Pension Fund (administered by the City of Edinburgh Council), and the City of Edinburgh Council. In addition to the payroll costs noted above, the company was also charged £1,010 (2018: £5,116) for services provided by directors employed by LPFE Limited during the year.

6. Trade and other receivables

| | 2019 | 2018 |
|-----------------|---------|--------|
| | £ | £ |
| Trade debtors | 160,139 | 34,200 |
| VAT recoverable | 454 | 24,765 |
| | 160,593 | 58,965 |
| | 160,593 | 58,965 |

The directors consider the fair value of receivables to be in line with carrying values.

7. Cash and cash equivalents

| | 2019 | 2018 |
|--------------------------|---------|--------|
| | £ | £ |
| Cash at bank and in hand | 126,624 | 83,209 |
| | 126,624 | 83,209 |

8. Trade and other payables

| | 2019 | 2018 |
|-------------------------------|---------|--------|
| | £ | £ |
| Trade creditors | 317 | 508 |
| Accruals | 7,250 | 30,084 |
| Corporation tax | 13,933 | 7,926 |
| Amounts due to group entities | 111,270 | 8,605 |
| | 132,770 | 47,123 |
| | 132,770 | 47,123 |

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

9. Share Capital

| | 2019 £ | 2018 £ |
|-------------------------------------------------------------------------|-----------|-----------|
| <i>Allotted, called up and fully paid</i> Ordinary shares of £1 each | 60,000 | 60,000 |
| | 60,000 | 60,000 |
| | 60,000 | 60,000 |

10. Reserves

| | Retained Earnings £ |
|-------------------------|---------------------------|
| <i>At 31 March 2017</i> | 432 |
| Profit for the year | 34,619 |
| <i>At 31 March 2018</i> | 35,051 |
| Profit for the year | 59,396 |
| <i>At 31 March 2019</i> | 94,447 |

11. Controlling interest

The City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) owns all the issued share capital of the company. The company itself has been established to support the administration of the Lothian Pension Fund. Administering authorities are required to prepare separate financial statements for the Local Government Pension Scheme funds that they administer and so it is considered appropriate to consolidate the company's individual financial statements into Lothian Pension Fund's consolidated financial statements.

Group accounts are available to the public from the following address:

Account Dept.
Lothian Pension Fund
Atria One
144 Morrison Street
Edinburgh
EH3 8EX

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

12. Related parties

| | 2019 | 2018 |
|--------------------------------------------------------------------------------------|-------------|-------------|
| | £ | £ |
| Lothian Pension Fund (pension fund administered by City of Edinburgh Council) | | |
| Business support costs | 442 | 1,083 |
| Payables at the period end | 442 | 1,083 |
| Loan facility repaid during the year | - | 16,000 |
| Interest payable during the period | - | 168 |
| LPFE Limited (company under common control) | | |
| Staff and other cost recharges | 10,988 | 20,236 |
| Recharges to collaborative partner on behalf of LPFE | 108,290 | - |
| Payables at the period end | 110,828 | 7,306 |
| Group tax losses utilised | - | 194 |
| Balance payable for group tax losses utilised | - | 215 |

The company has a loan facility agreement with Lothian Pension Fund for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the company returns any cash not immediately required and this can result in short periods when the company has returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Compensation paid in relation to key management personnel during the period was as follows:

| | 2019 | 2018 |
|----------------------------------|-------------|-------------|
| | £ | £ |
| Directors' remuneration (note 5) | 12,958 | 12,651 |
| | 12,958 | 12,651 |

All other key management personnel are employed by LPFE Limited, a company also under the control of Lothian Pension Fund (administered by the City of Edinburgh Council), and the City of Edinburgh Council. In addition to the compensation noted above, the company was also charged £1,010 (2018: £5,116) for services provided by key management personnel employed by LPFE Limited during the year.

LPMF LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

13. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable. Financial instruments do not include VAT, taxation, social security and deferred tax.

The company did not enter into any transactions that would be classed as derivative financial instruments during the period.

The totals for each category of financial instruments, measured in accordance with IAS 39 and detailed in the accounting policies, are as follows:

| | 2019 | 2018 |
|------------------------------------|----------------|----------------|
| | £ | £ |
| Financial assets | | |
| Cash and cash equivalents | 126,624 | 83,209 |
| Trade and other receivables | 160,139 | 34,200 |
| | <u>286,763</u> | <u>117,409</u> |
| Total financial assets | <u>286,763</u> | <u>117,409</u> |
| Financial liabilities | | |
| Trade and other payables | 118,837 | 15,197 |
| | <u>118,837</u> | <u>15,197</u> |
| Total financial liabilities | <u>118,837</u> | <u>15,197</u> |

Financial risk management policies

The company aims to manage its overall capital structure to ensure it continues to operate as a going concern. The company's capital structure represents the equity attributable to the shareholders of the company together with cash equivalents.

The Board is charged with the overall responsibility of establishing and monitoring the company's risk management policies and processes in order to identify, analyse and monitor the risks that are faced by the company. The company does not enter into or trade financial instruments for speculative purposes.

The main risks that the company is exposed to through its financial instruments are credit risk, liquidity risk and market risk. These are managed as follows:

a. Credit risk

Exposure to credit risk relating to financial assets arises from the potential non-performance by counterparties of contractual obligations that could lead to a financial loss to the company.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance sheet date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the statement of financial position and notes to the financial statements. As at 31 March 2019 none of the company's financial assets were past due or impaired.

Credit risk is managed and reviewed regularly by senior management. It mainly arises from amounts owed by customers. Given the financial stature of its customers the credit risk faced by the company is considered to be very small.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the year ended 31 March 2019

13. Financial Risk Management (continued)

b. Liquidity Risk

Liquidity risk arises from the possibility that the company might encounter difficulty in settling its debts or otherwise meeting its financial obligations as they fall due. The company manages this risk through the following mechanisms:

- preparing forward-looking cash flow analysis in relation to its operational, investing and financing activities; and
- ensuring that adequate unutilised borrowing facilities are maintained.

The tables below reflect an undiscounted contractual maturity analysis for financial liabilities.

Financial liability and financial asset maturity analysis

| | Within 1 Year 2019 £ | 1 to 5 Years 2019 £ | Total 2019 £ |
|-------------------------------------------------|-------------------------------|------------------------------|--------------------|
| Financial liabilities due for payment | | | |
| Trade and other payables | (118,837) | - | (118,837) |
| Total expected outflows | <u>(118,837)</u> | <u>-</u> | <u>(118,837)</u> |
| Financial assets — cash flows realisable | | | |
| Cash and cash equivalents | 126,624 | - | 126,624 |
| Trade and other receivables | 160,139 | - | 160,139 |
| Total anticipated inflows | <u>286,763</u> | <u>-</u> | <u>286,763</u> |
| Net inflow of financial instruments | <u>167,926</u> | <u>-</u> | <u>167,926</u> |

Cash flows realised from financial assets reflect management's expectation as to the timing of realisation. Actual timing may therefore differ from that disclosed. The timing of cash flows as presented in the table (to settle financial liabilities) reflects the earliest contractual settlement dates.

The company has been granted a £250,000 unsecured revolving loan facility by its parent, The City of Edinburgh Council. The ceiling of the facility has been set at a level to ensure sufficient cash is available to meet the company's short-term cash flow needs, should there be a delay in customers settling invoices for services provided.

LPFI LIMITED

Notes to the Financial Statements (continued)

For the period ended 31 March 2019

13. Financial Risk Management (continued)

c. Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the company's financial position. The company has no direct exposure to movements in foreign exchange or equity prices, and has very little exposure to interest rate movements, due to the low level of borrowing. The company monitors this risk but the directors are of the opinion that it is very unlikely to have a significant effect on the company's financial position.

14. Movements in financing (assets)/liabilities arising from financing activities

| | Share capital | Current loans & borrowings | Total |
|------------------------------------------------|----------------------|---------------------------------------|---------------|
| At 1 April 2017 | 50,000 | 16,000 | 66,000 |
| <i>Cash flows</i> | | | |
| Financing loans from group companies withdrawn | - | (16,000) | (16,000) |
| Issue of share capital | 10,000 | - | 10,000 |
| | <u>60,000</u> | <u>-</u> | <u>60,000</u> |
| At 31 March 2018 | <u>60,000</u> | <u>-</u> | <u>60,000</u> |
| | <u>60,000</u> | <u>-</u> | <u>60,000</u> |
| | <u>60,000</u> | <u>-</u> | <u>60,000</u> |
| At 1 April 2018 and 31 March 2019 | <u>60,000</u> | <u>-</u> | <u>60,000</u> |



Scott-Moncrieff Audit Services
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

Dear Sirs

Lothian Pension Fund and Scottish Homes Pension Fund

This representation letter is provided in connection with your audit of the Lothian Pension Fund and Scottish Homes Pension Fund Annual Report and Accounts for the year ended 31 March 2019 for the purpose of expressing an opinion as to whether the financial statements show a true and fair view of the financial transactions of the Funds during the year to 31 March 2019 and of the amount and disposition at that date of its assets and liabilities (other than liabilities to pay pensions and benefits after the end of the period) in accordance with Part VII of the Local Government (Scotland) Act 1973 and International Financial Reporting Standards as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 and making a statement about contributions.

