Public Document Pack

Notice of Meeting and Agenda

Pensions Committee

2.00 pm Wednesday, 20th March, 2024

COSLA Conference Centre (19 Haymarket Yards, Edinburgh, Scotland, EH12 5BH) - COSLA Conference Centre (19 Haymarket Yards, Edinburgh, Scotland, EH12 5BH)

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

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 Any items under "Private Business" will not be published, although the decisions will be recorded in the minute.

Contacts

Kimberley Russell, Company Secretary, Lothian Pension Fund

Tel: 0333 996 1587

Email: rus12k21@lpf.org.uk

Andrew Henderson, Committee Officer, City of Edinburgh Council Email: andrew.henderson@edinburgh.gov.uk

1. Quorum Check

1.1 The Convener will check to ensure a quorum is in attendance to ensure the meeting can proceed.

2. Order of Business

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

3. Declaration of Interests

3.1 Members of the Committee and members of the Pension Board 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.

4. Deputations

4.1 If any

5. Minutes

5.1 Minute of the Pensions Committee of 05 December 2023 – submitted for approval as a correct record — 9 - 18

5.2 Revised Minute of the Pensions Committee of 27 September 2023 – submitted for approval as a correct record. — 19 - 32

5.3 Action Tracker (circulated) — 33 - 34

6. Reports

6.1	Governance Update – report by the Company Secretary, Lothian Pension Fund (circulated)	35 - 48
6.2	Referrals and Recommendations from Pensions Audit Sub-Committee	Verbal Report
6.3	Funding Strategy Statement Update – report by the Chief Finance Officer, Lothian Pension Fund (circulated)	49 - 102
6.4	Actuarial Valuation for Lothian Pension Fund – report by the Chief Finance Officer, Lothian Pension Fund (circulated)	103 - 156
6.5	Actuarial Valuation for Scottish Homes – report by Chief Finance Officer, Lothian Pension Fund (circulated)	157 - 194
6.6	Investment Strategy Review – report by Chief Investment Officer, Lothian Pension Fund (circulated)	195 - 210
6.7	2023/24 Business Plan and Budget Update, report by Chief Finance Officer, Lothian Pension Fund (circulated)	211 - 224
6.8	2024-5 Strategy & Business Plan Inc. Functional Plan and Budget – report by Chief Finance Officer, Lothian Pension Fund (circulated)	225 - 262
6.9	Lothian Pension Fund – Proposed Internal Audit plan for 2024/25 – report by the Head of Internal Audit, City of Edinburgh Council	263 - 276

(circulated)

6.10	External Audit Annual Plan 2023/24 by Azets – report by the External Auditor, Azets (circulated)	277 - 316
6.11	Cost Benchmarking, report by the Chief Investment Officer, Lothian Pension Fund (circulated)	317 - 326
6.12	Risk & Compliance Update, report by the Chief Risk Officer, Lothian Pension Fund (circulated)	327 - 342

7. Motions

7.1 This Committee:

Agrees that the briefing requested on 5 December concerning Lothian Pension Fund holdings in companies with involvement in Israel/Gaza, and circulated to committee members on 13 February, is made public.

8. Resolution to Consider in Private

8.1 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 3, 6 and 8 of Part 1 of Schedule 7A of the Act.

9. Private Business

9.1	Employers Participating in Lothian Pension Fund – report by Chief	343 - 356

Operations Officer, Lothian Pension Fund (circulated)

Deputations

Nick Smith

Service Director, Legal and Assurance

Committee Members

Councillors Watt (Convener), Burgess, Doggart, Nicolson and Ross; John Anzani and Richard Lamont.

Please note that members of the Pensions Board and the Independent Professional Observer will also be invited to attend and participate in the meeting.

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 in its separate capacity as administering authority of the Lothian Pension Fund. The Pensions Committee usually meets 4 times a year (every twelve weeks).

This meeting is being held on a hybrid basis in the Lomond Suite, EICC, Morrison Street, Edinburgh and by Microsoft Teams. The meeting is open to all members of the public. The meeting will be monitored by Kimberley Russell.

Pension Board Members

Alan Williamson, Brian Robertson, Darren May, Jim Anderson (Chair), Sharon Dalli, Thomas Carr-Pollock, Tom Howorth, Nick Chapman and Tony Beecher.

Information about the Pension Board

The Pension Board consists of 10 members, 5 members from the employer bodies and 5 members from trade unions representing members within the pension funds as set out in the regulations.

The role of the Pension Board is to help ensure that the operation of the pension funds is in accordance with the applicable law and regulation.

https://www.lpf.org.uk/us .

Independent Professional Observer

Alison Murray

Information about the Independent Professional Observer

The Independent Professional Observer is appointed by the Lothian Pension Fund to help strengthen the Lothian Pension Fund's governance. The role is to provide independent observations to the Pensions Committee and Pension Board.

The purpose of the role is to enhance the scrutiny of the decision making and provide the Committee and Board with additional experience and knowledge impartial from the Lothian Pension Fund's Officers.

City of Edinburgh Council Oversight

The City of Edinburgh Council has statutory responsibility to administer the Lothian and Scottish Homes pension funds. In order to most effectively carry out that function (and to reflect the separate statutory responsibilities, and regulation, of the pension funds) the City of Edinburgh Council has delegated management responsibility for the pension funds to the Lothian Pension Fund Group and its two arms-length companies LPFE Limited and LPFI Limited. Critical parent oversight continues to be carried out by the Pensions Committee and Dr Deborah Smart, Executive Director of Corporate Services for the City of Edinburgh Council, as the Administering Authority for the Fund, to ensure that its statutory functions are being properly carried out.

Lothian Pension Fund Senior Leadership Team

The senior leadership team responsible and accountable for the business and activities of the

Lothian Pension Fund Group are:

David Vallery, Chief Executive Officer

Emmanuell Bouquet, Chief Investment Officer

Kerry Thirkell, Chief Risk Officer

Alan Sievewright, Chief Finance Officer

Helen Honeyman, Chief People Officer

Further Information and Contact

If you have any questions about the agenda or meeting arrangements, please contact Kimberley Russell, Company Secretary, Lothian Pension Fund, Atria One, 144 Morrison Street, Edinburgh EH3 8EX, Tel 0333 996 1587, email rus12k21@lpf.org.uk.

A copy of the agenda and papers for this meeting will be available for inspection prior to the meeting at the Main Reception, City Chambers, High Street, Edinburgh EH1 1YJ. The agenda, minutes and public reports for this meeting can be viewed via the City of Edinburgh Council committee portal.

This page is intentionally left blank

Pensions Committee Minutes

1.30pm, Tuesday 5 December 2023

Present:

Councillors Watt (Convener), Burgess, Doggart, Nicolson and Neil Ross; John Anzani and Richard Lamont.

Pension Board Members present:

Jim Anderson, Tony Beecher, Sharon Dalli, Tom Howorth, Darren May, and Alan Williamson.

Other Attendees:

Alison Murray (Independent Professional Observer).

Apologies: Brian Robertson, Pension Board Member and Thomas Carr-Pollock, Pension Board Member

1. Quorum

The Clerk confirmed that notice of the meeting had been given and that a quorum was present and the Convener declared the meeting open.

2. Order of Business

The Convener proposed that the order of business be adjusted to allow item 6.3 to be heard after the deputation at item 4.1.

Decision

To agree to adjust the order of business to hear Item 6.3 following the deputation at item 4.1.

(a) Point of Order – Audit Sub-Committee Convener's Annual Update Report

In response to a point of order raised by John Anzani in relation to Standing order 2.5 requesting clarification on the procedure for reports that had not been tabled at the previous meeting. The Convener clarified that as the report had not been submitted as an urgent item at the previous meeting in terms of standing order 2.5 the report would not automatically be submitted to the next meeting. The Convener further advised that the item had been concluded at the previous meeting. Thereafter the Convener agreed to discuss the issue with the Convener or of the Pensions Audit Sub Committee outside of the meeting and to look for ways of moving forward.

Decision

1) To note that the Convener of the Pensions Committee to discuss the issue with the Convener of the Pensions Audit Sub Committee outside of the meeting; and

2) To note the point of order raised by John Anzani.

(b) Point of Order – Update on Legal advice being sought on behalf of the Pensions Committee

In response to a point of order raised by John Anzani raised in relation to the legal advice being sought in relation to the Committees response to the legal review initiated by the Pension Board into the decision making process on Project Forth, The Convener confirmed that she would provide a verbal update at a later point in the meeting.

Decision

To note the point of order raised by John Anzani.

(c) Point of Order – Clarification on advice provided regarding standing order 13.2 and the Local Government Pension Scheme Regulation 2015.

In response to a point of order raised by Jim Anderson, the Convener agreed to invite the Head of Democracy Governance and Resilience to provide clarification regarding the advice provided regarding Standing order 13.2 and the Local Government Pension Scheme Regulations 2015 in relation to Item 6.7 at the meeting of the Pensions Committee on the 27th of September 2023.

Decision

1) To agree to invite the Head of Democracy Governance and Resilience to provide clarification regarding the advice provided regarding Standing order 13.2 and the Local Government Pension Scheme Regulations 2015; and

2) To note the point of order raised by Jim Anderson.

3. Declaration of Interests

(a) Declarations of Interest

John Anzani made a transparency statement outlining that no part of his income was impacted by the City of Edinburgh Council being the administrative authority.

John Anzani made a transparency statement as his wife is a non-Executive Director on the Board of Enjoy Leisure East Lothian.

Item 6.5 Councillor Doggart made a transparency statement as a Fellow of the Institute and Faculty of Actuaries.

Item 9.1 Richard Lamont made a transparency statement as an employee of Visit Scotland

(b) Enhanced conflict of interest register.

Officers took the opportunity to confirm that an enhanced conflict of interest register would be submitted from 2024.

Decision

To note that officers would be submitting an enhanced conflict of interest register in 2024.

4. Deputation

(a) Time To Divest (in relation to item 6.3 Business Plan and Budget Update)
The deputation shared details of the hostilities in Gaza and Israel, emphasising the deputation's opinion on the collective duty to stop atrocities being committed.
The deputation referenced LPF's responsibility to respect human rights and expressed concern in regard to investments the deputation viewed as having links to the crises. The deputation urged members to consider divesting from any such investments.

5. Business Plan and Budget Update

An update on the progress against the 2023-2024 strategy and business plan and performance indicators was provided along with an overview of the actions required to enable the fund to meet its objectives.

Following questions regarding 'The Employee Engagement index KPI of 70% or above' contained within the 2023-2024 Strategy and Business Plan, officers agreed to provide a detailed breakdown of employee engagement.

In response comments made in relation to paragraph 4.26, which referred to higher interest rates divert cash to unproductive interest payments members noted that US Government figures had been used and asked that officers make this clearer in future reports.

Following discussion in relation to the deputation submitted by Time to Divest, members agreed that officers would circulate a briefing note to members to provide more information and context enabling members to consider the issues raised by the deputation.

Decision

1) To note the progress of the Fund against the 2023-24 Business Plan, together with specific updates on:
   - Performance indicators
   - Membership and cashflow monitoring
2) To agree that officers provide a breakdown of employee engagement
3) To agree that officers circulate a briefing note to members to provide more information and context enabling members to consider the issues raised by the deputation. ; and
4) To note that United States Government figures had been used in relation to interest rates, and to request that this was made clear in future reports.

Dissent

Councillor Burgess requested that his dissent to the above decision be recorded.

(Reference – report by the Chief Finance Officer, Lothian Pension Fund, submitted.)

6. Minute

Decision

1) To request that the Committee Clerk seeks clarification for the Minute of the Pensions Committee 27 September 2023in regard to the wording of Section 7 in relation to the decision taken by Falkirk Pension Fund regarding the termination of Project Forth; and

2) To note that the revised minute would be submitted to the next regular meeting.

(Reference – report by the Chief Executive Officer, Lothian Pension Fund, submitted.)

7. Referrals and Recommendations from the Pensions Audit Sub-Committee of 04 December 2023

By way of a verbal update, the Convener of the Pensions Audit Sub Committee acknowledged the attendance of Andy Marchant, Independent Non-Executive Director of LPFE and LPFI, and colleagues from the City of Edinburgh Council's Internal Audit Team at the Audit Sub Committee meeting.

Positive responses were noted regarding the Internal Audit Update. Strong views were expressed in relation to data quality and the failure of employers to provide information on time.

The Audit Sub-Committee took the opportunity to commend the work undertaken by LPF officers in relation to the IT Information Security Update. It was noted that further updates and recommendations will be made at the relevant agenda items.

Decision

1) To note the update provided by the Convener of the Pensions Audit Sub Committee;

2) To commend the work undertaken by officers in relation to the IT Information Security Update; and

3) To note the updates provided by the Convener of the Pensions Audit Sub-Committee at relevant agenda items.

8. Agenda Planning Update

An overview of proposed reports for future Pensions Committee and Pensions Audit Sub-Committee meetings in 2024 was presented. An update was also provided on key actions from the meeting of Pensions Committee in September 2023. It was acknowledged that specific matters and papers that were not set out in the agenda planning document would be brought to the committee in addition to the papers outlined.

In response to members comments regarding the visibility of the action tracker, it was agreed that the action tracker which is currently appended to the Agenda Planning Update would be included as a separate item for discussion on future agendas.

Decision

1) To note the agenda planning document and the action tracker (appendix 2);
2) To note that the Pension Board members are invited to comment on agenda items during Committee meetings;
3) To note that the Audit Sub Committee will have an additional meeting on the 19 March 2024 to consider the actuarial valuation and the AVC review paper;
4) To agree that officers will submit a report in relation to training hours for members;
5) To agree that the action tracker appended to the Agenda Planning Update would be included as an item on future agendas; and
6) To note that a Governance review which will also include Committee and Board effectiveness reviews will be considered for 2024/25.

(Reference – report by the Chief Executive Officer, Lothian Pension Fund, submitted.)

9. Stewardship

An overview of the of the approach to stewardship of the funds' assets was provided with reference being made to the Statement of Responsible Investments which is approved annually by committee. Minor changes to the latest version of the Statement of Responsible Investments were highlighted including clarification on the funds approach to climate change.

The report referenced minor changes to the Statement of Responsible Investments as recommended by officers with clarification being provided of the fund's approach to climate change. Members were also reminded that the LPF's approach of engagement Is validated by the United Nations backed Principles for Responsible Investment and the Financial Reporting Council's Stewardship Conde.

Proposal 1

The following proposal was moved by Councillor Watt (seconded by Councillor Burgess):

1) To note the paper;
2) To approve the updated Statement of Responsible Investment Principles (SRIP);
3) To note the following;
    a. Regarding section 2.4 of the LPF officers report - 'This paper expands on the fund's approach to engagement rather than indiscriminate divestment, an approach that has been reviewed regularly by the Pensions Committee and officers, who have always agreed that engagement is more responsible and potentially impactful' – that this has not been and is not the unanimous view of the Pensions committee;

b. Regarding section 2.5 of the LPF officers report - ‘Several times in the past, the Pensions Committee has considered the rationale for and against divestment/ inclusion and always concluded that exclusion of a whole sector would constrain the fund and potentially be a breach of the fiduciary duty owed to the members and employers, who fund the scheme. When it comes to investing or not investing in shares, they have supported analysis of financial returns on a case-by-case basis’ - that this has not been and is not the unanimous view of the Pensions committee;

4) To agree to amend the SRIP at page 7, “Deny debt, engage equity” as below;

While the trading of equities (shares) may not in itself affect the capital position of a company, subscribing to new bonds and new equity does provide companies with funding. Within our equity portfolio we engage with our holdings, and that engagement includes using the tools and strategies we have at our disposal to influence companies to commit to align with the goals of the Paris agreement. In our debt portfolios we aim to deny funding to those non-aligned companies. Where material risks remain following engagement activity, we retain the ability to divest.

Proposal 2

The following proposal was moved by Cllr Doggart (seconded by Richard Lamont):

1) To note the paper; and

2) To approve the updated Statement of Responsible Investment Principles (SRIP);

Voting

For Proposal 1 - 4 votes

For Proposal 2 - 3 votes

(For Proposal 1 – Councillors Burgess, Nicolson, Ross and Watt.

For Proposal 2 – John Anzani; Councillor Doggart and Richard Lamont)

Decision

To approve Proposal 1 by Councillor Watt as follows:

1) To note the paper;

2) To agree to approve the updated Statement of Responsible Investment Principles (SRIP);

3) To note the following;

a. Regarding section 2.4 of the LPF officers report - ‘This paper expands on the fund's approach to engagement rather than indiscriminate divestment, an approach that has been reviewed regularly by the Pensions Committee and officers, who have always agreed that engagement is more responsible and potentially impactful’ – that this has not been and is not the unanimous view of the Pensions committee;

b. Regarding section 2.5 of the LPF officers report - ‘Several times in the past, the Pensions Committee has considered the rationale for and against divestment/

inclusion and always concluded that exclusion of a whole sector would constrain the fund and potentially be a breach of the fiduciary duty owed to the members and employers, who fund the scheme. When it comes to investing or not investing in shares, they have supported analysis of financial returns on a case-by-case basis' - that this has not been and is not the unanimous view of the Pensions committee;

4) To agree to amend the SRIP at page 7, "Deny debt, engage equity" as below;

While the trading of equities (shares) may not in itself affect the capital position of a company, subscribing to new bonds and new equity does provide companies with funding. Within our equity portfolio we engage with our holdings, and that engagement includes using the tools and strategies we have at our disposal to influence companies to commit to align with the goals of the Paris agreement. In our debt portfolios we aim to deny funding to those non-aligned companies. Where material risks remain following engagement activity, we retain the ability to divest.