By a resolution of the board, passed today, I am directed to confirm to you, in respect of the financial statements of the Funds for the year ended 31 March 2019 the following:

1. We have fulfilled our responsibilities for preparing financial statements which give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 and for making accurate representations to you.
2. We have provided you with:
 - access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - additional information that you have requested from us for the purpose of the audit; and
 - unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
3. All transactions have been recorded in the accounting records and are reflected in the financial statements.
4. We acknowledge our responsibilities for the design and implementation of internal control in order to prevent and detect fraud and to prevent and detect error.
5. We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity and involves:
 - management;
 - employees who have significant roles in internal control; and
 - others where the fraud could have a material effect on the financial statements.



Lothian Pension Fund
Atria One, 144 Morrison Street, Edinburgh EH3 8EX
Tel: 0131 529 4638 email: pensions@lpf.org.uk



6. We are not aware of any allegations of fraud or suspected fraud with a potential effect on the financial statements which have been communicated to us by employees, former employees, regulators or other third parties.
7. We have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations, whose effects should be considered when preparing the financial statements.
8. We confirm that, in our opinion, the assumptions that have been used in determining fair values, whether such values are disclosed or applied in the financial statements, are reasonable and reflect our ability and intent to carry out specific courses of action, where this is relevant to the determination of those values.
9. In our opinion the significant assumptions used by us in making accounting estimates are reasonable.
10. Where required, the value at which assets and liabilities are recorded in the net assets statement is, in our opinion, the market value. We are responsible for the reasonableness of any significant assumptions underlying the valuation, including consideration of whether they appropriately reflect our intent and ability to carry out specific courses of action on behalf of the Funds. Any significant changes in those values since the accounting reference date have been disclosed to you.
11. We have disclosed to you the identity of the company's related parties and all related party relationships and transactions of which we are aware.
12. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of International Financial Reporting Standards as adopted by the European Union.
13. In particular, no trustee, shadow trustee, their connected persons or other officers had any indebtedness, agreement concerning indebtedness or disclosable interest in a transaction with the Funds at any time during the year.
14. The following have been properly recorded and, when appropriate, adequately disclosed in the financial statements:
 - losses arising from sale and purchase commitments;
 - agreements and options to buy back assets previously sold;
 - assets pledged as collateral.
15. We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.
16. We have no plans to abandon activities or other plans or intentions that will result in any excess or obsolete stocks, and no stock is stated at an amount in excess of net realisable value.
17. The Funds have satisfactory title to all assets and there are no liens or encumbrances on the Funds' assets, other than as disclosed in the financial statements.
18. We have recorded or disclosed, as appropriate, all liabilities, both actual and contingent, and all guarantees that we have given to third parties.
19. All events subsequent to the date of the financial statements and for which International Financial Reporting Standards as adopted by the European Union require adjustment or disclosure have been adjusted or disclosed. Should any material events occur which may necessitate revision of the figures included in the financial statements or inclusion in the notes thereto, we will advise you accordingly.
20. The Funds have complied with all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance.
21. To the best of our knowledge and belief, the information disclosed in the financial statements in respect of parties which control the Funds is complete and accurate.

22. Except as disclosed in the financial statements, the results for the year were not materially affected by:
- any change in accounting policies;
 - transactions of a type not usually undertaken by the Funds' group;
 - circumstances of an exceptional or non-recurrent nature; or
 - charges or credits relating to prior periods.
23. There is no pending or potential litigation against the Funds and there are no contingencies of a material amount for which provision has not been made in the financial statements.
24. We confirm that we have reviewed going concern considerations and are satisfied that it is appropriate for the financial statements to have been drawn up on the going concern basis. In reaching this opinion we have taken into account all relevant matters of which we are aware and have considered a future period of at least one year from the date on which the financial statements were approved.

Yours faithfully

John Burns
Chief Finance Officer (Section 95 Officer for the Pension Funds)

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Pensions Committee

2.00pm, Wednesday 25 September 2019

Lothian Pension Fund - Contract Awards (Period 1 January to 30 June 2019)

| | |
|----------------------------|----------------|
| Item number | 5.4 |
| Executive/Routine | Routine |
| Wards | |
| Council Commitments | |

1. Recommendations

It is recommended that the Committee notes the contents of this report and the authorisations made under the Scheme of Delegation to Officers. A further report will be submitted to the Committee in approximately six months' time.

Stephen S. Moir

Executive Director of Resources

Contact: Iain Strachan, Chief Procurement Officer,

Finance Division, Resources Directorate, The City of Edinburgh Council

E-mail: iain.strachan@edinburgh.gov.uk | Tel: 0131 529 4930

Lothian Pension Fund – Contract Awards (Period 1 January – 30 June 2019)

2. Executive Summary

- 2.1 This report updates the Pensions Committee on the scope of contracts awarded by Lothian Pension Fund in the period 1 January to 30 June 2019. This provides visibility of contracts awarded under the Scheme of Delegation to Officers, inclusive of direct contract awards not openly tendered due to specific circumstances permitted in regulation and those awarded following a waiver of the Council's Contract Standing Orders (CSOs).

3. Background

- 3.1 A report is presented to Finance and Resources Committee on a six monthly basis detailing the scope of contracts awarded across the Council under the Scheme of Delegation to Officers.
- 3.2 It was identified that, rather than including them in the reporting to Finance and Resources Committee and reflecting the separate governance arrangements for the Lothian Pension Fund, it would be more appropriate to report these contracts awarded by Lothian Pension Fund to the Pensions Committee on a similar six monthly basis. By way of explanation, these contracts are in the name of the Council, but acting in its separate capacity as Administering Authority for the Lothian Pension Fund.

4. Main report

- 4.1 This report updates the Pensions Committee on the scope of contracts awarded by Lothian Pension Fund in the period 1 January to 30 June 2019, inclusive of direct contract awards not openly tendered due to specific circumstances permitted in regulation and those awarded following a waiver of the CSOs.

- 4.2 The Council's CSOs outline contract approval thresholds for goods, works and services, identifying both the level of award which can be undertaken and those with the authority to award.
- 4.3 In specific circumstances, direct awards can be undertaken, where it is not practically viable to 'tender' the requirement.
- 4.4 A waiver of CSOs to allow a contract to be awarded or extended without competitive tendering may also be required in certain circumstances. Inevitably, there will always be a need for a select number of waivers, however each is evaluated on its own merits and approval given only if fully justifiable and in the best interests of the Council. Such circumstances continue to be tightly controlled and scrutinised and will be reported to this Committee moving forward.
- 4.5 The CSOs state that contracts above a threshold of £1m for supply of goods and services and £2m for works require approval from the Committee prior to award.
- 4.6 A summary of contracts awarded under the Scheme of Delegation to Officers is presented in Table 1 below.

Table 1 Contracts Awarded under Delegated Authority

| Date | Lothian Pension Fund | | |
|------------|-------------------------------------------|------------------------------------------------------------------------------------|----------------|
| | Supplier | Contract Description | Value |
| 15/02/2019 | Pensions and Lifetime Savings Association | Pensions and Lifetime Savings Association Subscription. | £11,566 |
| 21/02/2019 | Local Government Association | Subscription for Local Government Association for Lothian Pension Fund (FY 18/19). | £8,160 |
| 21/02/2019 | Pendragon | Annual Subscription to Perspective. | £17,760 |
| 11/03/19 | Local Government Association | Subscription for Local Government Association for Lothian Pension Fund (FY 19/20). | £8,160 |
| 09/04/2019 | PRI Association | Membership Annual Subscription. | £8,000 |
| 05/06/2019 | Style Research Ltd | Membership of the Joint Investment Strategy Panel. | £25,000 |
| | | | £78,646 |

- 4.7 A summary of contracts awarded under the Scheme of Delegation to Officers by way of a waiver of CSOs is presented in Table 2

Table 2 - Contracts awarded under Waiver of CSOs by Delegated Authority

| Waiver No. | Lothian Pension Fund | | |
|-------------|------------------------------------------|------------------------------------------------------------------------------------------------------------------------------|-----------------|
| | Supplier | Justification for waiver | Value |
| Waiver 1614 | ClubVita | Subscription to services from sole provider of specialist longevity modelling to Local Government Pensions. | £18,000 |
| Waiver 1660 | FTSE Russell | Sole supplier of benchmark index data required by Lothian Pension Fund oversight body. | £35,995 |
| Waiver 1750 | Hermes Equity Ownership Services Limited | Interim arrangement to allow LPF to collaborate with other Pension Fund providers until Scottish Government review complete. | £246,000 |
| Waiver 1779 | Deloitte LLP | Pension related accountancy expertise for tax related audit. | £13,000 |
| Waiver 1785 | Hymans Robertson LLP | Specialist longevity modelling website for Local Government Pension Scheme, sole provider. | £10,000 |
| | | | £322,995 |

5. Next Steps

- 5.1 A further report will be submitted to the Committee in approximately six months' time.

6. Financial impact

- 6.1 Through a robust procurement approach, proactive management of contract cycles, aggregating spend and carrying out competitive procurement where appropriate, this should continue to support commercial efficiency and achieve Best Value for Lothian Pension Fund contracts.

7. Stakeholder/Community Impact

- 7.1 Lothian Pension Fund has been consulted in relation to their expiring contracts, waivers and suppliers in the collation of this report. On an ongoing basis, the CSOs outline the appropriate measures of consultation and approval that must be sought from officers or committee for each waiver, dependent on the expected value.

- 7.2 Due to the significant volumes of activity and numbers of stakeholders involved in purchasing and procuring goods, services and works, CPS relies on services, inclusive of Lothian Pension Fund, to provide accurate information through their Contract Register entries and timely requests for procurement assistance. To mitigate against any risks in this area, data is reviewed for accuracy and reliability in consultation with services.
- 7.3 A waiver denotes a departure from the CSOs. There may be an increased risk if the Lothian Pension Fund has departed from European Union (EU) or Procurement Reform Act requirements. However, each waiver is scrutinised on its own merits in this context and requires appropriate checks and balances both within the directorate concerned and corporately, and is only approved if justifiable given the circumstances or permitted in accordance with EU or obligations.
- 7.4 There are no equalities or sustainability impacts directly arising as a result of this report.

8. Background reading/external references

- 8.1 N/A

9. Appendices

- 9.1 N/A

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Pensions Committee

2.00pm, Wednesday, 25 September 2019

Overpayments of Pension

| | |
|---------------------|-----|
| Item number | 5.5 |
| Executive/routine | |
| Wards | All |
| Council Commitments | |

1. Recommendations

The Pensions Committee is recommended to:

- 1.1 note that the Fund is currently pursuing recovery of an overpayment of pension totalling £13,373.30; and
- 1.2 to further approve that the overpayment should be written off, to the extent that the Fund's pursuit of recovery proves unsuccessful.

Stephen S. Moir

Executive Director of Resources

Contact: Carole Thomson, Pensions Operations and Development Manager, Lothian Pension Fund

E-mail: carole.thomson@edinburgh.gov.uk | Tel: 0131 529 4662

Overpayment of Pension

2. Executive Summary

- 2.1 This report highlights an overpayment of pension totalling £13,373.30 and details the circumstances through which this has arisen.

3. Background

- 3.1 Delegated authority has been granted, in certain circumstances, to write-off pension overpayments up to £3,000. Any overpayment above this limit requires approval of the Committee.

4. Main report

- 4.1 In July 2019, a mistake was discovered in that the Fund had been paying a pension for a dependent child into an incorrect bank account since September 2015. All overseas pension payments are paid directly into a Western Union bank account. A reference number then re-routes pension payments into each individual overseas pensioner bank account. A mis-keyed reference number meant that payment was made directly to the bank account of another pensioner. Both the dependent child and unintended recipient reside in Australia.
- 4.2 Although procedures were in place for manual checking of the input, the mistake was not spotted by the member of staff responsible for the validation.
- 4.3 The dependent child has a sibling whose benefit entitlement has been paid correctly. The death of children's mother was a late notification (pensioner member), so the father received a death grant together with a backdated pension for himself and one of his children. It appears that he failed to notice that the pension payments only reflected entitlement for one child instead of two. The Fund has written to the father and made payment to the child. In accordance with Scottish Local Government Pension Scheme regulations, payment is being made to an account held in the child's name.
- 4.4 Payment to the incorrect bank account has been stopped.
- 4.5 The unintended recipient of the child's pension, this also including the initial backdated lump sum, is 79 years old. This member's own pension is only £110 per

month. Conscious of the potential sensitivities, the Fund has written to the member requesting that he should contact a named member of staff to discuss his pension. This will enable initial soundings as to the potential for any debt recovery.

- 4.6 Requisite control enhancements have been made by the Fund to prevent recurrence. Since the initial payroll processing error in 2015, payroll processing is now embedded within the core pension administration team and the Fund no longer employs any member of staff with discrete payroll responsibilities. More fundamentally, a monthly check is now being made against all overseas pensioner pension payments to ensure that both the reference number and bank details are correct.

5. Next Steps

- 5.1 The overpayment will be pursued further. Depending on the specific circumstances of this case, for example, if recovery of the overpayment would cause the pensioner undue hardship, it may not be possible to recoup any significant proportion of the overpayment. Once investigations have been concluded, a letter will be sent to the overseas pensioner member to confirm the decision of Committee.

6. Financial impact

- 6.1 The expenditure has already been reflected in the relevant financial statements of Lothian Pension Fund and so there is no additional financial impact arising from the overpayment of pension, except that a decision not to pursue the amounts does crystallise the loss in ruling out any future recovery.

7. Stakeholder/Community Impact

- 7.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the fund and they are invited to comment on the relevant matters at Committee meetings.
- 7.2 There are no adverse health and safety, governance, compliance, or regulatory implications as a result of this report.
- 7.3 There are no adverse sustainability impacts arising from this report.

8. Background reading/external references

- 8.1 None.

9. Appendices

9.1 None.

Pensions Committee

2.00pm, Wednesday, 25 September 2019

Service Plan Update

| | |
|---------------------|-----|
| Item number | 5.6 |
| Executive/routine | |
| Wards | All |
| Council Commitments | |

1. Recommendations

The Pensions Committee is recommended to:

- 1.1 note progress of the fund against the 2018-2020 Service Plan, together with the regulatory update and specifically;
- an update on performance indicators: and
 - the Local Government Pension Scheme (Scotland) Regulations.

Stephen S. Moir

Executive Director of Resources

Contact: John Burns, Chief Finance Officer, Lothian Pension Fund

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

Service Plan and Regulatory Update

2. Executive Summary

- 2.1 The purpose of this report is to provide an update on progress against the 2018–2020 Service Plan, performance indicators and the actions to enable the fund to meet its key objectives.
- 2.2 Overall progress is being made against the service plan objectives for 2019/20. An underspend is projected for the financial year.

3. Background

- 3.1 The 2018-2020 Service Plan outlines the performance indicators and the key actions to enable the fund to meet its four key objectives:
 - Customer First;
 - Honest and Transparent;
 - Working Together; and
 - Forward Thinking.
- 3.2 The Lothian Pension Fund's Service Plan is reviewed every two years to ensure its key performance indicators and objectives are up-to-date, clear, challenging and achievable.

4. Main report

- 4.1 Progress is being made against the service plan. Progress of particular note since the last update to Committee is shown below. The following areas are covered elsewhere on the agenda:
 - audit reports and plans;
 - pensions data quality; and
 - fraud prevention.

Local Government Pension Scheme (Scotland) Regulations

- 4.2 As previously reported to Committee, new Scheme Regulations were introduced with effect from 1 June 2018. These changes including the earliest age members can voluntarily retire reducing it from age 60 to age 55. However, amendments to the Transitional Provisions, including Rule of 85 protections, were not made which resulted in further legislation being required to allow deferred members age 55 and over to retire.
- 4.3 The Scottish Public Pensions Agency (SPPA) issued an amendment to the Regulations on 28 June 2019 and this has resulted in the transitional provisions being updated.

Annual Benefits Statements

- 4.4 Employers must provide membership data to allow the Fund to meet The Pension Regulator's statutory deadline of issuing annual benefit statements by the end of August. All employers provided data by the deadline of 19 April, this being the first time ever full compliance has been achieved.
- 4.5 At the time of writing 52,152 annual benefit statements were produced representing 99.96% of the requirement. It is fully expected that 100% of records will have a statement by the statutory deadline of 31 August 2019.
- 4.6 Included in this total are 18,299 deferred members where 100% of records have been issued with an annual benefit statement. 3,800 of these members who are age 55 or over on 28 June 2018 are now eligible to have their benefits paid following the recent Regulation change. Information on how to claim their benefits was included with their annual newsletter.
- 4.7 For 2,132 deferred members, the Fund does not hold a current address and has been unable to send newsletters to these. This represents 11.6% of the deferred membership. A specialist tracing company has been appointed and attempts to trace these members are ongoing.
- 4.8 A separate update on data quality is being provided to the Audit Sub-Committee on 24 September.