(Reference – report by the Chief Investment Officer, Lothian Pension Fund, submitted)

10.Holdings Report

The report provided a written in response to the request at the meeting of Pensions Committee on the 27 September 2023 for a detailed outline of all investment currently held by the Lothian Pension Fund in companies whose primary business is fossil fuels. It was outlined that officers have supported transparency by publishing all holdings on the Lothian Pension Funds website and have highlighted the broader context for the fund's investments.

Decision

1) To note the report; and

2) To agree that LPF officers provide a report to the committee on the progress being made towards, and the feasibility of, reducing current investments in fossil fuel companies and increasing investment in the transition to low-carbon energy and industry, including;

   a. the pros and cons for sustainability of fund income over the short to long-term

   b. a potential outline plan and timeline for achieving this goal

(Reference – report by the Chief Investment Officer, Lothian Pension Fund, submitted)

(References – Pensions Committee 27 September 2023 (item 14); report by the Chief Investment Officer, Lothian Pension Fund, submitted)

11.Risk & Compliance Update

An overview of the monitoring and assurance undertaken by Lothian Pension Fund since the last meeting along with material observations and exceptions was provided. The report also provided a summary of the ongoing work to enhance current risk management arrangements.

Decision

To note the report.

(Reference – report by the Chief Risk Officer, Lothian Pension Fund, submitted)

12.Additional Item – Valedictory Remarks

Members of the Pensions Committee took the opportunity to register thanks to Bruce Miller for his work with Lothian Pension Fund and his work with both the Pensions Committee and the Pensions Board.

Decision

To note the Committee's thanks to Bruce Miller for his work with Lothian Pension Fund and his work with both the Pensions Committee and the Pensions Board.

13.2023 Triennial Valuation Update

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the item of business on the grounds that it involved the disclosure of exempt information as defined in Paragraphs 1 and 6 of Schedule 7(A) of the Act.

Decision

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

(Reference – report by the Chief Finance Officer, Lothian Pension Fund, submitted)

14.Additional Item – Update on Legal advice being sought on behalf of the Pensions Committee

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

Decision

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

by virtue of paragraph(s) 1, 3, 6 of Part 1 of Schedule 7A
of the Local Government(Scotland) Act 1973.

Document is Restricted

This page is intentionally left blank

Pensions Committee Minutes

2pm, Wednesday 27 September 2023

Present:

Councillors Watt (Convener), Burgess, Doggart, Nicolson and Neil Ross; John Anzani and Richard Lamont.

Pension Board Members present:

Jim Anderson, Tony Beecher, Thomas Carr-Pollock, Nick Chapman, Sharon Dalli, Tom Howorth, Darren May, and Alan Williamson.

Other Attendees:

Andy McKinnell (Independent Professional Observer).

Apologies: Brian Robertson, Pension Board Member.

1. Quorum

The Clerk confirmed that notice of the meeting had been given and that a quorum was present and the Convener declared the meeting open.

2. Order of Business

The Clerk advised there was no change to the order of business.

(a) Point of Order – Item 6.1 – Audit Sub-Committee Convener's Annual Update Report

The Convener of the Pensions Audit Sub-Committee raised a point of order in relation to Item 6.1 Audit Sub-Committee Convener's Annual Update report, noting that despite submission to officers, the report was not tabled on the agenda.

Decision

To note that officers would review the procedure for submitting papers to the Committee going forward.

(b) Point of Order – Item 6.3 - Project Forth Update

John Anzani raised a point of order in relation to Item 6.3 Project Forth Update highlighting that, in accordance with Standing Order 13.1 "a decision of the Committee cannot be changed by the

Committee within six months unless notice has been given of the proposed item in the summons for the meeting and the Convener rules there has been a material change of circumstances or the Committee agrees that the decision was based on erroneous, incorrect or incomplete information".

The Head of Democracy, Governance and Resilience, City of Edinburgh Council, advised that due notice of the item had been given in the meeting papers in terms of the Local Government (Access to Information) Act 1985 and explained the Convener's role around ruling a material change of circumstances

Decision

To note the advice provided.

(c) LAPF Investments Awards 2023

The Convener took the opportunity to congratulate the LPF Team on winning the LGPS Fund of the Year at the LAPF Investments Awards 2023.

3. Declaration of Interests

Item 9.3 – Councillor Doggart made a transparency statement as a Fellow of the Institute and Faculty of Actuaries.

John Anzani made a transparency statement in relation to his wife's role as a non-Executive Director on the Board of Enjoy Leisure East Lothian.

4. Minute

Decision

1) To approve the minute of the Pensions Committee of 21 June 2023 as a correct record.
2) To note that the training session on Hermes EOS referred to in item 9 of the minute had been rescheduled to be held in November 2023.

5. Referrals and Recommendations from the Pensions Audit Sub-Committee of 26 September 2023

By way of a verbal update, the Convener of the Pensions Audit Sub Committee praised the unqualified annual accounts and highlighted that there had been no material subsequent alterations. The Sub-Committee had then taken the opportunity to thank Hugh Dunn for his contribution as Service Director, Finance and Procurement, Andy McKinnell for his contribution as Independent Professional Observer and Lesley Birrell for her contribution as clerk to the Pensions Committee and the Pensions Audit Sub Committee. Further updates and recommendations would be made at the relevant agenda items.

Decision

To note the updates.

6. Agenda Planning and Governance Update

An overview of proposed reports for future Pensions Committee and Pensions Audit Sub-Committee meetings for December 2023 and March 2024 was presented. Committee members took the opportunity to thank Hugh Dunn for his contributions and then welcomed Richard Lloyd Bithell and Alison Murray to their respective positions.

Decision

1) To note the agenda planning document and the action tracker set out in appendix 2.

2) To note the recruitment of the new Independent Professional Observer subject to agreement regarding mutually acceptable terms and conditions for the provision of independent professional service for Lothian Pension Fund.

3) To note the LPF governance update regarding the changes in membership of the LPFE and LPFI Boards.

4) To note that the Pension Board members were invited to comment on agenda items during committee meetings.

5) To note there would be an actuarial valuation update paper presented to Committee in December.

6) To thank Hugh Dunn, Chair of LPFE and LPFI for his commitment and contribution to the work of the Fund and extended their best wishes for his retirement and to welcome Richard Lloyd-Bithell as the newly appointed Service Director, Finance and Procurement, City of Edinburgh Council.

7) To thank to Andy McKinnell, Independent Professional Observer for his commitment and contribution to the Fund and to welcome Alison Murray newly appointed into the IPO role.

8) To welcome Dr Deborah Smart, Executive Director of Corporate Services, City of Edinburgh Council as the newly appointed Chair of LPFE.

(Reference – report by the Chief Executive Officer, Lothian Pension Fund, submitted.)

7. Project Forth Update

The Convener ruled, in terms of Standing Order 13, that the following item was competent as a result of a material change of circumstances making reference to the information contained in the supplementary report submitted by the Chief Executive, City of Edinburgh Council and the verbal update from the Chief Executive, Lothian Pension Fund confirming that Falkirk Council Pension Fund no longer had the appetite to pursue Project Forth at this time and was working on the assumption that the Project would not go ahead.

An update in relation to the Project Forth Update report was provided, together with, a brief overview of the supplementary paper.

Proposal 1

The following proposal was moved by Councillor Watt:

1) To note, as requested at the June 2023 committee meeting, the provision of the paper originally prepared for the March Committee which set out the results of the updated and final evaluation of the proposed merger structures and the recommendations that had been anticipated at that time;

2) To support the recommendation as originally made in June 2023 to cease the project for the reasons given at that meeting noting that it had been communicated to the CEO of LPF that Falkirk were operating under the presumption that Project Forth would not be proceeding and did not anticipate revisiting a merger within the next couple of years; and

3) To note that officers may revisit the proposals when either circumstances or priorities change and, in any event, to review options in 2 years' time and subject to Falkirk Council Pension Fund being minded to re-engage at that time.

Proposal 2

The following proposal was moved by John Anzani:

To reject the recommendations set out in the report by the Chief Executive Officer, Lothian Pension Fund.

Voting

For Proposal 1	-	4 votes
For Proposal 2	-	1 vote
Abstentions	-	2

(For Proposal 1 – Councillors Burgess, Nicolson, Ross and Watt.

For Proposal 2 – John Anzani.

Abstentions – Councillor Doggart and Richard Lamont.)

Decision

To approve Proposal 1 by Councillor Watt as follows:

1) To note, as requested at the June 2023 committee meeting, the provision of the paper originally prepared for the March Committee which set out the results of the updated and final evaluation of the proposed merger structures and the recommendations that had been anticipated at that time.

2) To support the recommendation as originally made in June 2023 to cease the project for the reasons given at that meeting noting that it had been communicated to the CEO of LPF that Falkirk were operating under the presumption that Project Forth would not be proceeding and did not anticipate revisiting a merger within the next couple of years; and

3) To note that officers may revisit the proposals when either circumstances or priorities change and in any event to review options in 2 years' time and subject to Falkirk Council Pension Fund being minded to re-engage at that time.

(References – Pensions Committee 21 June 2023 (item 15); report by the Chief Executive Officer, Lothian Pension Fund and supplementary report by the Chief Executive, City of Edinburgh Council, submitted)

8. Updates to Investment Governance arrangements

Officers provided an update on changes being made to the terms of reference of the Joint Investment Strategy Panel as a result of the expansion of services provided by LPFI to Fife and Falkirk and the recent regulatory compliance review of LPFI.

As a result of these changes, references in the Statement of Investment Principles required to be updated in addition to other minor amendments to simplify and remove duplication.

The revised Statement of Investment Principles for Lothian Pension Fund and Scottish Homes Pension Fund was presented for approval.

Decision

1) To note the contents of the report as they related to documentation of roles and management of conflicts in relation to investment decision making.

2) To agree to adopt the revised Statement of Investment Principles.

(Reference – report by the Chief Executive Officer, Lothian Pension Fund, submitted)

9. Lothian Pension Fund - Contract Awards and Supplier Overview (Period 1 July 2022 to 30 June 2023)

Officers provided a brief overview of the report making reference to the contracts awarded by the Fund in the period between 1 July 2022 and 30 June 2023 and sought approval to waive the Council's Contract Standing Orders in connection with a further extension of certain high value contracts.

Decision

1) To note the report.

2) To approve the continuation of the appointment of the Fund's external investment managers for global equities, by way of waiver of the Contract Standing Orders for the period from 1 October 2023 as referred to in paragraph 4.5 of the report.

(References – Pensions Committee 22 March 2022 (item 18); report by the Chief Executive Officer, Lothian Pension Fund, submitted)

10. Audited Annual Report and Accounts of the Lothian Pension Fund and Scottish Homes Pension Fund

An overview and details of the Audited Annual Report and Accounts for the year ended 31 March 2023 for Lothian Pension Fund and Scottish Homes Pension Fund was presented to members by the Chief Finance Officer, Lothian Pension Fund and the Fund's external auditor, Nick Bennett from Azets Audit Services.

The external auditor presented the audit findings to members including the audit opinion, key findings on audit risks, audit adjustments and accounting systems and internal controls.

Members were pleased to note that an unqualified opinion had been provided on the financial statements and other prescribed matters for Lothian Pension Fund and Scottish Homes Pension Fund.

Key points within the Audit Report included confirmation that work had been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK and Ireland) and Ethical Standards.

Some minor disclosure and presentational adjustments had been identified during the audit and these had been reflected in the final set of financial statements as set out in appendix 2 of the report.

The Convener of the Pensions Audit Sub-Committee welcomed the unqualified accounts and commended the work of Azets as the Fund's external auditor.

Decision

1) To note the report by Azets Audit Services "Lothian Pension Funds 2022/23 Annual Audit Report to Members of the Pensions Committee and the Controller of Audit" set out in Appendix 1.

2) To approve the audited annual report for the year ended 31 March 2023 for the Lothian Pension Fund and the Scottish Homes Pension Fund set out in appendix 2.

3) To note that the audited financial statements for the year ended 31 March 2023 of both the wholly owned companies, LPFE Ltd and LPFI Ltd, had been approved by the respective Board of Directors in June 2023, set out in appendices 3 and 4.

4) To note the "Letter of Representation (ISA 580)" by the Chief Finance Officer, Lothian Pension Fund set out in appendix 5.

5) To record the Committee's thanks and appreciation to the LPF staff team and the external auditor for their work in preparing and finalising the annual accounts.

(Reference – report by the Chief Finance Officer, Lothian Pension Fund, submitted)

11. Stewardship Report

The Fund's Stewardship Report covering the period from 1 January 2022 to 31 March 2023 was presented in compliance with the UK Stewardship Code 2020. The report had been updated with new examples of the Fund's application of the principles by way of case studies and new voting and engagement data over the period.

Members took the opportunity to thank officers for the readability of the section of the report which referenced Environmental, Social and Governance.

Decision

To note the Stewardship Report.

(Reference – report by the Chief Investment Officer, Lothian Pension Fund, submitted)

12. Business Plan and Budget Update

An update in relation to the progress of the 2023-2024 Strategy and Business Plan, performance indicators and actions was provided.

In response to questions regarding the impact of the McCloud judgement, officers confirmed that following data gathering exercises they did not foresee a material difference to individual members' benefits. a.

Following questions in relation to the Convene committee management software program, officers confirmed that further training on the functionality of the system could be provided to members if required.

Decision

To note progress of the Fund against the 2023-24 Business Plan together with specific updates on:

- Performance indicators.
- Membership and cashflow monitoring.
- Capital injection into LPFI.

(Reference – report by the Chief Finance Officer, Lothian Pension Fund, submitted)

13. Risk & Compliance Update

An overview was provided of monitoring and assurance undertaken by Lothian Pension Fund noting any material observations or exceptions together with a summary of the ongoing work to enhance current risk management arrangements.

Introduction of the revised risk assessment methodology as well as a full review and validation of the risks and controls themselves had led to some changes in risk ratings as set out in appendices 1 and 2 of the report. There were currently 2 high rated risks – Regulatory Breach and Supplier Performance and Oversight, however the LPF management team were satisfied that the action plans established to address the noted weaknesses in both reviews would mitigate these risks.

In response to questions regarding Councillor Watt's role on the Scottish Local Government Pension Scheme Advisory Board, it was clarified that Councillor Watt sits as the COSLA representative on the Board and that the Chief Investment Officer, Lothian Pension Fund acts as the Fund's adviser to the Board.

Decision

1) To note LPF Group's risk register and quarterly update.

2) To note a review of the existing Group risk register had been undertaken and a revised risk register created.

3) To note the ongoing strategy and development around the Group's risk management framework.

4) To note the increase in capital request to LPFI Board to meet FCA regulatory capital requirements.

(Reference – report by the Chief Risk Officer, Lothian Pension Fund, submitted)

14. Motion by Councillor Burgess – Lothian Pension Fund Investments in Oil and Gas Companies

The following motion by Councillor Burgess was submitted in terms of Standing Order 11 and verbally adjusted:

"Committee:

1) Notes given the Climate Emergency and the fiduciary duty of pension funds that it is important for the Lothian Pension Fund to be clear about its investments in companies whose principal business is oil and gas.

2) Requests a report to the next committee meeting detailing all investments currently held by Lothian Pension Fund in companies whose principal business is in fossil fuels, for example BP, Shell, TotalEnergies, Exxon and Chevron."

3) Requests the report include information on changes to these investments in the last 3 years.

Decision

To approve the adjusted motion by Councillor Burgess.

15. Employer Covenant Review 2023

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, excluded the public from the meeting for the item of business on the grounds that it involved the disclosure of exempt information as defined in Paragraphs 1 and 6 of Schedule 7(A) of the Act.

A brief overview was provided of the recent employer covenant analysis undertaken by the Fund in preparation for the 2023 Actuarial Valuation.

Decision

1) To note the results of the employer covenant analysis for the Fund.

2) To note that such analysis would be reported to Committee on an annual basis.

(Reference – report by the Chief Finance Officer, Lothian Pension Fund, submitted)

16. Employers Participating in Lothian Pension Fund

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, was requested to exclude the public from the meeting for the item of business on the grounds that it involved the disclosure of exempt information as defined in Paragraphs 1 and 6 of Schedule 7(A) of the Act.

An overview of the Employers Participating in the Lothian Pension Fund was provided.

Decision

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

2) To note the progress made by Lothian Pension Fund in engaging with employers to recover cessation debts.

(Reference – report by the Chief Operating Officer, Lothian Pension Fund, submitted)

17. 2023 Triennial Valuation – High Level Indicative Results

The Committee, under Section 50(A)(4) of the Local Government (Scotland) Act 1973, was requested to exclude the public from the meeting for the item of business on the grounds that it involved the disclosure of exempt information as defined in Paragraphs 1 and 6 of Schedule 7(A) of the Act.

The initial high level results of the 2023 Triennial Valuation were presented. The valuation report explained the process, derivation of assumptions and analysis of change from the previous valuation.

Decision

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

1)

(Reference – report by the Chief Executive Officer, Lothian Pension Fund, submitted)

This page is intentionally left blank

by virtue of paragraph(s) 1, 6 of Part 1 of Schedule 7A
of the Local Government(Scotland) Act 1973.