Awards

- 4.9 The Fund has been shortlisted for 4 categories in the LAPF Investment Awards. The awards will be announced on 19th September 2019. The shortlisted categories are Fund of the Year (over £2.5billion), Fund of the Year (under £2.5billion) for Scottish Homes Fund, Private markets and Scheme Administration. A verbal update will be provided at the Committee meeting.

Performance Indicators

- 4.10 Performance Indicators for the second quarter of the 2019/20 financial year are provided in appendix 1. Committee will recall there are currently 27 performance indicators including a wider range of pensions administration indicators.
- 4.11 Nine of the indicators are currently amber.

4.12 These include:

- Overall customer satisfaction at 87.2% against a target of 91%.
- 83.3% of transfer-in quotes were provided within 10 working days of receiving the Cash Equivalent Transfer Value. The target is 96%. There is currently significant resource pressure in the Pension Administration section. However, ongoing recruitment should ensure this position should recover over the year.
- Level of sickness absence of 4.72% with a target of 4%.
- Proportion of staff engaged as measured in the Staff Engagement Survey 69% with a target of 70%.

Website

4.13 The Fund has wished to replace the current website for a number of years and has begun two projects that due to changes in supplier were not made live. Hymans Robertson provide a bespoke member website and the fund will move to this in Autumn 2019.

4.14 At the same time, the current site will be updated to provide a more user-friendly web experience for users including employers within the current publishing platform provided by the City of Edinburgh Council.

Membership and Cashflow monitoring

4.15 Tables detailing the cashflows as at the end of July 2019 and projections for the financial year are shown in Appendix 2. These have been prepared on a cashflow basis (compared to the accruals basis of the year-end financial statements and budget projections).

4.16 It is expected that Lothian Pension Funds' active members as a proportion of total membership will continue to decrease during the year, causing a fall in contributions and increase in pension and lump sum payments.

4.17 Funds' expenditure cashflows are anticipated to continue to exceed cashflow income

4.18 For the last three years Lothian Pension Fund has had a negative cash flow position, whereby pension payments exceed total contributions received. This is a trend that is likely to continue for the foreseeable future. Increased investment income has been targeted in recent years for this scenario, which is expected to exceed net cashflow for the long term.

5. Next Steps

5.1 The Fund will continue to progress matters in accordance with the Service Plan 2018-20 and respond to regulatory consultations as appropriate.

6. Financial impact

6.1 A summary of the projected and year-to-date financial outturn compared to the approved budget for 2019/20 is shown in the table below:

| Category | Revised Approved Budget £'000 | Projected Outturn £'000 | Projected Variance £'000 | Budget to date £'000 | Actual to date £'000 | Variance to date £'000 |
|------------------------------------|----------------------------------|----------------------------|-----------------------------|-------------------------|-------------------------|---------------------------|
| Employees | 5,354 | 5,106 | (248) | 1,785 | 1,517 | (268) |
| Transport & Premises | 255 | 255 | - | 85 | 79 | (6) |
| Supplies & Services | 2,128 | 2,128 | - | 709 | 625 | (84) |
| Investment Managers Fees -Invoiced | 5,200 | 4,500 | (700) | 1,733 | 1,560 | (173) |
| -Uninvoiced | 19,700 | 19,700 | - | 6,567 | 6,567 | - |
| Other Third Party Payments | 1,439 | 1,399 | (40) | 480 | 441 | (39) |
| Central Support Costs | 643 | 672 | 29 | 214 | 224 | 10 |
| Depreciation | 147 | 147 | - | 49 | 49 | - |
| Gross Expenditure | 34,866 | 33,907 | (959) | 11,622 | 11,062 | (560) |
| Income | (1,915) | (1,915) | - | (638) | (658) | (20) |
| Total Cost to the Funds | 32,951 | 31,992 | (959) | 10,984 | 10,404 | (580) |

6.2 The financial outturn includes year to date budget, actual expenditure and variance as at the end of July 2019. Year to date actual expenditure includes provision for services incurred but for which no invoice has yet been received.

6.3 The projection shows an underspend of approximately £959k. The key variances against budget are:

- *Employees* - £248k underspend. A review of LPFE's staffing structure took place in the first quarter of the year with a number of new posts created and responsibilities clarified. Currently, the Fund is recruiting staff to fill these positions, with this timing difference creating the majority of the expected underspend. All new hires have been achieved through salary levels at or below the existing budget.
- *Investment Management Fees (Invoiced)* – £700k underspend. The Aberdeen Standard property portfolio will be managed by the newly created, in-house investment team at the end of September, this delivering a significant saving against budget. Similarly, the Fund has also secured savings through realisation of £50m in externally managed equity, this being used to fund purchases of investment grade credit (fees to be reflected in uninvoiced expenditure).
- *Other Third Party Payments* - £40k underspend; savings forecast on global custody given the Lothian Buses consolidation into the main Fund and also more favourable terms agreed with the Fund's custodian in the two year contract extension.
- *Central Support Costs* - £29k overspend. This overall sum remains provisional pending clarification of the Fund's ICT service arrangements. At present, no change has been

reflected in the overall budgetary provision of £500k for ICT, albeit that the Fund recognises that the charge levied by the Council for ICT and Telephony services provided through by the Administering Authority's Digital Services Team and its contract with CGI UK Ltd is anticipated to be higher than in previous years. Estimated charges of £166k (assuming full year) represent an 82% increase on the 2018/19 fee, although other elements of the overall recharge to the Fund for Administering Authority professional and technical support services are also being reviewed due to the Fund's increasingly independent service arrangements. The forecast overspend on this cost centre represents net higher than budgeted costs for the remaining support services provided by the Council through Annual Service Level Agreement.

- 6.4 Uninvoiced expenditure (i.e. investment management costs deducted from capital) is assumed to be in-line with budget. There has been no change to the investment strategy for the period, on which the budgeted figures are based. The fund continues its efforts to enhance the monitoring of these fees and is working with managers to improve the transparency of these charges.
- 6.5 The Fund will provide an update on its investment shared service activities (cost allocation model) to Committee at its meeting in December 2019.

7. Stakeholder/Community Impact

- 7.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the fund and they are invited to comment on the relevant matters at Committee meetings.
- 7.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report.
- 7.3 There are no adverse sustainability impacts arising from this report. Background reading/external references

8. Background reading/external references







- 8.1 [LPF Service Plan 2018-2020](#)

9. Appendices


Appendix 1 – Service Plan Performance Indicators

Appendix 2 – Forecasted Cashflow

Service Plan Performance Indicators – Targets & Actual Performance 2019/20

| | 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 in early 2020 | | | Retain CSE Award | Not yet known |
| Maintain Pensions Administration Standards Association (PASA) accreditation (assessment March 2019). | Annual accreditation to be carried out in Autumn 2019 (delayed by review of process by PASA) | | | Retain PASA accreditation | Not yet known |
| Overall satisfaction of employers, active members and pensions measured by surveys | Rolling 12-month performance to end June 2019 is 87.2% | | | 91% |  |
| Proportion of active members receiving a benefit statement and time of year statement is issued | | | | 100% issued by 31 August 2019 | Not known yet |
| Forward Thinking | | | | | |
| Performance and Risk of Lothian Pension Fund | Actual 11.3%pa, Benchmark 10.9%pa. Exceeding benchmark with lower risk. | | | 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 | 96.6% | | | Greater than 92% |  |
| Provide new members with scheme information within 20 working days of getting details from employer | N/A | | | 100% | |
| Provide transfer-in quote within 10 working days of receiving the Cash Equivalent Transfer Value (CETV) from member's previous pension provider. | 83.33% | | | 96% |  |
| Notify members holding more than 3 months, but less than 2 year service, of their options at leaving. As there is a one month and a day lying period, the target is within 10 days of the end of the lying period or after the employer providing full leaving information if later. | 82.61% | | | 85% |  |
| Pay a refund of contributions within 7 working days of receiving the completed declaration and bank detail form. | 95.12% | | | 91% |  |

| | Q1 April to June | Q2 July to Sept | Q3 Oct to Dec | Target | Status |
|---------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|--------------------|------------------|---------------------|---------------|
| Notify early leavers entitled to deferred benefits of their rights and options within 10 days of being informed of end of pensionable service. | 98.83% | | | 91% | |
| Provide a maximum of one guaranteed Cash Equivalent Transfer Value (CETV) within 10 working days of receiving a request. | 98.38% | | | 91% | |
| Payment of CETV within 20 working days of receiving all completed transfer out forms. | 95.24% | | | 96% | |
| Pay lump sum retirement grant within 7 working days of receiving all the information we need from the member. | 99.13% | | | 96% | |
| Estimate requested by employer of retirement benefits within 10 working days. | 93.64% | | | 91% | |
| Pay any lump sum death grant within 7 working days of receipt of the appropriate documentation. | 93.24% | | | 96% | |
| Notification of dependant benefits within 5 working days of receiving all necessary paperwork. | 97.98% | | | 96% | |
| Acknowledge the death of a member to next of kin within 5 working days. | 98.65% | | | 96% | |
| Respond in writing within 20 working days to formal complaints that have escalated from frontline resolution, or recorded directly as an investigation. | 100% | | | 100% | |
| Pension Admin Workflow - Non Key Procedures Performance. | 81.39% | | | 76% | |
| Honest & Transparent | | | | | |
| Audit of annual report | | | | Unqualified opinion | Not yet known |
| Percentage of employer contributions paid within 19 days of month end | 99.5% | | | 99.00% | |
| Data quality – compliance with best practice as defined by the Pensions Regulator | Assessment made at 2019 year-end | | | Fully compliant | Not yet known |
| Monthly Pension Payroll paid on time | 100% | | | Yes | |
| Working Together | | | | | |
| Level of sickness absence | 4.72% | | | 4% | |
| Proportion of staff engaged as measured in the Staff Engagement Survey | 69% | | | 70% | |

| | Q1 April to June | Q2 July to Sept | Q3 Oct to Dec | Target | Status |
|---------------------------------------------------------------------|----------------------------|---------------------------|-------------------------|---------------|-------------------------------------------------------------------------------------|
| Percentage of staff that have completed two days training per year. | 66.3% | | | 100% |  |

Service Plan Membership and Cashflow Monitoring 2019/20

| Lothian Pension Fund | 2019/20 YTD | 2019/20 Projected |
|--------------------------------------------------------------|------------------------|------------------------------|
| <u>Income</u> | £'000 | £'000 |
| Contributions from Employers | 60,990 | 183,000 |
| Contributions from Employees | 17,198 | 50,500 |
| Transfers from Other Schemes | 1,898 | 4,500 |
| | 80,086 | 238,000 |
| <u>Expenditure</u> | | |
| Pension Payments | (58,634) | (178,200) |
| Lump Sum Retirement Payments | (21863) | (61,500) |
| Refunds to Members Leaving Service | (175) | (650) |
| Transfers to Other Schemes | (3,563) | (13,000) |
| Administrative expenses | (833) | (2,500) |
| | (85,068) | (255,850) |
| Net Additions/(Deductions) From Dealings with Members | (4,982) | (17,850) |

| Scottish Homes Pension Fund | 2019/20 YTD | 2019/20 Projected |
|--------------------------------------------------------------|------------------------|------------------------------|
| <u>Income</u> | £'000 | £'000 |
| Administration charge | 80 | 80 |
| <u>Expenditure</u> | | |
| Pension Payments | (2,177) | (6,450) |
| Lump Sum Retirement Payments | (112) | (550) |
| Transfers to Other Schemes | - | (100) |
| Administrative expenses | (27) | (80) |
| | (2,316) | (7,280) |
| Net Additions/(Deductions) From Dealings with Members | (2,236) | (7,200) |

Pensions Committee

2.00pm, Wednesday, 25 September 2019

Risk Management Summary

| | |
|---------------------|-----|
| Item number | 5.7 |
| Executive/routine | |
| Wards | All |
| Council Commitments | |

1. Recommendations

The Pensions Committee is requested to:

- 1.1 note the Quarterly Risk Overview.

Stephen S. Moir

Executive Director of Resources

Contact: Struan Fairbairn, Chief Risk Officer, Lothian Pension Fund

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Susan Handyside, Customer Service & Compliance Officer, Lothian Pension Fund

E-mail: susan.handyside@edinburgh.gov.uk | Tel: 07771 378238

Risk Management Summary

2. Executive Summary

- 2.1 In line with the Pension Funds' ongoing risk management procedures, this paper provides an overview of the Fund's risk analysis for consideration by the Committee.

3. Background

- 3.1 The Lothian Pension Funds' risk management procedures require the Fund to:
- 3.1.1 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
 - 3.1.2 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)

4. Main report

- 4.1 The Operational Risk Register is issued to the Conveners of the Pensions Committee and the Pensions Audit Sub Committee and the Independent Professional Observer on a quarterly basis.
- 4.2 The Quarterly Risk Overview, as at 19 August 2019, is set out in Appendix 1 to this report for consideration.
- 4.3 A verbal update of the status of various IT projects will be provided as part of the separate paper specifically on the Fund's current and future ICT provision.
- 4.4 At its meeting in 26 June 2019, the Pension Committee requested that a separate risk to monitor cybersecurity be included in the risk register. Risk 35 'Cybersecurity protections and/or back-up not sufficient to prevent cyber-attacks or minimise their

impact' has now been added to the register and will be monitored on a quarterly basis alongside all other risks.

- 4.5 From December 2019 Appendix 1 will include a three year graphic of the risks as requested at the Pension Committee on 26 June 2019.

5. Next Steps

- 5.1 Quarterly review and reporting of risk register.

6. Financial impact

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

7. Stakeholder/Community Impact

- 7.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the pension funds and they are invited to comment on the relevant matters at Committee meetings.
- 7.2 The forward planning of the Committees' agendas should facilitate improved risk management and governance for the pension funds.
- 7.3 There are no adverse sustainability impacts arising from this report.

8. Background reading/external references

- 8.1 None.



9. Appendices




Appendix 1 – Quarterly Risk Summary, as at 19 August 2019





QUARTERLY RISK OVERVIEW

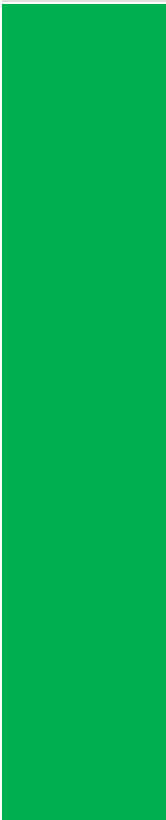
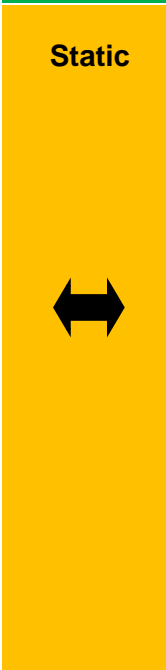
19 August 2019



UPDATE ON MOST NOTABLE RISKS




| Risk & Reference Number | Update | Trend / RAG |
|-----------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------|
| <p>Adverse Investment performance causes funding levels to fall requiring higher employer contributions. (1)</p> | <p>The fund is considering the outcomes from the Joint Investment Strategy Panel's investment strategy review with its partner funds, and prioritising implementation of resulting strategies to improve synergies across the portfolios of the three funds.</p> | <p>Static</p>  |
| <p>Adverse change in non-investment actuarial assumptions cause funding levels to fall requiring higher employer contributions (2)</p> | <p>The contribution stability mechanism will be reviewed towards the end of the year with training for the Pension Committee and Board Members taking place in November. A report will be presented to the Pensions Committee in December, and in advance of the 2020 valuation.</p> <p>The fund continues to review its communication with employers around comparative LGPS contribution rates, including on the longer-term implications and the potential benefits of LPF's unitisation strategy and internal investment approach. Effective communication regarding this is critical to the fund's wider strategy of ensuring the long-term sustainability of the scheme and that it is a destination of choice for employers.</p> <p>Monitoring of funding levels is also ongoing, as is engagement with employers to put in place bespoke arrangements to help manage affordability issues. <i>See below for risk 3.</i></p> | <p>Static</p>  |

| Risk & Reference Number | Update | Trend / RAG |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------|
| <p>Failure of an employer to pay contributions causes funding levels to fall, requiring higher contributions from other employers (3)</p> | <p>The funding approach introduced in the 2014 actuarial valuation for employers that are close to exiting the scheme reduces the overall risk to the fund and the other employers.</p> <p>The fund continues to engage with employers regarding any potentially adverse financial impact of the funding strategy and will consult with employers on the newly revised Strategy.</p> <p>Funding agreements for payment of cessation debt are being put in place where relevant for employers exiting the fund. As above, the fund continues to pursue guarantees and securities from employers (where appropriate) and updated admission agreements in order to further mitigate this risk, which is becoming more applicable as the fund considers exits from larger employers.</p> <p>The fund continues to work with some employers to improve affordability by adopting a higher risk investment strategy in consideration for additional security being provided by those employers to off-set any additional risk to the fund and its other stakeholders.</p> | <p>Decrease</p>  |
| <p>Failure of IT systems used in the Fund with serious consequences for investment management, benefit administration and oversight activities (7)</p> | <p>The fund continues to experience delays and service disruption across a number of areas. Operational issues are, to some extent, being dealt with by liaising directly with the fund's ICT relationship manager in the Council and notifying CGI of delays and disruptions experienced.</p> <p>A further ICT update is being presented to the Committee as part of the private B agenda this quarter and will provide a more detailed overview of this risk. However, the risk has reduced due to the introduction of three new controls, (i) the digital strategy / ICT pathway (approved by Pensions Committee in June 2019) giving approval to exit the provision of ICT support from CEC and its provider CGI, (ii) the appointment of an IT oversight manager (August 2019) and (iii) the increased direct contact with CGI to further our aim of closer oversight and monitoring.</p> | <p>Decrease</p>  |
| <p>Elected members take decisions against sound advice (9)</p> | <p>The risk has reduced as a result of the governance review now being well underway as reported in March and in June 2019 and the reduced levels of external lobbying. The Committee and Board will continue to receive quarterly governance updates until December, when the substance of the review process is expected to conclude.</p> <p>In addition, the two non-elected Committee members, John Anzani and Richard Lamont have been reappointed for a further two years.</p> | <p>Decrease</p>  |