Document is Restricted

This page is intentionally left blank

Pensions Committee
Action Log

Meeting	Type	Owner / Lead	Detail	Update	Completion date	Status
05/12/2024	Action	LPF Chief Investment Officer/LPF Chief People Officer	**Business Plan and Budget Update:** 1) officers circulate a briefing note to members in relation to possible options to address the concerns raised by the deputation. 2) Officers to provide a breakdown of employee engagement.	1) briefing note circulated to committee and board 2) breakdown of employee engagement will be provided before the March 2024 committee.	20/03/2024	Propose to close
05/12/2024	Action	CommServices/LPF Assistant Company Secretary	**Minute:** 1)Clarification sought for the Minute of the Pensions Committee 27 September 2023 subject to changes to the wording of Section 7 in relation to the decision taken by Falkirk Pension Fund with regard to the termination of Project Forth. 2)To note that the revised minute would be submitted to the next regular meeting,	1) amended minute tabled for consideration in March 2024 committee	20/03/2024	Propose to close
05/12/2024	Action	LPF Assistant Company Secretary	**Governance Update and Agenda Planning** 1) officers will submit a report in relation to training hours for members; 2) the action tracker appended to the Agenda Planning Update would be included as an item on future agendas	1) Action tracker submitted as separate item. 2) Training hours provided to all committee members and submitted for consideration as appendix 2 of the Governance Update.	20/03/2024	Propose to close
05/12/2023	Action	LPF Chief Investment Officer	**Holdings report** 1) LPF officers provide a report to committee on the progress being made towards, and the feasibility of, reducing current investments in fossil fuel companies and increasing investment in the transition to low-carbon energy and industry, including; the pros and cons for sustainability of fund income over the short to long-term and a potential outline plan and timeline for achieving this goal.	1) update will be provided at June 2024 committee.	26/06/2024	open
	Action	Convenor	1) An update to be provided to the Pensions Committee on the Pension Board request.	A verbal update by the Convenor will be provided at the Pensions Committee meeting in March 2024.	05/12/2024	open

This page is intentionally left blank

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Governance Update

Item number 6.1

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 note that the Pension Board members are invited to comment on agenda items during Committee meetings;

1.2 note the agenda planning document set out in Appendix 1 to this report;

1.3 note that the Pension Board Chair, Jim Anderson, steps down from the Pension Board at the end of March 2024, having made a significant contribution to Lothian Pension Fund and the Pension Board over the last 9 years;

1.4 note the Pension Board Chair arrangements from 1 April 2024 to 31 March 2025;

1.5 note the appointment process for the non-elected Pension Committee members;

1.6 note the update on members training hours and the development of training; and

1.7 note the expected introduction of the Pensions Regulator new general code with effect from 27 March 2024.

Kimberley Russell

Company Secretary, Lothian Pension Fund

Contact: Susan Handyside, Assistant Company Secretary, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Governance Update

2. Executive Summary

2.1 At its meeting in December 2023, the Pensions Committee requested that officers provide regular updates on governance matters, including compliance with the Nomination and Appointments and Training and Attendance Policies, as well as any other relevant matters arising, in addition to the usual agenda planner. This report seeks to provide that fuller update.

2.2 Work is underway to appoint new members for current and anticipated vacancies in the Pension Board and Pensions Committee.

2.3 All four Committee Members and eight Pension Board Members have met the training requirement. The remaining Committee Members have confirmed their intention to meet the requirement before the period end. Appendix 2 of the report provides detail of Committee and Board training hours undertaken over the year.

2.4 A gap analysis has commenced to assess LPF's compliance against the new The Pensions Regulator (TPR) code with the results and implications being reported to Committee in June.

2.5 Appendix 1 of the report provides the proposed agendas for future meetings of the Pensions Committee and Audit Sub Committee.

3. Background

3.1 Committee meetings are held on a quarterly basis and additionally as required; the Audit Sub Committee meetings are held at least three times a year.

3.2 To provide an overview of the content of those future meetings, and an awareness of the annual cycle of items, an agenda planning document is submitted each quarter. The content of the agenda planning document arises from several sources: (a) standing items for each meeting, (b) re-occurring items at a specific cadence (quarterly, annually, biennially, for example), and (c) ad hoc or stand-alone items, where those arise. The agenda planning document is maintained by LPF's Company Secretariat and governance team and presented as a standing item at each meeting for noting.

4. Main Report

Future Dates and Agenda Planning

4.1 The Committee meeting dates for 2024/25 are set out below and calendar invites have been issued. These meetings will be held in person with the option, if required, to attend virtually.

Pensions Committee	Audit Sub Committee
• Wednesday 26 June 2024 at 2pm	• Monday 24 June 2024 at 2pm
• Wednesday 25 September 2024 at 2pm	• Tuesday 24 September 2024 at 2pm
• Thursday 5 December 2024 at 2pm	• Tuesday 3 December 2024 at 2pm
• Wednesday 26 March 2025 at 2pm	• Tuesday 25 March 2025 at 2pm (provisional)
• Wednesday 25 June 2025 at 2pm	• Monday 23 June 2025 at 2pm

4.2 The proposed agendas for the June and September 2024 meetings are set out in the following tables, based on the usual Committee cycle plus any additional and intra-cycle requests. The current annual agenda planning document is set out in Appendix 1.

4.3 Specifically in respect of the Pension Committee, the agenda for June includes a paper on the approach to responsible investment. The Convenor of the Pension Committee shall provide an update at the Committee in March regarding the Pension Board review request.

4.4 In respect of the Audit Sub Committee, the agenda for June includes the two papers deferred from the December meeting. These were the AVC Review Update and a report regarding Global Custody Services Performance. While it had been reported that the former would be brought to the Audit Sub Committee in March, this has not been possible. A fuller update regarding the status of the AVC Review is provided in the Business Plan and Budget report, with a provisional hold for the AVC Review scheduled for the Audit Sub-Committee's meeting in June. The Global Custody Services Performance will be available for LPF to report in June.

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

June 2024

Pensions Committee	Audit Sub Committee
• Referrals / recommendations from Pensions Audit Sub Committee • Annual Report and Accounts of Lothian Pension Fund and Scottish Homes Pension Fund (unaudited) • Internal Audit Annual Report and Opinion • Statement of Investment Principles • Joint Investment Strategy Panel Activity • Annual Investment Update – Lothian Pension Fund • Annual Investment Update - Scottish Homes • Annual LPF Group Governance Update • Approach to Responsible Investment • Risk and Compliance Update	• Annual Report and Accounts of Lothian Pension Fund and Scottish Homes Pension Fund (unaudited) • Internal Audit Annual Report and Opinion • Internal Audit Update • AVC Review (provisional) Private agenda • Global Custody Services Performance • IT Information Security Update • Risk and Compliance Update

September 2024

Pensions Committee	Audit Sub Committee
• Audit Sub Committee Convenor's Annual Update, including any referrals / recommendations from Pensions Audit Sub Committee • Employer Covenant Review • Discretions Policy • Audited Annual Report and Accounts of the Lothian Pension Fund and Scottish Homes Pension Fund (including the Annual Audit Report and Opinion by the External Auditor) • Stewardship Report • Operating Plan and Budget Update • Contract Awards Update • Risk and Compliance Update Private agenda • Employers participating in the scheme	• Lothian Pension Fund Annual Report and Accounts (Audited) • Internal Audit Update including any key audit finding reports completed in the reporting period • Fraud Prevention Private agenda • Risk and Compliance Update

Rotation of the Pension Board Chair & Membership of the Pension Board

4.6 The current Pension Board Chair, Jim Anderson, steps down from the Pension Board at the end of March. Jim has been a dedicated member of the Pension Board since its inception in March 2015. This report wishes to formally note and record thanks and gratitude to Jim for his significant contribution to the Pension Board.

4.7 In respect of the position of Pension Board Chair, the Pension Board constitution states that 'the chair of the Pension Board will be rotated on an annual basis' (with provision for the Chair's tenure to be extended for one further year, subject to approvals). As Jim was drawn from the member representation, the 2024/25 Chair is, accordingly, required to be drawn from the employer membership of the Pension Board.

4.8 The Pension Board are scheduled to meet in advance of the March Pensions Committee. It is, therefore, expected that the Pensions Board shall provide a verbal update to the Committee regarding the Chair appointment for 2024/25.

4.9 More broadly, regarding Pension Board membership, a panel met to interview an applicant for an employer representative vacancy on Wednesday 6 March. In accordance with the Nomination and Appointments Policy ("Appointments Policy"), the panel comprised (a) the Chair of the Pension Board, (b) the Convenor of the Pensions Committee, (c) the Independent Professional Observer, and (d) Kimberley Russell (deputising for LPF's Chief Executive Officer). The panel unanimously supported the appointment, which is being taken forward in accordance with the Appointments Policy. A verbal update on the appointment shall be provided at the Committee for noting. It is worthy of note that a few minor amendments to the Appointments Policy may be useful for clarity, and will be proposed as part of the annual governance update in June.

4.10 The Pension Board constitution provides that it will comprise five employer members and five employee members. With the appointment noted at paragraph 4.9 and Jim's departure, the membership of the Pension Board, at the time of writing this report, is four employee representatives and four member representatives. Activity to fill vacancies, being one employer representative and, following Jim's departure, one member representative, drawn from the trade Union Unison membership continues.

Non-Elected Members of the Pensions Committee

4.11 As set out in the LPF Nominations and Appointments Policy, non-elected members of the Pension Committee can serve a maximum of three consecutive years before either standing down or submitting themselves as a candidate for further election. The current non-elected Pension Committee members will come to an end of their tenure the end of June. LPF commenced the recruitment and appointment process in February and details of the process was communicated to both Committee and Pension Board members at that time. A verbal update on progress will be made to the Committee at the meeting.

Training hours 2023/24 for the Pensions Committee and Pension Board

4.12 In accordance with the Fund's Training Policy the expected training hours for members of the Pensions Committee and Pension Board is a minimum of three days (21 hours), with the annual training cycle being 1 April to 31 March. The Pensions Regulator also requires those involved with the governance of local government pension schemes to develop and build sufficient knowledge to effectively carry out their role.

4.13 Appendix 2 provides a breakdown of training hours of the Pensions Committee and Pension Board notified and recorded by the Company Secretariat team.

4.14 At the time of writing this report all Pension Board members have either met or exceeded the training requirement. Four of the Pension Committee Members have met the requirement. It is expected that all Pensions Committee members will fully achieve the minimum training requirement by the end of March.

4.15 Committee and Pension Board members have recently been given access to LPF's the Learning Management (training) System (LMS) enabling members to view recorded training sessions. It is also expected that members shall have access to update their training hours directly via the system from 1 April 2024.

The TPR General Code

4.16 The Pensions Regulators new general code (Code) was laid before Parliament in January this year and expected to come into force on 27 March. Set to replace ten of The Pension Regulators current codes of practice into a series of modules (related to five themes: the governing body; funding and investment; administration; communications and disclosure; and reporting), work has commenced to review the Code to identify any potential gaps in existing policies and practices. The Committee shall be updated in June on the output of that analysis.

5. Financial impact

5.1 None.

6. Stakeholder/Regulatory Impact

6.1 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.

6.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report.

7. Background reading/external references

7.1 City of Edinburgh Council, Committee Terms of Reference (sections 13 and 24)

8. Appendices

Appendix 1 – LPF's Annual Agenda Planning Cycle
Appendix 2 – Training Log 2023/2024

This page is intentionally left blank

Appendix 1

Frequency	Pensions Committee	Audit Sub Committee
Every 3 years	**December or March**	
	Actuarial Valuation: LPF SHPF	N/A
	March	
	Funding Strategy Statement	N/A
Biennial	**September**	
	Pension Administration Strategy	N/A
	Administrating authority Discretions Policy. Next review due September 2024	N/A
Annually	**March**	
	LPF Strategy and Business Plan and Budget	N/A
	Annual Audit Plans (Internal and External)	*Draft internal audit plan will be developed in consultation with the Convenor of the Audit Sub Committee, the CEO (LPF) and, if appropriate, the Independent Professional Observer and circulated to the Audit Sub Committee members for comment.*
	Benchmarking – Investment and Administration Costs	N/A
	June	
	Annual Report and Accounts Lothian Pension Fund and Scottish Homes Pension Fund (Unaudited)	Annual Report and Accounts Lothian Pension Fund and Scottish Homes Pension Fund (Unaudited)
	LPF Internal Audit Annual Report and Opinion	LPF Internal Audit Annual Report and Opinion
	Statement of Investment Principles	N/A
	Joint Investment Forum Activity Update	N/A
	Annual Investment Updates - Lothian Pension Fund and Scottish Homes Pension Fund	N/A
	Annual LPF Group Governance Update	N/A

Frequency	Pensions Committee	Audit Sub Committee
	September Employer Covenant Review Audited Annual Report and Accounts of the Lothian Pension Fund and Scottish Homes Pension Fund (including the Annual Report and Opinion by the External Auditor) Stewardship Report N/A Lothian Pension Fund Contract Awards Report	N/A Audited Annual Report and Accounts of the Lothian Pension Fund and Scottish Homes Pension Fund (including the Annual Report and Opinion by the External Auditor) N/A Fraud Prevention N/A
	December Annual Report by External Auditor **(or September if available)** N/A Stewardship (including the statement of responsible investment principles) N/A N/A N/A	Annual Report by External Auditor **(or September if available)** Investment Income Review-Cross-Border Withholding Tax and EU Tax Recoveries N/A Pensions Data Quality Global Custody Services Performance Additional Voluntary Contributions (AVC) Review
Biannual	**March & September** Employers Participating in Lothian Pension Fund **June & December** N/A	N/A IT Information Security Update
3 Times per year	**March[1], September & December** Operating Plan and Budget Update	N/A

[1] The March update will have the dual purpose of a business strategy update, budget review and budget approval for the forthcoming financial year

Frequency	Pensions Committee	Audit Sub Committee
	June, September & December Referrals / recommendations from Pensions Audit-Sub	N/A
Quarterly	**March, June, September & December** Risk and Compliance Update N/A	Risk and Compliance Update (in-depth) Internal Audit Update
As required	Investment Strategy Reviews (at least every 3 years – next due June 2024)	N/A

This page is intentionally left blank

LPF INTERNAL DATA

LPF PUBLIC DATA

Committee and Pension Board Members' Training Record
From 1 April 2023 to 31 March 2024

Appendix 2

LOTHIAN PENSION FUND Event:	TPR online training	PLSA Investment Conference 2023	LPF Training	Audit Sub Committee	Pensions Committee	LPF Training	Audit Sub Committee	Pensions Committee	LGC Investment Seminar Scotland 2023	LPF Training - Valuation Session	LPF Training - Virtual Valuation session	LPF Training	Audit Sub Committee	Pensions Committee	Investment Training	PLSA Investment Conference 2024	LPF Training	Audit Sub Committee	Pensions Committee	Additional training/ reading	Total
Date	n/a	6-8 June	12/06/23	19/06/23	21/06/23	15/09/23	26/09/23	27/09/23	19-20 Oct	31/10/23	15/11/23	17/11/23	04/12/23	05/12/23	06/02/24	27-29 Feb	07/03/24	19/03/24	20/03/24	N/A	
Pensions Committee																					
Steve Burgess	0	3	2.5	N/A	1	0	N/A	1	0	3	1.5	3	N/A	1	3	0	3	N/A			22.00
Neil Ross	0	0	3	0.5	1	3	0.5	1	2	3	1.5	3	0.5	1	3	0	1				24.00
Phil Doggart	0	0	3	0.5	1	3	0.5	1	0	3	1.5	3	0.5	1	3	0	3				24.00
Mandy Watt	0	0	3	N/A	1	3	N/A	1	0	3	1.5	3	N/A	1	0	0	3	N/A			19.50
Vicky Nicolson	0	0	0	N/A	1	3	N/A	1	0	3	0	3	N/A	1	0	0	2.75	N/A			14.75
John Anzani	0	0	0	0.5	1	0	0.5	1	0	3	0	3	0.5	1	3	tbc	3			49.64	66.14
Richard Lamont	0	0	0	N/A	1	3	N/A	1	0	3	1.5	3	N/A	1	3	0	3	N/A		7.5	27.00
Lothian Pension Funds' Pension Board																					
Employer Representatives																					
Darren May, (Scottish Water)	0.5	0	3	N/A	1	0	N/A	1	7.5	2	0	3	N/A	1	3	0	0			6.25	28.25
Sharon Dalli (Police Scotland)	0	0	3	N/A	1	3	N/A	1	0	3	1.5	3	N/A	1	0	0	3			13	32.50
Alan Williamson (Edinburgh College)	0	0	3	N/A	1	0	N/A	1	9	0	0	3	N/A	1	3	0	1.25			7.5	29.75
Nick Chapman (Lothian Valuation Joint Board) (Left 22/06/2023)	0	0	3	0.5	1	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	n/a	N/A	N/A	N/A	N/A	2.5	7.00
Vacancy	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	0.00
Member Representatives																					
Brian Roberston (UNITE)	0	0	0	N/A	0	3	N/A	0	0	2.5	1.5	0	N/A	0	3	0	3			19	32.00
Jim Anderson (UNISON)	1	16.5	3	N/A	1	3	N/A	1	8	0	1.5	3	0.5	1	0	12	3			14.5	69.00
Tom Howorth (UNISON)	0	6	3	N/A	1	3	0.5	1	0	3	0	3	N/A	1	3	9	3			9	45.50
Thomas Carr Pollock (GMB)	1	0	0	N/A	1	3	N/A	1	6	3	1.5	0	N/A	0	3	5	3			3	30.50
Tony Beecher (UNITE)	2	0	3	N/A	1	3	N/A	1	0	0	0	0	N/A	1	0	0	3			13.11	27.11
Total	4.5	25.5	32.5	2	15	33	2	14	32.5	34.5	13.5	36	2	13	30	26	38	0	0	145	499.00

This page is intentionally left blank

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Funding Strategy Statement Update

Item number 6.3

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 note the summary of responses received as part of the consultation process; and

1.2 approve the revised Funding Strategy Statement.