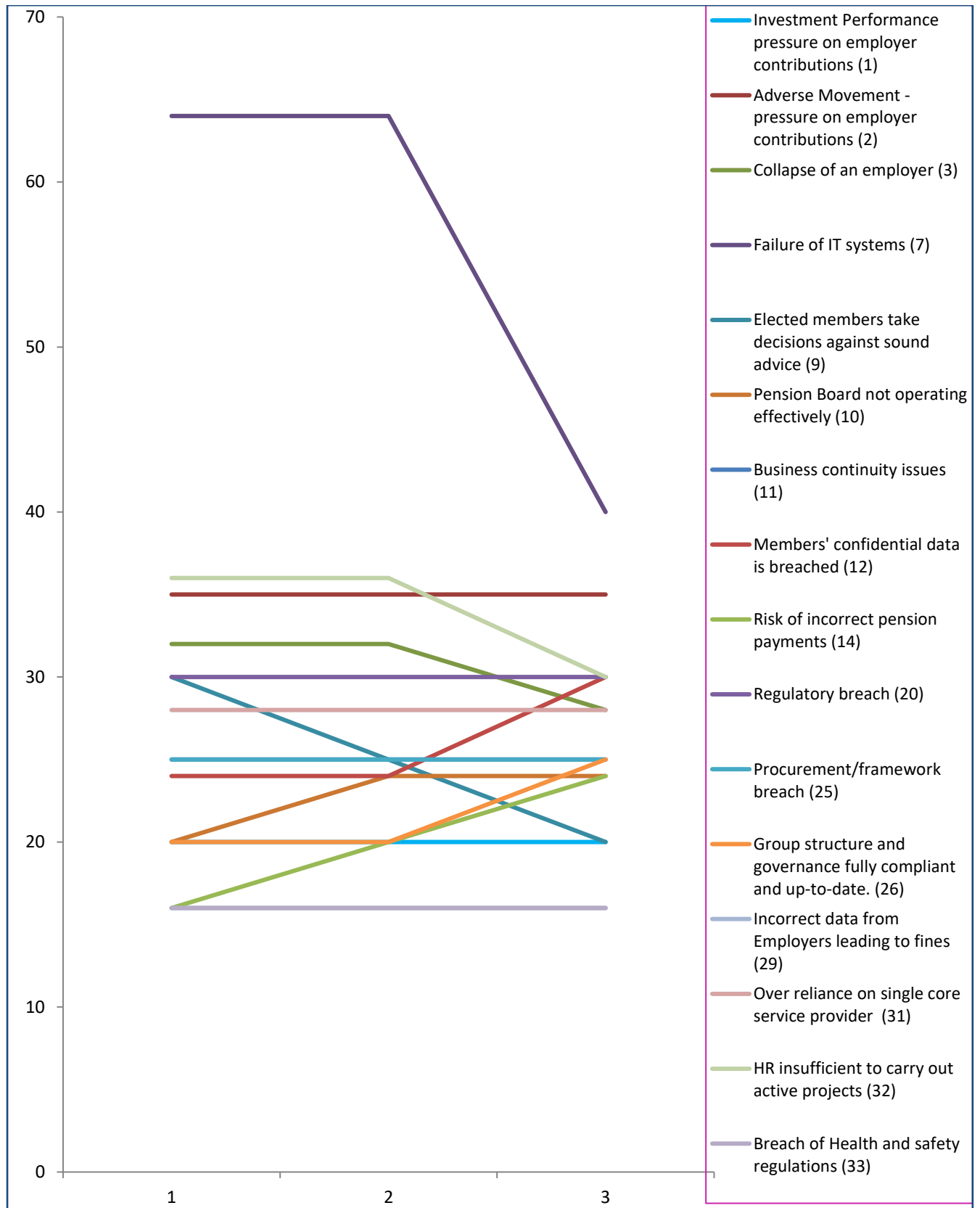
| Risk & Reference Number | Update | Trend / RAG |
|----------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Pension Board does not operate effectively to the detriment of the Fund. (10) | The vacancies on the pension board and the higher turnover of board members had raised this risk slightly last quarter. However, this has reduced again due to the appointment of an employer representative leaving only one vacancy on the Pension Board which is expected to be filled by the next Committee meeting in December. | <p style="text-align: center;">Decrease</p> <p style="text-align: center;"></p> |
| Business continuity issues (11) | <p>Business continuity has been discussed with other key third party providers and procedures added to the fund's business continuity plan. It is also being addressed as part of the pensions administration system contract and with others as opportunities prevail.</p> <p>The current ICT review process has highlighted the need to include more detail in the business continuity plan around the fund's directly managed third party ICT systems and specific systems architecture, business continuity options and future preferences. This will be picked up as the wider ICT project develops.</p> <p>The fund will present a report to Committee in September that provides an update on the review to assess its current and future accommodation requirements, as well as its wider organisational/staff requirements.</p> <p>The business continuity risk is expected to reduce once the ICT and office matters have been addressed, allowing those areas to be properly taken into account in the business continuity plan.</p> | <p style="text-align: center;">Static</p> <p style="text-align: center;"></p> |
| Members' confidential data is lost or made public. Breach of Data Protection Act. (12) | <p>In order to strengthen the Funds controls the it has requested that the Pensions Administration system provider set tolerance controls for employers to alert them when uploading data on to the system. Until the tolerance levels are in place the risk has been increased slightly. The fund will continue to mitigate this risk by continuing manual checks until automatic checks are in place.</p> <p>A new automatic mailing system is now in place, which has significantly reduced the amount of manual printing and mail compilation by LPF staff. This should reduce the risk of manual error in the mailing process, but currently remains under review to ensure there are no weaknesses in the automated process.</p> | <p style="text-align: center;">Increase</p> <p style="text-align: center;"></p> |
| Risk of incorrect pension payments (14) | <p>Closure of the outstanding management action in respect of the high rated Internal Audit finding is dependent upon the specific methodology for measurement of "Key Performance Indicator- 99% accuracy of pensions calculations" being defined and contractually embedded with the pensions administration software supplier. This had been expected in early 2019. Following restructuring of its operations and the departure of its Group Client Director in April 2019, however, the supplier withdrew its own proposal (of the KPI definition) at a point when LPF had already accepted such and the matter was in the</p> | <p style="text-align: center;">Increase</p> <p style="text-align: center;"></p> |

| Risk & Reference Number | Update | Trend / RAG |
|-------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------|
| | <p>hands of the company's legal officer for formal update to the core contract. LPF has been pursuing matters, as a priority, with the company's new Chief Executive since then. At a meeting on 15 August 2019, the company reiterated its commitment to ensure compliance with its contractual obligations and a revised methodology is expected from the company imminently. The Chief Internal Auditor has been advised of expected implementation (including validation review) by 31 October 2019. Given the fundamental importance of assurance on this matter for LPF's pensions administration service, our contractual stipulation of KPI embodying 99% threshold level of calculation accuracy, failure to meet such leading to the imposition of contractual Service Credit penalties, represents a critical advance. The supplier has advised that it does not have any other Local Government Pension Scheme (LGPS) administering authority client which has insisted upon such assurance incentivisation.</p> <p>Reflecting this position, together with risk 12 in respect of tolerance controls, the assessed risk has increased.</p> |  |
| <p>Regulatory breach (20)</p> | <p>The fund continues to be engaged in a compliance readiness project to ensure it is well placed for additional regulations that will come into scope on LPFI providing extended services to collaborative partners. This also now includes the impact of the Competition Authority's recent order around the investment consultancy industry/services, and the subsequent implementing regulations and guidance from the government bodies and regulators (TPR, FCA and HMRC).</p> <p>BDO (formerly Moore Stephens) continues to be instructed to carry out on-site regulatory compliance audits of LPFI in order to ensure assurance in this area.</p> <p>The fund has reviewed the implications of the Senior Manager and Certification Regime coming into force at the end of 2019 and a full compliance implementation programme is currently in process.</p> | <p data-bbox="1337 1055 1417 1088">Static</p>  |