Alan Sievewright

Chief Finance Officer, Lothian Pension Fund

Contact: Erin Savage, Senior Pensions Employer and Member Manager, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Funding Strategy Statement Update

2. Executive Summary

2.1 As required under the Local Government Pension Scheme (Scotland) Regulations, the Lothian Pension Funds' Funding Strategy Statement (FSS) has been reviewed as part of the actuarial valuation process to ensure that it remains appropriate. In revising the FSS, the fund has considered:

- Actuarial valuation results;
- Consultation feedback from fund employers;
- Guidance from Hymans Robertson, the Fund's actuary; and
- Regulatory amendments.

3. Background

3.1 The FSS is a policy document which summarises the approach to funding pension liabilities of Lothian Pension Fund and the Scottish Homes Pension Fund. Relevant policies are appended to the FSS for completeness, including:

- employer admission to the Fund;
- employers leaving the Fund;
- Setting employer contribution rates; and
- Salary strain mechanism.

3.2 The FSS is formulated under guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA), which states that the FSS must be reviewed formally at least every three years as part of the triennial valuation. The valuation sets employer contribution rates within the framework provided by the FSS. The FSS should also be reviewed if there are any material changes in the policy set out in the FSS.

3.3 The last review of the FSS was carried out in June 2023. At that time amendments were made to the salary strain mechanism following employer feedback.

3.4 A draft revised FSS was presented to Committee in December 2023. The changes proposed took account of indicative results of the 2023 valuation and changes made to funding policy as a result. Following Committee approval of the revised draft FSS, an employer consultation exercise was carried out.

3.5 In February 2024, the Local Government Pension Scheme (Scotland) (Amendment) Regulations 2024 were laid before the Scottish Parliament. These amendments come into force on 28 March 2024, and the FSS has been revised in anticipation of these amendments.

3.6 The revised FSS, which has been reviewed by the Fund actuary (Hymans Robertson), is attached as Appendix 1 to this report.

4. Main Report

Actuarial Valuation of the Pension Funds

4.1 As separately reported to Committee on this agenda, the Fund actuary carried out a valuation of the Funds as at 31 March 2023. These valuations are required under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2018, and the Actuary has prepared the reports in line with required Technical Actuarial Standards.

4.2 The valuation reports contain rates and adjustments certificates setting out employer contribution rates for the 3 years from 1 April 2024. The valuation must be completed before the first anniversary of the valuation date, ie by 31 March 2024. In setting contribution rates, the Actuary must have regard to the FSS and the actuary will certify these rates following Committee approval of the FSS.

Employer Consultation

4.3 A draft revised FSS was presented to Committee for approval in December 2023. As required under the Local Government Pension Scheme (Scotland) Regulations 2018, employers must be consulted on changes being made to the FSS. The draft revised FSS was issued to employers in December 2023. Employers were invited to comment on during the consultation period which ran from 11 December 2023 to 31 January 2024.

4.4 A summary of the comments received from employers, together with responses to these comments is attached at Appendix 2. The summary will be circulated to all employers via the next Employer Bulletin. As set out in Appendix 2, no changes to the FSS are being made as a result of this feedback.

The Local Government Pension Scheme (Scotland) (Amendment) Regulations 2024

4.5 In February 2024, the Local Government Pension Scheme (Scotland) (Amendment) Regulations 2024 were laid before the Scottish Parliament. These amendments include amendments and clarifications relating to employers considering exiting the Fund and the FSS has been revised in anticipation of these amendments.

4.6 The FSS was revised in 2022 to introduce the ability for employers to request an indicative exit valuation which would remain valid for 90 days. Previously, employers looking to exit were at the risk of adverse market movements between the time they received an indicative exit valuation and the date of exit. The 2024 amendments clarify that the 90 days is from the date used in the indicative valuation. In addition, a further condition regarding the provision of exit valuations has been introduced, namely that they will not be provided if the employer has requested an indicative exit valuation within the previous 12 months.

4.7 Section 7.11 of the FSS ('Employers Leaving the Fund') has been amended to highlight this latter change. Further, for completeness wording has been added to confirm that when such valuations are carried out, up-to-date membership data will be used. This approach, as opposed to 'rolling forward' membership data from the last triennial valuation, means that liabilities will be valued more accurately and will therefore reduce risk to the Fund and employer.

Review by Fund actuary, Hymans Robertson

4.8 The draft revised FSS was shared with the Fund actuary who reviewed and provided comments for consideration. In the main, comments related to clarification of certain points for ease of reading, however Committee may wish to note the following key amendments:

- References to the suspension of the Contribution Stability Mechanism have been amended to confirm that it previously covered the period to 31 March 2024 to prevent confusion.
- The table in Section 7.6 (Employer Time Horizons') has been amended to confirm time horizons for specific employers.
- Section 2.3 ('Principles for determining payment') of the Bulk Transfer policy (Appendix B) has been amended to confirm that transfer terms will be negotiated by the relevant actuaries and that if agreement cannot be reached for any reason, an independent third actuary will be consulted.
- In Appendix E ('Calculation of Employer Contributions'), the table setting out how the methodology will be applied to individual employers has been amended to ensure that all employers are included. In addition, the Actuary has also provided another version of the table showing the calibration of the Economic Scenario Service as at 31 March 2023. The revised table shows annualised returns for 10, 20 and 40 years compared to 5,10 and 20 years in the previous version.
- The salary strain mechanism does not apply to employers which are part of the contribution stability mechanism. In addition, the salary strain monitoring only relates to benefits built up in the scheme before 1 April 2015. Such benefits are final salary benefits and therefore salary increases have a direct impact on the member's benefits on retirement.

5. Financial impact

5.1 The funding strategy is intended to ensure that the Fund has sufficient assets in the long term to meet is liabilities.

6. Stakeholder/Regulatory Impact

6.1 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.

6.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report.

7. Background reading/external references

7.1 None.

8. Appendices

Appendix 1: Draft revised Funding Strategy Statement.
Appendix 2: Funding Strategy Statement – response to employer comments

This page is intentionally left blank

LOTHIAN
PENSION FUND

Funding Strategy Statement

LOTHIAN PENSION FUND

CONTENTS

1. Introduction	**3**
1.1 Maintenance	
1.2 Availability	
2. Purpose of the Funding Strategy Statement	**4**
2.1 Regulatory Framework	
3. Aims and Purpose of the Fund	**6**
3.1 Aims of the Fund	
3.2 Purpose of the Fund	
4. Responsibilities of the Key Parties	**7**
4.1 The Administering Authority	
4.2 The Individual Employers	
4.3 The Fund Actuary	
5. General Funding and Solvency Issues	**9**
5.1 Funding Principles	
5.2 Solvency	
5.3 Long term cost efficiency	
5.4 Financial Assumptions & Link to Investment Strategies	
5.5 Demographic Assumptions	
5.6 Contributions	
6. Funding – Scottish Homes Pension Fund	**13**
7. Funding – Lothian Pension Fund	**14**
7.1 Objectives of Lothian Pension Fund's Funding Strategy	
7.2 Investment Strategy	
7.3 Employer Asset Tracking	
7.4 Setting Employer Contribution rates	
7.5 Contribution Stability	
7.6 Deficit/Surplus Spreading	
7.7 Admission Bodies – Affordability constraints	
7.8 Post Valuation Adjustments	
7.9 Employers Joining the Fund	
7.10 Employers leaving the Fund	
7.11 Bulk Transfers	
8. Key Risks and Controls	**22**

Appendix A – Admission Policy
Appendix B – Bulk Transfer Policy
Appendix C – Policy on Employers leaving the Fund
Appendix D – Charging policy
Appendix E - Calculation of Employer contributions
Appendix F – Salary Strain Recharging Mechanism

1. INTRODUCTION

This is the Funding Strategy Statement (FSS) of Lothian Pension Fund ("the Fund"). It has been prepared and maintained by the City of Edinburgh Council, in its capacity as the Administering Authority of the Fund, in consultation with the Fund's Actuary and following a period of consultation with participating employers.

The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues.

This FSS is produced in accordance with the Chartered Institute of Public Finance & Accountancy (CIPFA) revised statutory guidance "Preparing and maintaining a funding strategy statement in the Local Government Pension Scheme (LGPS) 2016", which affirms the FSS as being a key part of a pension fund's risk management framework.

This statement was approved by the Pensions Committee on 20 March 2024 and is effective from 21 March 2024. It replaces all previous Funding Strategy Statements and policies on funding.

1.1 Maintenance

The Administering Authority will review the FSS every three years in conjunction with actuarial valuations or more frequently if considered appropriate.

1.2 Availability

This document is available on the Fund's website (www.lpf.org.uk).

2. PURPOSE OF THE FUNDING STRATEGY STATEMENT

CIPFA's 'Preparing and maintaining a funding strategy statement in the Local Government Pension Scheme 2016' states that the purpose of the FSS 'is best defined by reference to the discussion paper issued by the Office of the Deputy Prime Minister (ODPM) on 23 July 2003, 'Local Government Pension Scheme – Strategy Proposals: Stocktake Discussion Paper – Funding Strategy Statement Proposals' ', namely:

1. to establish a clear and transparent fund-specific strategy that will identify how employers' pension liabilities are best met going forward;
2. supports the desirability of maintaining as nearly constant a primary contribution rate as possible; and
3. takes a prudent longer-term view of funding those liabilities.

These objectives are desirable individually - but may be mutually conflicting.

The FSS shall also ensure that the regulatory requirements to set contributions to ensure the solvency and long-term cost efficiency of the Fund, as defined by the Public Service Pensions Act 2013, are met.

The statement and appendices set out how the Administering Authority balances the potentially conflicting aims of affordability of contributions, transparency of process, stability of employers' contributions, and prudence in the funding basis. Specific clarity is provided as to the Fund's policies in respect of:

1. employers being admitted to the Fund;
2. employers leaving the Fund (exits);
3. bulk transfers; and
4. the charging for services and recovery of costs incurred.

2.1 Regulatory Framework

Pension benefits accrued by members of the Fund are determined by statute.

The contributions paid by the members of the Fund are fixed in the Scheme Regulations (defined below). Employers pay the balance of the cost of delivering the benefits, however, in line with the requirements of the Public Service Pensions Act 2013, the Scheme Regulations incorporate a cost sharing mechanism to ensure sustainability of the Scheme over the long term.

The FSS focuses on the pace at which employers pay for the benefits i.e. the approach used to determine contribution rates. It forms part of a framework that includes:

- the Local Government Pension Scheme) (Scotland) Regulations 2018 (as amended), the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015 and the LGPS (Management and Investment of Funds) (Scotland) Regulations 2010 (the 'Scheme Regulations');
- the Pensions Committee, the Pensions Audit Sub-Committee and the Pension Board;

- the Rates and Adjustments Certificate, which can be found appended to the Fund Actuary's valuation report;
- actuarial factors for valuing early retirement costs and the cost of buying extra service; and
- the Fund's Annual Report, including the Annual Governance Statement, the Governance Compliance Statement and the Statement of Investment Principles.

This is the framework within which the Fund's Actuary carries out triennial valuations to set employers' contributions and provides recommendations to the Administering Authority when other funding decisions are required, such as when employers join or leave the Fund.

3. AIMS AND PURPOSE OF THE FUND

3.1 Aims of the Fund

The aims of the Fund are to:

- manage employers' liabilities effectively and ensure that sufficient resources are available to meet all liabilities as they fall due;
- seek returns on investment within reasonable risk parameters; and
- enable primary contribution rates to be kept as nearly constant as possible and (subject to the Administering Authority not taking undue risks) at reasonable cost to scheduled and admitted bodies, whilst achieving and maintaining fund solvency and long-term cost efficiency. This should be assessed taking appropriate cognisance of the risk profile of the fund and employers and the risk appetite of the administering authority and employers alike.

3.2 Purpose of the Fund

The Fund provides benefits to members and their dependants. In this regard, the purpose of the Fund is to:

- receive monies in respect of contributions, transfer payments and investment income and recover costs and charges, pay pension benefits, transfer values and administration costs, charges and expenses; and
- make investments to meet the future costs of pension promises made to members of the Scheme.

LOTHIAN PENSION FUND

4. AIMS AND RESPONSIBILITIES OF THE KEY PARTIES

The sound and effective management of the Fund can only be achieved if all interested parties exercise their statutory responsibilities conscientiously. Although a number of these parties, including investment managers and external auditors, have a responsibility to the Fund, the following may be considered of particular relevance to the funding strategy:

4.1 The Administering Authority should:

- operate the Fund as per the Scheme Regulations;
- collect and account for employer and employee contributions, investment income and other amounts due to the Fund as stipulated in the Scheme Regulations;
- invest surplus monies in accordance with the Regulations;
- ensure that sufficient cash is available to meet liabilities as and when they fall due;
- pay relevant benefits from the Fund as set out in the Scheme Regulations;
- manage the actuarial valuation process in consultation with the Fund's Actuary, including providing all required data and employer covenant analysis;
- prepare and maintain a Funding Strategy Statement and Statement~~;~~ of Investment Principles after proper consultation with interested parties;
- monitor all aspects of the Fund's performance and funding, and amend the Funding Strategy Statement/Statement of Investment Principles accordingly;
- take measures as set out in the Scheme Regulations to safeguard the Fund against the consequences of employer default;
- effectively manage any potential conflicts of interest arising from its dual role as both Fund administrator and scheme employer;
- manage any exit valuation in consultation with the Fund's Actuary;
- prepare and maintain admission, exit, bulk-transfer and charging policies, copies of which are included in this document,
- enable the Pension Board to review the valuation process as set out in their Constitution; and
- fulfil all other duties as specified in Lothian Pension Fund's Pensions Administration Strategy – available in the 'Publications' section of the Fund's website www.lpf.org.uk

4.2 The individual Employers should:

- calculate an employee's contribution rate and deduct the correct contributions from members' salaries;
- pay employee and employer contributions to the Administering Authority on a timely basis and provide appropriate supporting documentation in a format and timescale specified by the Fund;
- develop and maintain a policy where discretion can be exercised within the regulatory framework (e.g. granting enhanced benefits) bearing in mind costs;
- make additional contributions, in accordance with agreed arrangements, for example, award of additional pension and early retirement strain costs;
- notify the Administering Authority promptly of organisation changes for example, changes in ownership or structure, TUPE transfers which could affect future funding;
- notify the Administering Authority of a possible ending of its admission agreement/participation in the Fund within the terms of that agreement or otherwise as required by the Scheme Regulations (typically a 3 month notice period is required), including closed employers where the last employee member is leaving (whether due to retirement, death or otherwise leaving employment);

- pay any exit payments due on ceasing participation in the Fund in line with provisions set out in the Fund's Policy on employers leaving the Fund (see Appendix C);
- meet costs as specified in the Charging Policy (see Appendix D); and
- fulfil all other duties as specified in the Fund's Pensions Administration Strategy. This includes provision of all data required for effective administration and record-keeping, and payment of any charges levied by the Fund following poor performance by the employer.
- participate in annual covenant reviews carried out by the Fund, the results of which will be shared with the employer's guarantor or aligned body as appropriate.

4.3 The Fund Actuary should:

- prepare actuarial valuations to assess the solvency of the Fund and the required employers' contribution rates;
- engage with the Administering Authority in consultation processes;
- prepare advice and calculations in connection with bulk transfers and the funding aspects of individual benefit related matters such as pension strain costs, ill-health retirement costs, compensatory added years costs, etc.;
- provide advice and valuations on the on the exit of employers from the Fund;
- provide advice to the Administering Authority as required on bonds or other forms of security against the financial effect on the fund of employer default;
- assist the Administering Authority in assessing whether employer contributions need to be revised between valuations as required by the Scheme Regulations; and
- ensure that the Administering Authority is aware of any professional guidance or other professional requirements that may be of relevance to his or her role in advising the Fund.

5. GENERAL FUNDING AND SOLVENCY ISSUES

5.1 Funding Principles

The cost of the benefits is not known in advance. The approach to funding determines the pace at which employers pay for the benefits and the ways in which the Fund ensures that it will have enough money to pay the benefits due to its members.

5.2 Solvency

The notes to the Public Service Pensions Act 2013 state that solvency means that the rate of employer contributions should be set at "such level as to ensure that the scheme's liabilities can be met as they arise".

It is not regarded that this means that the pension fund should be 100% funded at all times. Rather, and for the purposes of Section 13 of the Public Service Pensions Act 2013, the rate of employer contributions shall be deemed to have been set at an appropriate level to ensure solvency if they are set to target a funding level (assets divided by liabilities) for the whole fund of 100% over appropriate time periods and using appropriate actuarial assumptions.

If the conditions above are met, then it is expected that the Fund will be able to pay scheme benefits as they fall due.

The Fund's Actuary is required to report on the solvency of the Funds and recommend future employer contribution rates every three years. In assessing the solvency and employer contribution rates, the Actuary must make a number of financial and demographic assumptions (see below). The solvency of the Funds and the contribution rates can be very sensitive to these assumptions.

In calculating solvency, the Actuary values the benefits using the assumptions described below. Assets are taken into account at their market value.

The Scheme Regulations specify the principles which must be used in the funding strategies. However, it is the responsibility of the Administering Authority, acting on the advice of the Fund's Actuary, to determine the precise approach and the financial and demographic assumptions to be used in the actuarial valuation.

The principal issues facing the solvency of the Funds include the ability to finance liabilities as and when they arise, the rate or volatility in the rate of contribution paid by the employers, the pace at which deficits are recovered (or surpluses used up) and the returns on the Fund's investments.

The Fund carries out annual employer covenant reviews to gather a range of key financial and non-financial information. This includes a request for details of funding sources and for annual financial statements to be provided. In addition, membership numbers are regularly reviewed to monitor membership maturity. The results of the covenant review are used to rank employers on risk level, with details being provided to the Fund's Actuary to inform the actuarial valuation.

As required under Section 13(4)(c) of the Public Service Pensions Act, The Scottish Public Pensions Agency has appointed the Government Actuary's Department to report on whether the rate of employer contributions to the Fund is set at an appropriate level to ensure the solvency of the Fund and the long-term cost efficiency of the Scottish Local Government Pension Scheme, so far as relating to the Fund. Such reports must be made following each triennial valuation of the Fund.

When developing this Funding Strategy, the Administering Authority has had regard to the review under Section 13(4)(c).

5.3 Long term cost efficiency

The notes to the Public Service Pensions Act 2013 state "Long-term cost-efficiency implies that the rate must not be set at a level that gives rise to additional costs. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the time".

The rate of employer contributions shall be deemed to have been set at an appropriate level to ensure long-term cost efficiency if the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual, with an appropriate adjustment to that rate for any surplus or deficit in the Fund.

In assessing whether the above condition is met, the review under Section 13(4)(c) may have regard to the following considerations:

- the implied average deficit recovery period
- the investment return required to achieve full funding over different periods, e.g. the recovery period
- if there is no deficit, the extent to which contributions payable are likely to lead to a deficit arising in the future
- the extent to which the required investment return is less than the administering authority's view of the expected future return being targeted by a fund's investment strategy, taking into account changes in maturity/strategy as appropriate.

5.4 Financial Assumptions and link to investment strategies

The key financial assumption in calculating the solvency and contribution rates is the rate of return which will be achieved on the Funds' investments. 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 (resulting from the investment strategy). To the extent that investment returns may be lower than expected, then higher contributions may be required from employers, and vice versa. Hence, the funding and investment strategy are inextricably linked.

The discount rate(s) adopted in the actuarial valuation is derived by considering the expected rate of investment return which is anticipated to be achieved by the underlying investment strategy.

The Funds invest in assets other than gilts in order to reduce the cost to the employers in the long term, subject to the alignment to the expected duration and admission basis of the individual employer's membership. However, the investments are not guaranteed to deliver returns in excess of gilts. This means that the funding level can be volatile, particularly in the short term. In order to minimise the degree of short-term change in employer contribution rates, expected investment returns are considered over the long term.

The Pensions Committee is responsible for setting investment strategies after taking professional investment advice.

A formal review of the Funds' investment strategies is undertaken at least every three years to ensure appropriate alignment with liabilities. This is typically after the results of the triennial Actuarial Valuation are known. Guidance for the Pensions Committee on investment strategy is provided by a Joint Investment Strategy Panel (JISP), working in collaboration with the Falkirk Council Pension Fund and Fife Council Pension Fund.

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

The JISP is comprised of senior fund officers from the three pension funds plus external investment advisers.

The JISP meets quarterly to monitor the risk, return and implementation of the investment strategy, and to discuss current issues, including asset allocation. This involves an appraisal of the current investment market opportunities and risks and the distribution of the Funds' investments across different assets, countries, sectors and companies to ensure that overall risk is being managed appropriately.

Further information on the investment strategies can be found in the Funds' Statement of Investment Principles which is available on the Fund's website (www.lpf.org.uk).

5.5 Demographic Assumptions

The Actuary makes a number of demographic assumptions including mortality, salary growth, rates of retirement, commutation experience and withdrawal. They are intended to be best estimates of the future experience of the Funds.

The assumptions take into account the past experience of the employer and Funds, other Local Government Pension Schemes and/or the general population, as considered appropriate by the Actuary.

5.6 Contributions

Employee contributions are determined by the Local Government Pension Scheme (Scotland) Regulations 2018. A member's contribution rate is calculated by the employer on an annual basis, dependent on their actual pensionable pay at 1 April each year and allowing for any election made under Regulation 10 (50:50 option).

Employer contributions are calculated by the Fund Actuary. They are made up of two elements:

A: the **primary** rate of the employers' contribution. This is the contribution rate required to meet the cost of the future accrual of benefits expressed as a percentage of pensionable pay ignoring any past service surplus or deficit but allowing for any employer specific circumstances, such as the membership profile of that employer, the funding strategy adopted for that employer, the actuarial method chosen and/or the employer's covenant, and,

B: the **secondary** rate of the employers' contribution. This is an adjustment to the primary rate to arrive at the rate each employer is required to pay. In broad terms, payment of the Secondary rate is in respect of benefits already accrued at the valuation date. The time horizon over which an employer is asked to target full funding is covered further in Sections 6 and 7 below.

For employers open to new entrants, secondary contributions are expressed as a percentage of payroll.

For employers closed to new entrants, secondary contributions, where positive, are typically expressed as a fixed monetary sum, rather than as a percentage of payroll. Any fixed monetary deficit contributions should be paid in equal monthly instalments along with the primary rate contributions, or by prior arrangement as a one-off lump sum at the start of the year.

For any employer, the rate they are required to pay is the sum of the primary and secondary rates.

The Fund operates a salary strain recharging mechanism to recoup any funding strain associated with salary increases above expectations. Further detail of this mechanism is detailed in Appendix F.

The rates for all employers are shown in the Fund's Rates and Adjustments Certificate, which forms part of the formal Actuarial Valuation Report. The contributions stated are minimum amounts – employers can pay more than this. The Actuary will take account of any higher amounts paid at subsequent valuations.

All employers are required to pay the estimated additional cost (strain cost) of **non-ill health early retirements**, to allow for the fact that the pension is paid earlier and for longer. This is calculated at the time of the early retirement. The Fund's general policy is that strain costs are payable as a one-off payment at the time of the early retirement, however, at the Fund's discretion, alternative arrangements may be permitted if the early retirement occurs at the time of exit, depending on the employer's circumstances.

The Administering Authority monitors the actual contributions received to ensure they are in line with those expected. As set out in the Fund's Pensions Administration Strategy, employers are expected to provide requisite detailed information on a monthly basis to assist this monitoring exercise and to substantiate the payments made.

6. FUNDING – SCOTTISH HOMES PENSION FUND

Scottish Government acts as guarantor to the Scottish Homes Pension Fund. A bespoke funding strategy has been developed for the Scottish Homes Pension Fund. This has been agreed by the Administering Authority, the Fund's Actuary and the Scottish Government (previously known as the Scottish Executive).

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 is closed to new members and the liabilities will mature over the time, the investment strategy is designed to reflect the expressed requirements of the Scottish Government, namely low risk, with investments now exclusively bonds.

7. FUNDING – LOTHIAN PENSION FUND

7.1 Objectives of the Lothian Pension Fund's Funding Strategy

The objectives of the funding strategy include:

- 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.

7.2 Investment Strategy

The Fund has put in place four investment strategies for differing employer risk profiles.

<u>Primary Strategy</u>

This strategy 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.

This strategy applies to the following types of employers:

- Large employers with enduring membership which are open to new entrants (including but not limited to Councils and other statutory bodies);
- All other employers which are open to new entrants and have 5 or more active members;
- Transferee Admitted Bodies;
- Employers admitted to the Fund following a transfer of staff from another Fund employer; *
- Employers which have exited the Fund and their guarantor/aligned body agrees that assets can be moved to the primary strategy in order to maximise investment returns; and
- Any employer which has provided the Fund with requisite and sufficient legal security over assets

*the question of whether an employer was admitted following a transfer of staff from another Fund employer shall be determined at the Fund's discretion, provided that the ceding employer may dispute such determination should there be any ambiguity or uncertainty relating to historic transfers of staff. In such scenarios, the ceding employer shall be required to present the rationale and sufficient evidence to satisfy the Fund that the employer should not be treated as a Transferee Admitted Body for funding purposes.

Employers invested in the Primary Strategy will have individual contribution rates certified by the Actuary.

Any employer who does not admit any new entrants within a reasonable period is deemed to be closed to new entrants. For the purposes of this statement, a reasonable period is an inter-valuation period (i.e. three years between formal valuations of the Fund). Where an employer is deemed closed, they will move to the Medium Risk strategy or Lower Risk strategy as appropriate. Any employer classed as deemed closed which takes on new staff who join the Fund will revert to the Primary strategy with immediate effect.

Lower Risk Strategy
This strategy adopts a lower-risk approach for employers which have a short expected duration in the Fund and invests in index-linked government bonds to reduce the degree of short-term change in funding level and employer contribution rates in the period prior to the employer leaving the Fund and hence manage risks for both the individual employer and for the Fund as a whole.

This strategy was first introduced with effect from 1 April 2015.

This strategy applies to the following types of employers:

- Employers who have left the Fund (excluding bodies which may be aligned);
- Employers which are closed to new entrants and:
    - Have fewer than five active members and/or
    - Average membership age of 55 or higher.

Such employers will have individual contribution rates certified by the Actuary.

Medium Risk Strategy
This strategy adopts a balanced investment strategy reflecting the maturing membership and liability profile of the relevant employers. It is intended to act as a transition between the Primary Strategy and the Lower Risk Strategy, for those employers which are closed to new entrants. Accordingly, investments will be targeted to represent 50% allocation from the Primary Strategy and the Lower Risk Strategy. This will serve to reduce the degree of change in employer contribution rates which would result from moving immediately from the Primary Strategy to the Lower Risk Strategy. This strategy was first introduced with effect from 1 April 2018.

This strategy applies to the following types of employers:

- Employers which are closed to new entrants but do not meet the criteria for the lower-risk strategy.

Such employers will have individual contribution rates certified by the Actuary.

Lothian Buses
A bespoke strategy is in place for Lothian Buses. Lothian Buses closed to new entrants in 2008 and this strategy reflects the maturity of the membership, the liability profile and the existence of a shareholders' guarantee.

Allocation to strategies
An employer will change to an alternative investment strategy with immediate effect between valuations in the following situations:

- An employer closing to new entrants will move to the medium-risk or lower-risk strategy as appropriate;
- An employer that is part of the medium risk strategy which falls below five active members, will move to the lower-risk strategy.

In these circumstances, the Actuary will provide revised employer contribution rates.

Where an employer has closed to new entrants, it will not be able to reverse this decision and offer membership to new staff without the agreement of the Administering Authority and where applicable, the body acting as guarantor.

The Fund may consider a request for an employer to be assigned to an alternative investment strategy to that which strict application of the criteria would indicate, but only in circumstances where a higher risk strategy is supported by an explicit guarantor and/or where the Fund would not consider such to represent a scenario of greater risk exposure to other employer(s). The Fund may also consider a request to be assigned to an alternative (higher risk) investment strategy should provision of satisfactory security over assets be offered.

It is not practical for the Fund to offer individual employers full flexibility on asset allocation.

7.3 Employer Asset Tracking

The Lothian Pension Fund is a multi-employer fund. ~~Previously, individual employer asset shares have been calculated triennially at formal valuations by the Fund's Actuary using an analysis of surplus technique and tracked between valuations using a cash flow or roll forward approach. However, i~~In order to enhance the transparency, accuracy and auditability of individual employer asset allocations and reduce any cross-subsidy between participating employers, from 1 April 2014 the Fund introduced an employer asset tracking system based on cash flows. This is a form of unitisation of investments, where each investment or disinvestment of monies involves the purchase or selling of units in the Fund. By sub-dividing the assets into units, the Fund can more easily and accurately track each individual employer's assets. Changes in the value of the underlying assets are reflected by changes in unit prices.

Such unitisation therefore provides an efficient way of accurately apportioning assets to individual employers by allowing for employer cash flows and investment returns achieved by the Fund. In addition, this provides a mechanism for facilitating and managing a range of investment strategies within the single Fund to meet the needs of employers with different maturity profiles, funding levels or investment objectives.

7.4 Setting employer contribution rates

All employers in the Fund are required to fund the benefits of their own employees; therefore, the Actuary calculates a different contribution rate specific to each employer.

The Actuary uses a three-step process to calculate employer contribution rates which requires Fund and the Actuary to consider the following factors for each employer:

1. The employer's **funding target**, which is based on a set of ongoing assumptions about the future (e.g. investment returns, inflation, pensioners' life expectancies). If an employer is approaching the end of its participation in the Fund then its funding target may be set on a more prudent basis, so that its liabilities are less likely to be spread among other employers after its cessation.

2. The **time horizon** required over which the funding target is achieved. Employers may be given a lower time horizon if they are closed to new entrants, or do not have tax-raising powers to increase contributions if investment returns under-perform.

3. The **likelihood of achieving** the funding target over that time horizon will be dependent on the Fund's view of the strength of employer covenant and its funding profile. Where an employer is considered to have weaker financial strength then the required likelihood will be set higher, which in turn will increase the required contributions (and vice versa).

A risk-based approach is used to set employer contribution rates. This risk-based approach allows for thousands of possible future economic scenarios when assessing the likelihood of contributions being sufficient to meet both the accrued and future liabilities over a given time horizon for each employer.

Changes in employer contributions may be phased over time in order to minimise the degree of short-term change and enhance affordability. The Administering Authority, in consultation with the Fund's Actuary decides how any reductions or increases to contribution rates are introduced, taking into account specific employer circumstances.
Further information on calculating employer contribution rates is set out in Appendix E.

7.5 Contribution Stability

The general policy of the Fund is to operate a Contribution Stability Mechanism on an ongoing basis, subject to regular reviews, in order to provide certainty of pension contributions to Fund employers for future years, together with ensuring appropriate assurance of funding level to the Fund. Access to the Contribution Stability Mechanism will not be offered to all employers – each employer's particular circumstances will be considered, in particular the strength of the covenant offered and the extent of membership commitment to the Fund. Employers are not obliged to participate in the Contribution Stability Mechanism, but if they wish to opt out, they must make an election at the outset. This election will cover the entire duration of the Contribution Stability Mechanism as well as future reviews of the Contribution Stability Mechanism. Any decision to allow an employer to join the Contribution Stability Mechanism at a later date will be at the discretion of the Administering Authority.

An employer which chooses not to participate will instead pay the risk-based contribution rate as set by the Fund Actuary at the actuarial valuation.

Employers which are open to new entrants and have contribution rates calculated based on their individual circumstances will be offered access to the Contribution Stability Mechanism subject to:

- satisfactory assessment of the employer covenant; and
- agreement by their guarantor to inclusion of the employer in the Contribution Stability Mechanism (where appropriate).

An employer's participation in the Contribution Stability Mechanism is expected to extend to the full duration of the mechanism. However, access to the Contribution Stability Mechanism will be subject to ongoing review by the Fund which reserves the right to remove an employer from the Contribution Stability Mechanism should particular circumstances deem it prudent to do so, for example assessment of employer covenant, financial or demographic experience. In addition, if an employer closes to new entrants they will be removed from the Contribution Stability Mechanism and a recalculation of their contribution rate may be required.

Access to the Contribution Stability Mechanism will not be afforded to the following employers:

- Employers which are closed to new entrants;
- Transferee Admission Bodies; and
- Small Community Admission Bodies without a guarantor.

Full information on the Contribution Stability Mechanism is available on the Fund's website.

A contribution stability mechanism operated between 2013 and 31 March 2023. From 1 April 2024, the contribution stability mechanism will be suspended for a period of three years and is expected to be reintroduced following the 2026 actuarial valuation. A review will be carried out in 2025 in order to establish how the stabilisation mechanism will operate following the 2026 valuation.

Commented [DV1]: Probably need to retain some mention 2the CSM operated between 2013 and 2023. It was suspended at the 2023 valuation and is expected to be reintroduced prior to 2026". You have the second part. Think the first is necessary

The Fund will aim to keep contribution rates for stabilised employers within agreed parameters, however, there may be specific circumstances relevant to an employer which will merit the Actuary certifying a rate outside these parameters. Each case will be reviewed at the Fund's discretion.

7.6 Employer time horizons

In deciding the period over which any funding deficit or surplus is spread, the Administering Authority considers a number of factors including the objective of minimising the degree of short-term change in employer contribution rates and employers' ability to meet their commitments to the Fund.

The time horizons used for different employers range from 20 years for Councils, to the remaining contract period for Transferee Admission Bodies which can in some cases be a matter of months. The differences in time horizons reflect the financial strength of the employers and the perceived long-term commitment to the Fund.

The following table shows the employers in the Fund for which are required to fund the benefits of their own employees, setting out the key characteristics of each type of employer which influence the period over which any surplus/deficit has been spread.

Where an employer can offer security over assets or otherwise improve their covenant, the Fund may, at its discretion, allow a longer time horizon to be used.

	Employer	Time Horizon (Years)
Councils/Large Scheduled bodies	City of Edinburgh Council	20
	Midlothian Council	
	West Lothian Council	
	East Lothian Council	
	Scottish Fire & Rescue Service (Civilians)	
	Scottish Police Authority	
	Lothian Valuation Joint Board	
	Scottish Water	
	Visit Scotland	15
Universities / Colleges	Heriot-Watt University	15
	Newbattle Abbey College	
	Queen Margaret University College	
	Napier University	
	Edinburgh College	
	West Lothian College	
	Scottish Rural University College	FWL [1]
	University of Edinburgh	
	Edinburgh Leisure	15
	Enjoy East Lothian Lothian Buses LPFE Scottish Futures Trust West Lothian Leisure	20 ~~(TBC)~~
Other ~~T~~transferee Admission Bodies	Transferee Admission Bodies not named above	Shorter of FWL [1] or contract period
Employers open to new entrants	Scheduled bodies and open Community Admission Bodies not named above	15
Employers closed to new entrants	Closed Community Admission Bodies not named above	FWL [1]

[1] Future Working Lifetime of current active members or duration in Fund if shorter

7.7 Admission bodies – affordability constraints

As noted in section 5.6 above, the Fund Actuary certifies minimum contributions which each employer is required to pay. In circumstances where an employer's membership of the Fund is not mandated by Regulations and that employer is unable to meet the minimum certified contributions, then its membership will be terminated, with notice period of three months being applied by the Fund.