| Risk & Reference Number | Update | Trend / RAG |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------|
| | <p>As above, the fund's ICT provision is a critical aspect of its ongoing compliance with existing and enhanced data protection and financial services regulations, and so this risk will remain amber until such time as the fund has sufficiently addressed its key ICT strategies. In particular, the ICT transformation will support key strategic initiatives, including the separation of the financial ledger system/accounts from CEC and the implementation of a new document management system.</p> <p>The fund has reviewed any necessary Brexit contingency planning (including any staff issues) in the lead up to a possible exit of the EU, but as a UK based pension fund, collaborating with other similar UK based funds, the direct and immediate impact is expected to be limited. The position therefore remains as reported in previous risk updates.</p> | |
| <p>Procurement/frame work breach (25)</p> | <p>The fund is liaising with CEC's procurement team to ensure that the processes and procedures are sufficiently streamlined for the fund's specific needs and circumstances where appropriate. The amendment of the Council's contract standing orders and terms of reference provide the Pension Committee with greater oversight and procurement processes to become more streamlined.</p> <p>Procurement compliance is an important and necessary part of the fund's obligations, but the governance around this continues to be a material inefficiency for the fund - with a direct impact on resource and adverse reputational implications with critical suppliers and the wider business sector. This continues to be addressed through the fund's Governance Review.</p> | <p>Static</p>  |
| <p>Group Structure and Governance not fully compliant and up to date (including integration of subsidiaries) or working effectively resulting in adverse impact on group strategy and business plan delivery (26)</p> | <p>As requested by the Pensions Committee, refresher training on the group structure will be provided in September 2019.</p> <p>The risk has slightly increased to reflect transitional risk in implementing both the organisational development review of the staff structure and also the changes being introduced by the governance review. In addition, LPF continues to monitor the resourcing of certain internal teams on which it relies for intra-group services.</p> | <p>Increase</p>  |

| Risk & Reference Number | Update | Trend / RAG |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------|
| <p>Limited or incorrect data from Employers leading to incorrect valuation of liabilities /benefit payments / fines from Pensions Regulator (post April 2015) (29)</p> | <p>The Fund continue PAS monitoring and the process is now underway to address poor performance, the details of which will be presented to the Pension Committee under a private agenda in September 2019. Until the process is complete the risk has increased.</p> | <p>Increase</p>  |
| <p>Over reliance on single service provider for core functions, potential leading to loss of service on the collapse or withdrawal of that provider. or artificially inflated costs (31)</p> | <p>This risk remains at amber and is likely to do so until there is less dominance of key service providers and greater options available to the Fund.</p> | <p>Static</p>  |
| <p>Human resource within the LPF Group not sufficient to carry out core tasks in conjunction with active or anticipated projects (32)</p> | <p>The risk remains under close scrutiny due to the continuing resource drain attributable to the significant time spent on wider strategic initiatives, including collaboration, employer initiatives, other national initiatives and liaison with CEC services to manage service provision and/or provide assurance for oversight functions. However, the risk has been significantly reduced following the successful recruitment to key roles identified in the Organisational Development Review. Implementation of this strategy nevertheless continues and requires to be bedded in.</p> | <p>Decrease</p>  |
| <p>Cybersecurity protections and/or back-up not sufficient to prevent cyber-attacks or minimise their impact (35)</p> | <p>At its meeting on 26 June 2019 the Pension Committee asked that Cybersecurity be monitored by the Fund separately to the ICT risk (7) and the Business Continuity risk (11). At its management risk meeting on 19 August 2019 the Fund discussed and agreed monitoring and controls for the new risk with the help of the new ICT Oversight manager.</p> | <p>New Risk</p> |

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

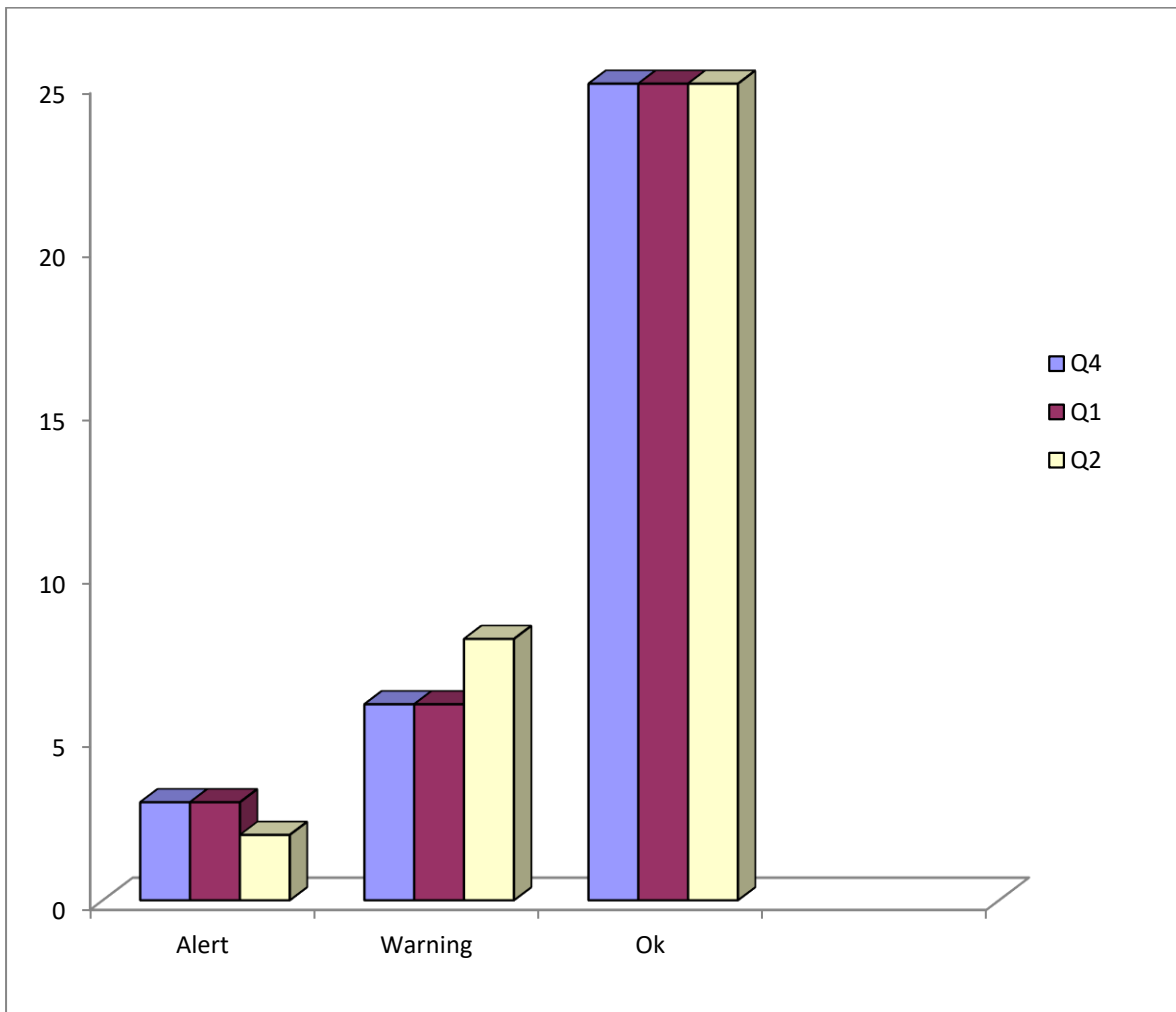


OTHER KEY POINTS

| | Comments |
|--------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| New notable risks | Cybersecurity protections and/or back-up not sufficient to prevent cyber-attacks or minimise their impact (35) |
| Other new risks | None. |
| New controls | <p>Investment management oversight model including reviews, policy statements and quantitative analysis (1)</p> <p>Ongoing management of staff data management on systems and manual inputs. (6)</p> <p>IT Oversight and Governance Manager appointed (August 2019). (7, 35)</p> <p>Increased direct contact with CGI to further our aim of closer oversight and monitoring. (7)</p> <p>Digital strategy / ICT pathway approved by Pensions Committee (June 2019) giving approval to exit CGI partnership. (7)</p> <p>Non-Elected members appointed. (9)</p> <p>Pending action from system provider to apply both tolerance limits and additional controls for bulk uploads of member data from employers through its i-Connect portal, LPF is undertaking its own validation each day on live system. (12, 14)</p> <p>Extended reminders as part of PAD approvals. (16)</p> <p>Compliance procedures. (35)</p> <p>Contract checks generally. (35)</p> <p>Third party supplier management process. (35)</p> |
| Eliminated risks | None. |

| | Comments |
|--------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Notable initiatives / actions | <p>Admission agreement reviews and update following employer covenants review ongoing. (3)</p> <p>Implementing a 'whole of group' succession plan and SLT organisational review process underway. (4)</p> <p>2019 Governance Review and proposed outcomes. (4, 9, 12)</p> <p>Definition of KPI re accuracy of pensions calculations to be contractually agreed with the supplier (14)</p> <p>Review of all staff role profiles to ensure greater consistency, clear understanding of roles and training requirements for each role within the fund. (6)</p> <p>Enhanced cross-team training and CPD to continue to be developed. (6) Reviewing the fund's present and future accommodation requirements. (11)</p> <p>Detailed review of existing CGI and third-party supplier systems, controls, prevention measures and governance around cyber security and our own monitoring and transparency of this. (35)</p> |
| Material litigation | None. |

All Risks: Status Overview



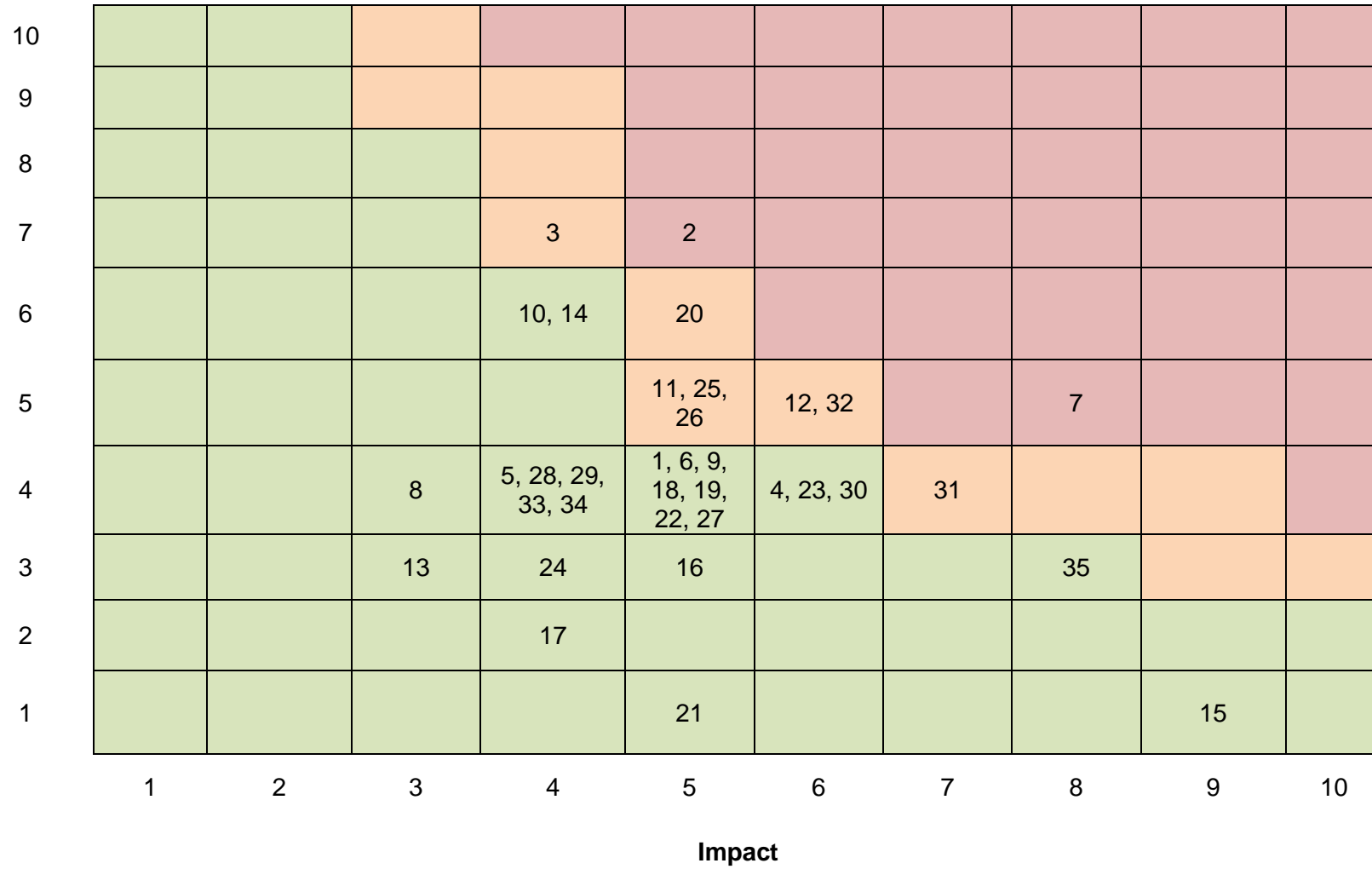
Quarter 1
2019/20 All Risks: Impact and Probability Overview

Page 310
Probability

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|----|---|----|-------------------|--------------------------|---------------|----|---|----|---|----|
| 10 | | | | | | | | | | |
| 9 | | | | | | | | | | |
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| 6 | | | 10 | 20 | 32 | | | | | |
| 5 | | | 14 | 9, 11, 25 | | | | | | |
| 4 | | 8 | 5, 28, 29, 33, 34 | 1, 6, 18, 19, 22, 26, 27 | 4, 12, 23, 30 | 31 | | | | |
| 3 | | 13 | 24 | 16 | | | | | | |
| 2 | | | 17 | | | | | | | |
| 1 | | | | 21 | | | | 15 | | |
| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
| | | | | | | | | | | |




Quarter 2
2019/20 All Risks: Impact and Probability Overview

Page 311



Key: Risks by Number

| | | | |
|----|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | Adverse Investment performance causes funding levels to fall requiring higher employer contributions | 20 | Regulatory Breach |
| 2 | Adverse change in non-investment actuarial assumptions cause funding levels to fall requiring higher employer contributions assumptions- pressure on employer contributions | 21 | FOI process not in accordance with law |
| 3 | Failure of an employer to pay contributions causes funding levels to fall, requiring higher contributions from other employers | 22 | Incorrect communication with members |
| 4 | Failure to recruit, engage and retain talent leads to workforce capability gaps with implications for oversight, control, administration and achievement of service plan goals | 23 | Acting beyond proper authority/delegations |
| 5 | Fraud or theft of Council/Pension Fund assets | 24 | Inappropriate use of pension fund monies |
| 6 | Staff Negligence | 25 | Procurement/framework breach |
| 7 | Failure of IT systems used in the Fund with serious consequences for investment management, benefit administration and oversight activities | 26 | Group Structure and Governance not fully compliant and up to date (including integration of subsidiaries) or working effectively resulting in adverse impact on group strategy and business plan delivery. |
| 8 | Employers make individual or collective employee decisions without considering the impact on the pension fund causing exceptional benefit entitlement or additional fund strain not able to be recovered at point of decision | 27 | Claim or liability arising from shared services |
| 9 | Committee members take decisions against sound advice | 28 | Unauthorised access to PensionsWEB |
| 10 | Pension Board not operating effectively | 29 | Incorrect data from Employers leading to finds etc |
| 11 | Business continuity issues | 30 | Inadequate contractual protection for services |
| 12 | Members' confidential data is breached | 31 | Over reliance on single core service provider |
| 13 | Loss due to stock lending default | 32 | Human resource insufficient to carry out active projects |
| 14 | Risk of incorrect pension payments | 33 | Breach of health and safety regulations |
| 15 | Failure to pay pensions as they fall due | 34 | Inadequate, or failure of, supplier and other third-party systems (including IT and data security) |
| 16 | Market abuse by investment team or others | 35 | Cybersecurity protections and/or back-up not sufficient to prevent cyber-attacks or minimise their impact |
| 17 | Portfolio transition issues | | |
| 18 | Disclosure of confidential information | | |
| 19 | Material breach of contract | | |

| Risk Status | |
|-----------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------|
|  | Materially beyond appetite: resolve urgently where possible (probability and impact total 35 and above) |
|  | Beyond appetite: resolve where possible (probability and impact total 25 to 34) |
|  | Within appetite: monitor (probability and impact total 24 and below) |

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Risk Scoring

| Impact | |
|--------|----------------------------------------|
| 0 | (None) |
| 1 | No discernible effect |
| 2 | Little discernible effect |
| 3 | Some effect noticeable |
| 4 | Some effect on service provision |
| 5 | Noticeable effect on service provision |
| 6 | Some disruption of service |
| 7 | Significant service disruption |
| 8 | Material disruption to services |
| 9 | Major service disruption |
| 10 | Catastrophic |

| Probability | |
|-------------|-------------------------------|
| 0 | (None) |
| 1 | Virtually impossible |
| 2 | Extremely unlikely |
| 3 | Remotely possible |
| 4 | May occur |
| 5 | Fairly likely to occur |
| 6 | More likely to occur than not |
| 7 | Likely to happen |
| 8 | Probably will happen |
| 9 | Almost certainly will happen |
| 10 | Already happening |

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