At each valuation, therefore, every employer will require to confirm its commitment to meet the certified minimum contributions. If an employer fails to provide such confirmation, following the notice period as specified above, the Administering Authority will terminate the admission agreement, and Appendix C: "Policy on employers leaving the Fund" will apply. Specifically, the Fund will arrange for an exit valuation to be carried out to assess the level of the employer's liabilities. The Fund will then engage with the employer in relation to the payment of any exit debt due to the Fund, determined in accordance with the Scheme Regulations.

7.8 Post Valuation adjustments

When determining future employer contributions at the triennial actuarial valuation the Administering Authority may (after consultation with the Fund Actuary) take into account any events that arise after the valuation date, but before the formal valuation report is signed off (which must occur within one year of the valuation date), that materially affect the employer contributions referred to above. In doing so, the Fund will aim to minimise the degree of short-term change in employer contribution rates while still ensuring the long-term solvency of the overall Fund.

The contribution rates are subject to review and change if there are changes in employer circumstances between actuarial valuations, for example, if an employer has closed to new members or has left the Fund. In the latter case, any residual liability may impact upon the rate(s) payable by employer(s) remaining in the Fund. In all instances, any such changes would be determined by the Administering Authority and require certification by the Fund Actuary.

7.9 Review of Employer Contribution Rates

The Fund may review employer contribution rates between actuarial valuations in the following circumstances:

- It is likely that the amount of liabilities arising or likely to arise relating to an employer has changed significantly since the last valuation;
- There has been a significant change in the employer covenant, as assessed in the annual employer covenant review; or
- The employer has requested a review of the contribution rate.

Where such a review is carried out the Fund will consult the affected employer(s) and the actuary in order to provide revised rates.

7.10 Employers joining the Fund

Appendix A sets out in full the Fund's policy on employers joining the Fund.

Bodies applying to join the Fund will be provided with a copy of this Statement and will be required to provide a written undertaking that they understand and are aware of the long-term financial implications of participation in the Fund prior to their admission.

7.11 Employers leaving the Fund

Appendix C sets out in full the Fund's policy on employers leaving the Fund in any of the following circumstances:

- When the employer is wound up or liquidated;
- When the last active member leaves or retires from an employer;
- When the admission agreement is otherwise terminated by either the employer or the Administering Authority, subject to the notice period specified in the admission agreement;
- In the case of Transferee Admission Bodies, when the contract comes to an end and is not renewed; and
- In the case of scheduled bodies, when the body no longer has an active member contributing to the Fund or through changes in over-riding legislation or Government policy can no longer contribute to the Local Government Pension Scheme.

Where an employer's admission agreement remains in full force and effect, but the employer has no active members and no new members will join in the future, then the admission agreement will be terminated. The actions detailed in Appendix C will apply, other than where specific provision exists in the admission agreement for such circumstances.

In order to make an informed decision, an employer considering exiting the fund may request an indicative exit valuation. The fund will arrange for indicative exit valuations to be provided unless the employer has requested an indicative exit valuation within the previous 12 months. Indicative exit valuations will be carried out using up-to-date membership data to ensure that liabilities are valued accurately.

7.12 Bulk Transfers

The treatment of bulk transfers of pension rights to and from the Fund are detailed in Appendix B.

LOTHIAN PENSION FUND

8. KEY RISKS AND CONTROLS

The Administering Authority has an active risk-management programme in place. The risk register is reviewed on an ongoing basis by the Risk Management Group, with a quarterly summary provided to the Pensions and Audit Sub-Committees. The following extract from the risk register, with Impact and Probability for each risk scored on a scale of 1-5, highlights those risks which can be considered of particular relevance to the funding strategy:

Risk Register as at December 2023

Risk Description	Existing controls	Impact	Probability	Current Risk
Investment returns are less than expected due to fall in fair price of securities including equities, bonds, real assets could impact value of the fund and consequently funding levels and liabilities	• Investment management oversight model including reviews, policy statements and quantitative analysis. • Formal review of strategy and investment assumptions as part of triennial valuation. • Asset liability studies. • Quarterly performance and funding level assessment by Joint Investment Strategy Panel. • Bespoke investment strategy offered to eligible employers.	3	3	
Failure of an employer with a deficit, or failure to pay required contributions or failure to fulfil a funding agreement on cessation may lead to the balance to be met by higher contributions from remaining employers	• Admissions Policy, including use of guarantees. • Regular contact with employers. • Education to improve understanding, including grant funding implications. • Annual employer covenant review, and quarterly membership monitoring. • Funding Strategy Statement includes alignment of higher-risk employers to Councils as appropriate. • Funding agreements in place for payment of cessation debt and security sought where appropriate. • Affordability confirmation built into Funding Strategy Statement.	3	3	

LOTHIAN PENSION FUND

	• Staff reminded of late reporting procedures regarding late payments to enable prompt action from the fund. • Additional employer covenant analysis and engagement in response to COVID-19 carried out with updates to be provided to all four Councils regarding aligned bodies.			
Unexpected drop in funding levels may require higher employer contributions which may be unaffordable to employers.	• Triennial valuation process. • Contribution stability mechanism and testing. • Funding Strategy Statement. • Investment strategy and monitoring.	2	3	
Insufficient funds and liquid assets to meet liabilities or capital requirements which may arise through contribution payment failure by employers, unexpected employer exits, shortfalls in expected investment income, unexpected investment calls and failure and delays of creditors and receivables.	• Quarterly review of financial performance highlights financial position of fund and subsidiaries by Financial Controller and Chief Financial Officer. This will highlight current cash position of the fund. • Regular review of cash position by Financial Controller also highlights if significant deterioration of operating account. • Action is then taken by Financial Controller to recall funds from Treasury activities.	2	3	
Investment Strategy does not deliver investment objective due to incorrect implementation, investments falling outside agreed risk parameters or inadequate Joint Investment Strategy Governance. This could lead to a fall in funding	• Joint investment panel with other Local Government Pension Scheme funds meets quarterly and provides advice and input on strategy. • Independent advisers in place on joint panel. • Front office systems pre- and post-trade monitoring in place to ensure implementation in line with strategy. Exceptions reported to investment team and monitored by investment committees and Joint Investment Strategy panel. • All trades placed follow approval rules before being placed. • Second line compliance checks are undertaken to review and escalate alerts when investments are outside agreed parameters.	2	2	

level.	LOTHIAN PENSION FUND			
Lothian Pension Fund don't adequately address Environmental, Social and Corporate Governance factors within the company, with service providers and through underlying investments due to lack of climate or sustainability strategy. This could lead to missed opportunities, regulatory scrutiny, financial loss and reputational or stakeholder challenge.	• Statement of Responsible Investment Principles updated annually. • Regular review of Scottish Local Government Pensions Scheme Advisory Board advice on fiduciary duties. • Pension Committee training on Responsible Investing and climate change risks. • Joint Investment Strategy Panel reviews climate-centred risks and opportunities at least annually. • Adherence to the UK Stewardship Code 2020 requirements.	3	3	

APPENDIX A: ADMISSION POLICY

1. Background

The Local Government Pension Scheme (LGPS) (Scotland) Regulations 2018 contain powers for the City of Edinburgh Council (acting in its separate capacity as administering authority) of the Lothian Pension Fund (LPF) to admit bodies into the Fund. Those bodies must meet certain conditions (generally relating to their purpose and aims), contained in the Scheme Regulations before being considered for admission.

This document sets out the policy of LPF in applying discretion to admit, on application, a new body into the fund for the purposes of allowing employees of that body access to the LGPS.

This policy will be reviewed as and when considered necessary.

2.General application of discretion to admit new bodies

LPF's Pensions Committee, as the executive body responsible for the administering authority function, delegates power to approve or reject applications to the Chief Executive Officer of Lothian Pension Fund.

LPF will consider all applications from bodies who meet the conditions of the Scheme Regulations. In making its decision, the Fund will carry out covenant analysis of all prospective new employers and due weight will be given to its relative merit.

Approved applications will be subject to the conclusion of an admission agreement containing the appropriate matters prescribed in Scheme Regulations. Appropriate legal advice will be obtained in drafting and concluding admission agreements.

The body will be provided with a copy of LPF's current Funding Strategy Statement and will be required to provide a written confirmation that they understand and are aware of the long-term financial implications of participation in the Fund.

A bi-annual report will be submitted to the Pensions Committee providing details of the delegated decisions made during the year.

3.Policy in relation to bodies admitted following the transfer of services from a Scheme Employer (TABs)

Part 1 of Schedule 2 of the Scheme Regulations lists a number of scheme employers. Certain employers may be admitted to the Fund following the transfer of services to that body, subject to the conclusion of an admission agreement between LPF, the scheme employer (where different) and the TAB. The scheme employer will also be required to act as a guarantor and undertake to meet any amounts due to the Fund in respect of any funding or contribution shortfall either during the period of their participation in the scheme or upon termination of the admission agreement.

4.Policy in relation to other admission bodies

The body applying to be admitted into the Fund must provide documentary evidence of their:

1. aims and objectives;
2. articles of association;

3. latest annual accounts; and
4. future income streams including the source and timing.

The body will be expected to find a guarantor who will undertake to meet any amounts due to the Fund in respect of any funding or contribution shortfall either during the period of their participation in the scheme or upon the termination of the admission agreement. The body must supply documentary evidence of the guarantee obtained and, where considered necessary by LPF, of the financial security of the guarantor.

LPF will try to recover any funding or contribution shortfall from the admission body in the first instance, before seeking any recovery from the guarantor.

APPENDIX B: BULK TRANSFER POLICY

1. Background

This is the policy of Lothian Pension Fund as regards the treatment of bulk transfers of pension rights to and from the Fund.

The purpose of bulk transfer negotiations is to determine the amount of service credits to be awarded and transfer payment to be paid when a number of members transfer their benefits from one pension scheme or LGPS fund to another.

1.1. Regulatory Framework

The Local Government Pension Scheme (Scotland) Regulations 2018 outline the general framework for employees and employers participating in the Local Government Pension Scheme in Scotland.

1.2 Reviews of Policy

This policy will be reviewed at least every three years following triennial valuations or following changes in the Scheme Regulations pertaining to employees transferring rights.

It should be noted that this statement is not exhaustive and individual circumstances may be taken into consideration where appropriate.

2. Principles

2.1. Over-riding Principles

Each bulk transfer will be dealt with on a case-by-case basis, however, in general the principles below will be applied.

Transfers Out

On transfers out to other LGPS Funds or other schemes, it is the Fund's general policy that:

- If the transfer out will result in the employer having no remaining active members, the bulk transfer amount should not leave the Fund (and the specific employer concerned) with insufficient assets to meet the remaining members' liabilities assessed on the appropriate exit basis as outlined in the Fund's 'Policy on employers leaving the Fund';
- For all other cases, unless otherwise agreed, the transfer amount will be set equal to the value of the benefits accrued to the transfer date for transferring members on the Fund's ongoing valuation basis, adjusted to take account of any underfunding in the transferring employer's share of the Fund, such that the maximum transfer value is not greater than the reserves held for the transferring members. This is known as a 'share of deficit' approach and is subject to a cap equal to 100% of the value of the transferring benefits.

Transfers in

In the event of a transfer in, the Fund's Actuary will be instructed to agree transfer terms with the transferring scheme's (or fund's) Actuary. For transfers in from a funded scheme (or another LGPS Fund), the Fund's Actuary will be instructed to agree terms where the minimum transfer amount from the transferring scheme is calculated on a 'share of deficit' basis. This approach is consistent to the calculation of the transfer amount if there was a transfer out of the Fund.

If the proposed transfer amount will result in a significant deterioration in the funding level of the receiving employer (due to, for example, the transferring scheme having a poor funding position), the Fund Actuary may be instructed to seek a higher transfer amount. If the transfer is from an unfunded scheme, the transfer will be subject to the Club Transfer rules. ~~Fund Actuary will be instructed to ensure the transfer value is equal to the value of transferring benefits based on the Fund's ongoing valuation basis.~~

If a bulk transfer in results in a deterioration of the receiving employer's funding level, the receiving employer will be required to make good the shortfall. The Fund's general policy is that the employer will be required to restore the funding level to the position immediately prior to the transfer. The employer will be required to repay the required top-up as a lump sum, or where the Fund considers the employer's covenant to be sufficiently strong, over an agreed recovery period or through the ongoing contribution rate (subject to the Fund's discretion).

The Fund reserves the right to refuse to accept a transfer in should the receiving employer's covenant be weak.

Transfer terms for both bulk transfers-in and transfers-out will be negotiated by the relevant actuaries, and if agreement cannot be reached for any reason, an independent third actuary will be consulted.

Intra-fund transfers

On transfers from one Fund employer to another existing Fund employer, assets equal to 100% of the transferring liabilities will be transferred, unless otherwise agreed.

On transfer from one Fund employer to a new Fund employer, the following principles will apply:

1. A fully funded transfer, on the ongoing valuation basis, if the new employer is a TAB, unless otherwise agreed.
2. A share of deficit transfer, on the ongoing valuation basis for all other types of employer, unless otherwise agreed.

Direction Orders

The Scheme Regulations specify the appropriate pension fund to which certain Scheme employers should belong. However, provisions exist to allow the Scottish Ministers to issue a direction order substituting a different Fund from that which is specified within the Scheme Regulations.

In these situations, the Fund will require the following assurances from the scheme employer before agreeing to a transfer under a direction order:

When liabilities are transferred into the Fund:

- Before agreement to the transfer can be provided, the employer must provide sufficient assurance to the Fund's satisfaction;
- Where applicable, the employer's guarantor/aligned body must agree to the transfer;
- In situations where the transfer will result in a deterioration of the employer's funding level, the employer must undertake to make such additional contributions to make good the shortfall. The level of contributions required, and the period of time over which these will be

LOTHIAN PENSION FUND

paid will be determined by the Fund in consultation with the Actuary; and
- The ceding fund must provide assurance that membership data meets the Pension Regulator's common and conditional standards. This will ensure that liabilities transferred are correct.

Where liabilities are transferred out of the Fund:

1. Where all the employer's liabilities are transferred out, all of the employer's assets will be transferred, such that the transferring employer has no remaining assets or liabilities in the Fund.
2. Where all of the employer's active members are being transferred out, but the liabilities relating to deferred and pensioner members remain with the Fund, the employer must ensure that the remaining liabilities are fully funded on the exit basis. The Fund will not recognise a Direction Order unless this condition is met.

2.2 Interaction with funding policy

It is the Fund's policy that each employer is responsible for the funding of all fund benefits of its own members, including current and previous employees. For the purpose of triennial funding valuations, the individual funding position for each employer is tracked by the Actuary at each valuation.

Any transfer of pension rights may have an effect on the valuation position of the employer and as noted above, a revised employer contribution rate may be required depending on the impact of the transfer on the employer's funding position and membership profile.

2.3 Principles for determining payment

The Fund will determine the transfer payment and service credits having taken actuarial advice.

The assumptions used to calculate transfer values out of the Fund will be based on those adopted for the latest formal valuation of the Fund updated for financial conditions on the date of transfer.

Transfers in should equally be updated to reflect financial conditions on the transfer date.

There is normally a lag between the date of the actual transfer of staff and the date of payment. During this period, on transfers out, the agreed transfer value will be adjusted by a factor as determined during initial negotiation of the bulk transfer terms.~~by an estimate of the movement in the investments as determined by the asset allocation of the Fund and the respective market indices.~~

This method of rolling up the transfer payment is to be recommended for incoming bulk transfers as well.

3. Process

3.1. Responsibilities of ceding/receiving employers

An employer which is aware of a transfer from or into the Fund is required to:

- advise the Fund, in writing, of the transfer. This communication should indicate where members are transferring to/from and how many members will potentially transfer;
- provide information and data as requested by the Administering Authority and the Fund's Actuary which is relevant, including in particular any changes to the membership which could affect the liabilities (e.g. salary increases and early retirements), contact details for the ceding/receiving scheme, etc.; and
- assist in the administration of option forms to transferring members as and when required.

3.2. Responsibilities of the Administering Authority

The Administering Authority will gather information as required, including, but not limited to, the following:

- details of the transfer – where are members transferring to/from, how many members are involved and (where a transfer out to a non-LGPS scheme) if the receiving scheme is broadly comparable to the LGPS;
- complete membership data for the transferring members;
- commission the Fund's Actuary to carry out bulk transfer negotiations where necessary;
- where applicable, liaise with the employer and ensure they are aware of their responsibilities, in particular for any residual deficit or risk associated with the transfer; and
- ensure that payments or receipts of transfer value payments are carried out on the agreed dates.

3.3. Responsibilities of the Actuary

Following commission of bulk transfer negotiations by the Administering Authority, the Fund Actuary will:

- on notification of the transfer, ensure that the data and information required is collated;
- propose/agree assumptions and transfer values based on the policies set out by the Fund;
- propose/agree service credits in line with relevant legislation and policies; and
- negotiate and agree the final transfer payment date and amount.

APPENDIX C: POLICY ON EMPLOYERS LEAVING THE FUND

1. Introduction

This is the policy of Lothian Pension Fund as regards the treatment of employers leaving the Fund.

This policy replaces all previous policies on employer termination and is effective from 29 September 2022.

1.1 Scope of Policy

This policy covers employers leaving the Fund in any of the following circumstances:

- when the employing authority is wound up or liquidated;
- when the last active member leaves or retires from an employer;
- when the admission agreement is otherwise terminated by either the employing authority or the admission authority, subject to the notice period specified in the admission agreement;
- in the case of Transferee Admission Bodies, when the contract comes to an end and is not renewed; and
- in the case of scheduled bodies, when the body no longer has an active member contributing to the Fund or, changes in over-riding legislation or Government policy determine that employees can no longer contribute to the Local Government Pension Scheme;

1.2 Reviews of Policy

This policy will be reviewed at least every three years following triennial valuations or following changes in the Scheme Regulations relevant to employers leaving the Fund.

2. Principles

2.1. Overriding Principles

If an employer leaves the Fund, or their admission agreement is otherwise terminated, the Administering Authority will instruct the Fund's Actuary to carry out a valuation of that employer's liabilities (an 'exit valuation').

Payment of any deficit does not guarantee that the assets in the Fund will be sufficient for the liabilities in the future: the actual cost of benefits will only be known after the last dependant dies and there is a risk that the amount estimated in the exit valuation does not cover the actual cost of the liabilities. In this situation, the Fund would seek recourse from the body which acted as guarantor to the employer, or alternatively the body which the employer was aligned.

The basis used to carry out such a valuation will depend on the circumstances of the change. The Fund's general policy is that the valuation will be carried out on a more prudent basis than that used in the ongoing actuarial valuation. However, the Fund may take into account the covenant strength of any successor body and/or guarantor which may be in place after the exit date.

The employer, successor body and/or guarantor may be required to pay additional contribution(s) or capital payments to the Fund

In normal circumstances, the Actuary will use the following assumptions for the exit valuation:

- A discount rate equivalent to the gilt yield at the date of the exit, with no allowance for outperformance of investments;
- An increase in the liabilities by 3% reflecting anticipated additional future improvements to life expectancies (over and above the ongoing valuation assumption); and
- Other assumptions would be consistent with the most recent actuarial valuation.

However, where the employer leaving the Fund is a Transferee Admission Body or an employer admitted to the Fund following a transfer of staff from another Fund employer the actuarial basis used will adopt a discount rate that is consistent with the basis used to assess the employer's opening assets and liabilities when the employer joined the Fund (updated for market conditions). On joining the Fund, Transferee Admission Bodies are set up on a fully funded basis with contribution rates calculated based on the duration of the contract in order to reduce the likelihood of a deficit arising on exit.

The Actuary may include an additional level of prudence when carrying out the exit valuation to take into consideration the McCloud judgement which found that the transition protections put in place when new public sector schemes were introduced were discriminatory. As a result, the benefit structure of the LGPS is being reviewed. Until clarity on a remedy is available, a loading factor may be applied to exit valuations.

If an employer becomes insolvent and it, or its guarantor, is unable to meet any deficit, additional contributions will be required from each remaining employer in the Fund, in proportion to their liabilities. This means that the majority of any deficit will fall on the large employers. However, where it has been established that there is a specific alignment to one or more other employers, then the pension liability will be assigned or apportioned accordingly to those other employer(s).

In the event of a Transferee Admission Body leaving the Fund and being unable to pay additional contributions to the Fund, the employer granting the contract will be liable for the additional contributions or capital payments.

The purpose of an exit valuation is to determine the level of any surplus or deficit in an employer's share of the Fund as at the date the employer leaves the Fund. Unless the cost of doing so is deemed to outweigh the likely recovery to the Fund, the Fund will pursue an outgoing body (including the liquidator, receiver, administrator or successor body if appropriate) for any deficit. The Fund will also pursue the guarantor for payment, where appropriate.

It is the Fund's policy that the determination of any surplus or deficit on termination should aim to minimise, as far as is practicable, the risk that the remaining, unconnected employers in the Fund have to make contributions in future towards meeting the past service liabilities of current and former employees of employers leaving the Fund.

LOTHIAN
PENSION FUND

2.2 Principles for Determining Payment of Exit Debt

The Administering Authority will determine the deficit/surplus attributable to the employer on exit having taken actuarial advice.

Where an exit valuation identifies that an employer is in surplus, this surplus will be returned to the employer in accordance with the Scheme Regulations.

If it is determined that there is a deficit and the employer will be required to make a payment to the Fund, the administering authority will advise the employer of the amount required. The Fund's general policy is for any deficit on exit to be recovered through a single lump sum payment to the Fund.

The Fund may, at its discretion issue a suspension notice to an employer leaving the Fund, suspending the employer's liability to make an exit payment. In such cases, the employer must continue to make contributions to the Fund at a level agreed by the Fund and the Fund Actuary. The suspension notice will specify the period during which the suspension notice is to apply. However, the fund may, at its discretion withdraw a suspension notice prior to the expiry of the suspension period. Once the suspension period has come to an end, or the fund has withdrawn the suspension notice, a further exit valuation will be carried out based on the relevant market conditions, asset values and updated membership data at that time.

In exceptional circumstances, and where it considers that this does not pose a material risk to the solvency of the Fund, the Fund may consider:

- allowing payment of any exit debt over longer terms rather than insisting on payment as a one-off payment or over shorter terms previously agreed;
- foregoing interest on such longer-term debt;
- agreeing repayment of an amount less than the exit debt in order to avoid the employer's 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 a legal agreement to address future improvements in the employer's financial circumstances. The Fund may take into account the covenant strength of the employer (including the availability of security in respect of the exit debt) and any successor body and/or guarantor which may be in place after the exit date. Interest at a rate advised by the Actuary may be applied to determine the appropriate payments to be made to the Fund.

The Fund may, at its discretion, enter into a written agreement with an exiting employer for that employer to defer their obligation to make an exit payment and to instead continue to make contributions at the secondary rate (a deferred debt agreement). Such agreements require a review of contributions every three years (ie in line with the triennial valuation of the Fund). The Fund will only consider a deferred debt agreement in situations where:

- the exiting employer has a strong financial covenant sufficient to meet the contributions during the term of the agreement and also any residual exit liability at the end of the agreement; and
- the exiting employer is willing to offer the fund suitable protection against the risk of future investment downturn or any other factors which may negatively impact the final exit valuation at the end of the agreement. As such, this may require the fund to be granted security over

the employer's assets; and
- a deferred debt agreement offers a better solution for the relevant employer than a debt spreading agreement as outlined above.

Adopting such principles would protect the interests of the Fund as a whole.

APPENDIX D: CHARGING POLICY

This is the policy of Lothian Pension Fund as regards meeting the cost of actuarial fees and other service costs which are recharged to employers. It covers the main circumstances where fees are payable but is not exhaustive.

The Fund will obtain the consent of the employer or member before carrying out any work which is likely to lead to fees being recharged.

1. Costs recharged to scheme members

The costs of general pension administration are not recharged to members of the Fund. However, costs associated with complex pieces of work, as well as costs of providing certain other confirmation may be recharged. This includes (but is not limited to) the following:

- costs associated with providing valuations under the Family Law (Scotland) Act 1985;
- costs of implementing pension sharing orders;
- costs of providing further cash equivalent transfer values where this information has already been provided once in the last twelve months; and
- costs of appointments with the Fund's independent medical advisers where appointments have been repeatedly missed without good reason, or where habitual requests for assessment are received without new medical evidence.

Details of the costs payable can be found on the Fund's website (www.lpf.org.uk). These costs will increase annually each April by CPI over the 12 months to the previous September.

2. Costs recharged to scheme employers

Employers should always contact the Fund in the first instance to establish whether fees will be recharged for any administration process or obtaining professional advice, and to obtain an estimate of likely fees.

Actuarial charges will be met by the Fund where the work is common to all or most employers, or where the work is required by the Scheme regulations and the employer has no choice whether or not the work is carried out.

However, where work is carried out or advice obtained at the request of a single or small number of employers, is not required by other employers, and is not a requirement of the Scheme Regulations, then the charges for that work or advice are generally recharged to the employer(s) concerned.

Details of the activities for which fees will be charged to the Fund and those that will be recharged to the relevant employer are set out in the schedule below.

3. Schedule

3.1 Actuarial Fees

Activities for which Lothian Pension Fund should be charged:

- all matters relating to the triennial actuarial valuation, except additional work done at the direct request of an individual employer;
- interim actuarial valuations if and when the Administering Authority require such valuations;
- actuarial advice regarding questions concerning the interpretation of Scheme Regulations and matters pertaining to the administration of Fund benefits;
- preparation for and attendance at the Fund meetings; and
- any other matters which affect or are likely to affect all or a significant number of Fund employers.

Activities for which actuarial fees will be recharged to an employer:

- extra, non-standard triennial actuarial valuation work done for and at the direct request of an individual employer;
- a common actuarial service used by most employers is the provision of figures for IAS19/FRS17/FRS102 accounting disclosure purposes. As this information is for the benefit of individual employers and not the Fund itself, the relevant costs are recharged to the individual employers;
- interim valuations where these are not a requirement for all employers but are either: -
  - required by an employer's admission agreement or;
  - not required but specifically requested by the employer concerned;
- calculations etc. in respect of the admission of a new Fund employer;
- Best Value and other outsourcing calculations and consequent interim valuations;
- where an employer has been admitted to the Fund and is required to provide a bond or indemnity to meet any shortfall in funding in the event of the employer ceasing to participate in the Pension Fund, the cost of assessment and subsequent annual reassessment of the value of the bond or indemnity;
- assessing whether a potential/actual contractor's pension arrangement is "broadly comparable" to the Local Government Pension Scheme;
- any other interim valuations for an employer that is required through some action, or failure to act, by that employer;
- bulk transfer work in respect of transfers out of or into the Fund;
- exit valuations; and
- any other charges specific to one employer, or specific to such a small number of employers that it would be unreasonable to spread the cost between the membership as a whole. Where a number of employers are involved, the charges will be proportioned in light of the circumstances of the case.

3.2 Other charges

In addition to recharging actuarial fees as specified above, and for those activities listed below, employers will be recharged for fees incurred in relation to certain requests which result in:

- additional administrative work and advice over and above the standard that is required;
- complex calculations;
- specific work for high earners; and

- if the Fund requires to seek advice or commission work from other providers (e.g. lawyers), costs arising will be recharged to employers in full if this work is specific to that employer or specific to such a small number of employers that it would be unreasonable to spread the cost across all employers in the Fund. Where more than one employer is involved, charges will be apportioned reflective of the circumstances.

Activities for which fees will be recharged to an employer:

- disclosure of information relating to Senior Officers and Councillors for inclusion in Local Authority Accounts:
  - provision of Cash Equivalent Transfer Value calculations and appropriate pension benefit calculations;
  - charges applied per case;
- setting up an Admission Agreement with the Fund for new employers joining the Fund;
  - costs to cover legal fees incurred by the Fund in drafting and finalising the Admission Agreement;
  - See note 1 below;
- attendance at meetings and associated work in connection with Employer projects involving transfers of staff (e.g. outsourcing, mergers etc);
  - a charge will be made where the Fund considers the work undertaken to be in excess of normal advice to employers;
  - costs will be based on Fund Officers time plus VAT; and
- interest payable on an exit valuation where the Fund allows payment to be spread over an agreed period; and interest will be charged at a rate advised by the Fund Actuary

Regulatory recharges

Where an employer has chosen to award compensation in the form of additional membership under Part III of the Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998, for ease of administration the Fund will pay the compensation pension to the member along with the funded pension. The compensation pension will be recharged to the employer on a monthly basis. However, should the awarding employer cease to exist, the compensation pension will cease. The funded pension would be unaffected.

Notes:

1. Any additional costs arising if specialist actuarial, legal etc advice is requested will be charged in full in addition to the figures quoted above.
2. The Fund will act in accordance with relevant procurement guidance in obtaining external professional services.

LOTHIAN PENSION FUND

APPENDIX E: CALCULATION OF EMPLOYER CONTRIBUTIONS

Section 7.4 of the Funding Strategy Statement sets out a broad description of the way in which employer contribution rates are calculated. This appendix considers these calculations in more detail.

The Fund Actuary uses a three-step process to calculate an employer's contribution rate:

1) Calculate the funding target for that employer, i.e. the estimated amount of assets it should hold in order to be able to pay all its members' benefits. The funding target is based on a set of assumptions about the future (e.g. investment returns, inflation, pensioners' life expectancies). If an employer is approaching the end of its participation in the Fund then its funding target may be set on a more prudent basis, so that its liabilities are less likely to be spread among other employers after its cessation;
2) Determine the time horizon over which the employer should aim to achieve that funding target. Employers may be given a lower time horizon if they have a less permanent anticipated membership, or do not have tax-raising powers to increase contributions if investment returns under-perform; and
3) Calculate the employer contribution rate such that it has at least a given likelihood of achieving that funding target over that time horizon (allowing for various possible economic outcomes over that time horizon). The likelihood of achieving the funding target over the employer's time horizon will be dependent on the Fund's view of the strength of employer covenant and its funding profile. Where an employer's financial strength is considered to be weaker, then the required likelihood will be set higher, which in turn will increase the required contributions (and vice versa).

The general policy of the fund is to operate a Contribution Stability Mechanism (CSM) which will apply to certain employers in the Fund. A CSM operated between 2013 and 2023. For the period 1 April 2024 – 31 March 2027, the CSM will be suspended. It is expected to be reintroduced following the 2026 valuation. For the purposes of setting employer contribution rates, employers will continue to be classified as stabilised or non-stabilised. Further information is set out in Section 7.5 of the Funding Strategy Statement.

The table below sets out how this methodology will be applied to each type of employer:

~~Type of Employer~~	~~Scheduled~~			~~Transferee Admission Bodies~~	~~Community Admission Bodies~~					
~~Sub-Group~~	~~Group 1~~	~~Group 2~~	~~Group 3~~	~~N/A~~	~~Open 1~~	~~Open 2~~	~~Closed 1~~	~~Closed 2~~	~~Closed 3~~	~~Lothian Buses~~
~~Investment Strategy~~	~~Main~~	~~Main~~	~~Main~~	~~Main~~	~~Main~~	~~Main~~	~~Medium~~	~~Low~~	~~Main~~	~~Lothian Buses~~
~~Stabilised contribution rate?~~	~~Yes~~	~~Yes~~	~~No~~	~~No~~	~~Yes~~	~~No~~	~~No~~	~~No~~	~~No~~	~~No~~
~~Funding Target Basis used~~	~~Ongoing~~	~~Ongoing~~	~~Ongoing~~	~~Ongoing~~	~~Ongoing~~	~~Ongoing~~	~~Gilts~~	~~Gilts~~	~~Ongoing~~	~~Gilts~~
~~Time Horizon (years)~~	~~20~~	~~15~~	~~15~~	~~Shorter of FWL [1]/ contract length~~	~~15~~	~~15~~	~~FWL~~	~~FWL~~	~~FWL~~	~~20~~
~~Likelihood of~~	~~80%~~	~~80%~~	~~[2]~~	~~[2]~~	~~[2]~~	~~[2]~~	~~N/A~~	~~N/A~~	~~N/A~~	~~80%~~

Formatted Table

LOTHIAN PENSION FUND

~~achieving target~~											

Type of Employer	Scheduled		Transferee Admission Bodies		Community Admission Bodies						
Sub-Group	Group 1	Group 2	TAB 1	TAB 2	Open 1	Open 2	Open 3	Closed 1	Closed 2	Closed 3	Closed 4	Lothian Buses
Investment Strategy	Main	Main	Main	Main	Main	Main	Main	Medium	Low	Main	Main	Lothian Buses
Stabilised contribution rate?	Yes	Yes	No	No	Yes	No	No	No	No	No	No	No
Funding Target Basis used	Ongoing	Ongoing	Ongoing	Ongoing	Ongoing	Ongoing	Ongoing	Medium	Gilts	Ongoing	Ongoing	Gilts
Time Horizon (years)	20	15	20	Shorter of FWL [1}/ contract length	15	20	15	FWL	FWL	FWL	20	20
Likelihood of achieving target	80%	80%	[2]	[2}	[2]	[2]	[2]	N/A	N/A	N/A	80%	80%

The Administering Authority recognises that there may occasionally be particular circumstances affecting individual employers that are not easily managed within the rules and policies set out in the Funding Strategy Statement. Therefore, the Administering Authority reserves the right to direct the Fund's Actuary to adopt alternative funding approaches on a case-by-case basis for specific employers.

[1] Future Working Lifetime of current active members or duration in Fund if shorter
[2] Likelihood based on employer covenant rating

This methodology is suitable for employers who are open to new entrants and who therefore have a long time horizon and are not expected to leave the Fund. This applies to all employers in the primary investment strategy. The risk-based method uses a long-term economic model of the future to set contributions which take account of expected future economic conditions rather than being dominated by current conditions. It also places much less reliance on the current funding position, particularly as the funding position in itself is of less importance to employers who aren't planning to leave the Fund.

The employers who participate in the medium and low risk investment strategies have had their contribution rates determined using a single set of economic assumptions about the future ("deterministic method"). These employers are all closed to new entrants and will eventually leave the fund, at which point their funding position will crystallise. The current funding position is therefore of more importance for these employers, as they have shorter time horizons which means that current or 'near term' market conditions become more relevant than long-term assumptions. It therefore makes more sense to use a deterministic method in which the current funding position and current market conditions are used as the basis for setting contributions.

These general principles apply to the majority of the Fund's employers. However, the Fund retains discretion to choose the most appropriate method based on an employer's specific circumstances, and this affects a small number of employers in practice. In particular, contribution rates for certain employers may be frozen to protect the accumulated surplus position at 31 March 2023.

Calculation of employer contribution rates: calculation methodology

The Primary rate is calculated such that it is projected to:

1) meet the required funding target for all future years' accrual of benefits*, excluding any accrued assets,
2) within the determined time horizon;
3) with a sufficiently high likelihood, as set by the Fund's strategy for the category of employer

*The projection is for the current active membership where the employer no longer admits new entrants, or additionally allows for new entrants where this is appropriate.

The Secondary rate is an adjustment to Primary rate and may be either positive or negative. Where the secondary rate is positive, this is calculated as the balance over and above the Primary rate, such that the total contribution rate is projected to:

1) meet the required funding target relating to combined past and future service benefit accrual, including accrued asset share,
2) at the end of the determined time horizon,
3) with a sufficiently high likelihood, as set by the Fund's strategy for the category of employer.

When the risk-based approach is used, ~~T~~the projections are carried out using an economic modeller (the "Economic Scenario Service") developed by the Fund's Actuary Hymans Robertson: this allows for a wide range of outcomes on key factors such as asset returns (based on the employer's investment strategy), inflation, and bond yields. The measured contributions are calculated such that the proportion of outcomes meeting the employer's funding target (at the end of the time horizon) is at least equal to the required likelihood.

Additional prudence has been included in the calculation of employer contribution rates from 1 April 2024 by building in the potential for an asset shock of 20% - that is a reduction in the value of current assets applied proportionally across all assets held by the fund. This means in the event of an immediate and permanent loss of assets of this scale, the contribution plan would still meet the minimum likelihood of success.

Actuarial Assumptions used to calculate employer contribution rates

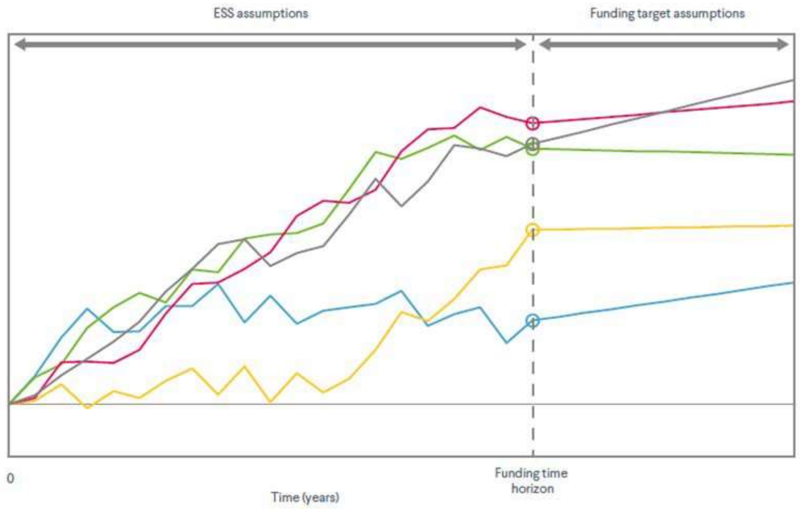
These are expectations of future experience used to place a value on future benefit payments ("the liabilities") and future asset values. Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, probabilities of ill-health early retirement, and proportions of member deaths giving rise to dependants' benefits.

Changes in assumptions will affect the funding target and required contribution rate. However, different assumptions will not of course affect the actual benefits payable by the Fund in future.

The f~~F~~und a~~A~~ctuary's risk-based approach to calculating employer contribution rates involves the projection of each employer's future benefit payments, contributions and investment returns into the future under 5,000 possible economic scenarios. Future inflation (and therefore benefit payments) and investment returns for each asset class (and therefore employer asset values) are variables in the projections. By projecting the evolution of an employer's assets and benefit payments 5,000 times, a contribution rate can be set that results in a sufficient number of these future projections (determined by the employer's required likelihood) being successful at the end of the employer's time horizon. In this context, a successful contribution rate is one which results in the employer having met its funding target at the end of the time horizon.

Setting employer contribution rates therefore requires two types of assumptions to be made about the future:

1) Assumptions to project the employer's assets, benefits and cashflows to the end of the funding time horizon. For this purpose, the Fund's Actuary uses Hymans Robertson's proprietary stochastic economic model - the Economic Scenario Service ("ESS")
2) Assumptions to assess whether, for a given projection, the funding target is satisfied at the end of the time horizon. For this purpose, the Fund has two different funding bases.



What assumptions are used in the ESS?

The Fund's Actuary uses Hymans Robertson's ESS model to project a range of possible outcomes for the future behaviour of asset returns and economic variables. With this type of modelling, there is no single figure for an assumption about future inflation or investment returns. Instead, there is a range of what future inflation or returns will be which leads to likelihoods of the assumption being higher or lower than a certain value.

The ESS is a complex model to reflect the interactions and correlations between different asset classes and wider economic variables. The table below shows the calibration of the model as at 31 March 2023. All returns are shown net of fees and are the annualised total returns over 5, 10 and 20 years, except for the yields which refer to the simulated yields at that time horizon.

LOTHIAN PENSION FUND

-		Annualised total returns							Inflation/Yields		
Time Period	**Percentile**	**Cash**	**All World ex-UK Equity**	**UK Equity**	**Index Linked Gilts (medium)**	**Fixed Interest Gilts (medium)**	**Property**	**Corporate Debt**	**Inflation (CPI)**	**17 year real yield (CPI)**	**17 year yield**
10 years	16th	2.5%	1.1%	1.3%	0.8%	2.4%	1.2%	2.7%	0.9%	-0.3%	2.7%
	50th	3.6%	7.3%	7.5%	2.8%	3.7%	6.2%	4.3%	2.5%	0.9%	4.1%
	84th	4.7%	13.6%	13.5%	5.1%	4.9%	11.5%	5.8%	4.1%	2.2%	5.9%
20 years	16th	2.3%	2.8%	3.0%	1.0%	3.3%	2.7%	3.7%	0.7%	-0.5%	1.4%
	50th	3.7%	7.4%	7.5%	2.7%	4.1%	6.4%	4.7%	2.3%	1.3%	3.4%
	84th	5.4%	12.2%	12.0%	4.5%	4.8%	10.3%	5.8%	3.9%	2.9%	5.9%
40 years	16th	1.8%	3.7%	3.9%	1.0%	2.9%	3.2%	3.4%	0.6%	-0.6%	1.2%
	50th	3.5%	7.2%	7.4%	2.7%	3.7%	6.2%	4.4%	2.0%	1.3%	3.3%
	84th	5.7%	10.9%	10.9%	4.6%	4.9%	9.5%	5.8%	3.5%	3.2%	6.1%
-	Volatility (Disp) (5 yr)	2%	18%	18%	7%	5%	15%	6%	3%	-	-

What assumptions are used in the funding target?

At the end of an employer's funding time horizon, an assessment will be made – for each of the 5,000 projections – of how the assets held compare to the value of assets required to meet the future benefit payments (the funding target). Valuing the cost of future benefits requires the actuary to make assumptions about the following financial factors:

- Benefit increases and CARE revaluation
- Salary growth
- Investment returns (the "discount rate")

Each of the 5,000 projections represents a different prevailing economic environment at the end of the funding time horizon and so a single, fixed value for each assumption is unlikely to be appropriate for every projection. For example, a high assumed future investment return (discount rate) would not be prudent in projections with a weak outlook for economic growth. Therefore, instead of using a fixed value for each assumption, the actuary references economic indicators to ensure the assumptions remain appropriate for the prevailing economic environment in each projection. The economic indicators the actuary uses are future inflation expectations and the prevailing risk-free rate of return (the yield on long term UK government bonds is used as a proxy for this rate).

The Fund has three~~wo~~ funding bases which will apply to different employers depending on their type. Each funding basis has a different assumption for future investment returns when determining the employer's funding target.

LOTHIAN PENSION FUND

Funding Basis	**Ongoing basis**	**Medium-risk basis**	**Low-risk basis**
Employer type	All employers except Community Admission Bodies closed to new entrants*	Community Admission Bodies closed to new entrants with 5 or more active members	Community Admission Bodies closed to new entrants with 5 or fewer active members
Investment return assumption underlying the employer's funding target (at the end of the time horizon)	Long-term government bond yields plus an asset outperformance assumption (AOA) of 1.6% +p.a**	Long-term government bond yields plus an asset outperformance assumption (AOA) of 0.8% +p.a	Long-term government bond yields with no allowance for outperformance on the fund's assets

*See section 7.2 for full information on employers to whom ongoing basis applies.

***For existing Transferee Admission Bodies, the ongoing investment return assumption at the end of the employer's time horizon is Long term government bond yields plus an asset outperformance assumption (AOA) of 1.5% +p.a

Formatted: Font: Bold

Formatted: Tab stops: 3.62 cm, Left

APPENDIX F: SALARY STRAIN RECHARGING MECHANISM

What is salary strain?

Prior to 1 April 2015, the Local Government Pension Scheme (LGPS) in Scotland was a 'final salary' scheme, so a member's pension accrued before 1 April 2015 is directly linked to their salary at retirement. This means that salary increases awarded to employees have a direct impact on total pension costs for employers. At each triennial valuation of the Fund, the Fund's Actuary makes an assumption about the level of future salary growth. At the next valuation, the Fund's Actuary assesses the difference between the increases awarded over the last three years compared to those assumed. If salary increases were higher than anticipated, this will lead to higher pension costs. This increase in costs is referred to as 'salary strain'.

Why is a salary strain mechanism in place?

At the 2020 valuation, the Fund discussed the appropriateness of the salary growth assumption, taking into account recent economic conditions and the outlook for future long term pay awards. The assumption agreed as part of the 2020 valuation discussions was significantly lower than that used at previous valuations and equivalent to a long-term rate of consumer price inflation ('CPI') plus 0.5% p.a. The valuation also includes an age-related allowance for promotional salary growth in addition to the inflationary element.

A lower salary growth assumption places a lower value on the liabilities and reduces future pension costs. All else being equal, employers therefore benefit via an improved funding position and lower contribution rate. However, assuming a lower level of future salary growth places a greater risk on the Fund of employers awarding larger than expected pay increases and not being able to meet the additional pension costs in the future. A salary strain recharging mechanism therefore controls this risk and allows the Fund to charge for salary strains if they occur.

The salary assumption agreed as part of the 2023 valuation is 3.0%. Although this is higher than the assumption used previously, the salary strain mechanism is retained as part of the Fund's ongoing monitoring and risk management processes.

How does the mechanism work?

The Fund will work with the actuary to monitor salary increases annually. Any salary growth strain arising will be billed immediately to the responsible employer.

Following each March year-end after the latest formal valuation, the Fund will provide an annual data cut of salary information to the Fund's Actuary for all employers in the Fund. The Fund's Actuary will then calculate whether any salary growth strain has occurred by comparing the employee's salary at the year-end against the expected salary for that same member (based on data from the previous formal valuation). The strain will then be totalled per employer. The actuary will also carry out an interim valuation of each employer's membership data at a recent date to provide an indicative funding for each employer. This will be considered alongside the results of the salary strain review and the following process will be applied:

- Where the employer has a funding level in excess of 130% the strain will be waived (although the employer can still pay), subject to the agreement of the scheme employer acting as guarantor (where applicable);

LOTHIAN PENSION FUND

- Where the employer has a funding level between 115% and 130% a lower strain payment will be due, subject to the agreement of the scheme employer acting as guarantor (where applicable). The amount due will be capped at the amount that would allow a funding level of 130%; and
- Where the employer's funding level is less than 115% any salary strain identified will be recharged in full.

Where a strain applies the Fund will recharge the additional cost to employers via an invoice.

Assessing and managing salary strain on an annual basis avoids any unexpected deterioration in funding position resulting from pay awards at future valuations. The mechanism is a way to recognise the cost of salary strain at the point at which pay awards are granted, rather than letting the cost be met over a much longer time period. In the past, any salary strains have been met via higher ongoing pension contributions (as a higher salary growth assumption was used) or they have emerged at the next valuation resulting in a funding deficit, causing future contributions to rise

For members who have left during the period, the period-end salary will be at the date of leaving. Members who have joined during the inter-valuation period will be excluded from the analysis. However, if there are members who have joined the Fund and had a transfer in of final salary past service, any salary strain or gain in relation to these members would be allowed for at the next formal valuation of the Fund.

What if salary increases are less than expected?

If a salary gain is calculated in one year (i.e. the salary growth is less than that expected), then we would allow this to offset a strain occurring in any future year up to the next formal valuation date. If the overall impact of salary increases between valuations is a gain, then this will be credited to the employer's funding position at the next valuation and will help to reduce its contribution rate going forward (all other things being equal).

For the avoidance of doubt, salary strain is calculated on a member-by-member basis, with salary gains for members with pay awards that are lower than assumed being offset against strains for members with high pay awards. This means that is possible for an overall strain to arise even if the average pay award for any given employer is <u>lower</u> than the valuation assumption e.g. where an employer grants high pay awards to a few employees with long LGPS service and/or high salaries, and lower pay awards to the rest of its workforce.

Appendix 2

Funding Strategy Statement – responses to employer comments

As required under the Local Government Pension Scheme Regulations 2018, the fund reviewed the Funding Strategy Statement (FSS), as part of the 2023 valuation process. The regulations also require that the fund must consult with employers on any changes being made.

The draft revised FSS was approved by Pensions Committee in December 2023 and issued to employers on 21 December 2023 as part of a special edition of the employer bulletin. The bulletin advised that the consultation period would run until 31 January 2024.

Officers received two official responses to the consultation. These comments and our feedback are detailed below:

- 'Regarding the change in setting of employer contribution rates; it is recognised that given the surplus at the most recent valuation, increased prudence to the likelihood of achieving the funding target has been built in, and the contribution stability mechanism has been suspended for the current valuation period. However, it is less clear how an equitable approach has been applied to the proposed reduction for stabilised employers (to pay contributions at a lower rate than previously expected) i.e. given not all long-term stabilised employers were paying the same rate, a revised common rate represents different levels of reduction relative to the current rates payable. How will this variance be addressed at the next valuation if/when the CSM is re-introduced?'

  Employer contribution rates are based on individual circumstances and as noted above, not all stabilised employers have paid the same employer contribution rate in the 2023/24 year. The 2023 valuation results have allowed the fund to propose a suspension in the contribution stability mechanism and a reduction to employer contribution rates for the three years from 1 April 2024. It is unclear however what the results will be at the next valuation and although additional prudence has been built into the valuation, there is a risk that rates may have to revert to previous levels (or higher). In applying contribution reductions, the employers with the largest membership group have seen the greatest reduction. These employers, with their larger membership base, and tax-raising powers, will be better placed to withstand any significant increases in contribution rates at the next valuation.

- 'Appendix E states "In particular, contribution rates for certain employers may be frozen to protect the accumulated surplus position at 31 March 2023". Is there a process and criteria for deciding which employers that this might apply to?'

  The fund is made of a variety of different employer types, from large Councils to small third sector bodies. The largest, most secure bodies were part of the Contribution Stability Mechanism (CSM), but smaller bodies were not. Appendix E of the FSS sets out how employer contributions are calculated. The table sets out the different employer groups and the funding bases which apply. As noted in Appendix E Employer covenant is also an important consideration and discussions with guarantors (where applicable) have also taken place.

- 'It also states in Appendix E that; "Additional prudence has been included in the calculation of employer contribution rates from 1 April 2024 by building in the potential for an asset shock of

20% - that is a reduction in the value of current assets applied proportionally across all assets held by the fund". Will this prudence be built in for future valuations or is it only for this year to take account of the better improvement in the funding position?'

The strong valuation results as at 31 March 2023 have resulted in a significant surplus at the valuation date. This result has been due to greater than expected investment returns and therefore we have taken steps to protect the fund, not only by moving some assets from more volatile equities to less risky assets, but also by ensuring that employer contribution rates set will be able to withstand an asset shock of 20%. We cannot predict the valuation results in 2026, but prudence is always a key consideration in any valuation and should a similarly strong surplus position arise in 2026, we may consider such steps again.

- 'We would like the opportunity to engage in the planned review of the stability mechanism taking place in 2024'.

  The contribution stability mechanism will be reviewed in December 2025 in advance of the 2026 triennial valuation. This will be a full review of asset liability modelling by the actuary and results and recommendations will be presented to Pensions Committee in December 2025. We will advise employers of the results and will also update our FSS to include details of how the mechanism will operate from 1 April 2027. Employers will, as always be consulted on changes to the FSS.

- 'It would be useful if someone could confirm when we might have confirmation of what the maximum change would be when the stability mechanism is reintroduced. We would need these changes to be controlled to allow planning for the increased costs that this may bring'.

  As noted above, we plan to carry out the review of the CSM in 2025 and this will allow us to complete the process in advance of the 2026 valuation which will set employer contributions for the three years from 1 April 2027. We fully understand that employer budgetary planning cycles do not align with the valuation but as always we will give as much notice as possible of changes.

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Actuarial Valuation for Lothian Pension Fund

Item number 6.4

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 Note the results of the 2023 Actuarial Valuation of Lothian Pension Fund.

Alan Sievewright
Chief Finance Officer, Lothian Pension Fund

Contact: Erin Savage, Senior Pensions Employer and Member Manager, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Actuarial Valuation for Lothian Pension Fund

2. Executive Summary

2.1 An actuarial valuation of Lothian Pension Fund (LPF) must, by law be carried out every three years. The fund actuary assesses the financial health of the pension fund and sets the employer contribution rates required for the next three years. The last actuarial valuation was carried out as at 31 March 2020.

2.2 The actuarial valuation of LPF, based on data as at 31 March 2023 has been carried out by the fund actuary, Hymans Robertson and the final valuation report is attached as Appendix 1.

3. Background

3.1 The Local Government Pension Scheme (Scotland) Regulations 2018 require each administering authority to obtain:

- An actuarial valuation of the assets and liabilities of each of its pension funds as at 31 March 2020 and on 31 March in every third year afterwards;
- A report by an actuary in respect of the valuation; and
- A rates and adjustments certificate prepared by the actuary.

3.2 The Regulations require that the actuarial valuation based on data as at 31 March 2023 must be completed by 31 March 2024.

3.3 The actuarial valuation has three main purposes:

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

3.4 In December 2023, Pensions Committee approved a draft revised Funding Strategy Statement (FSS) which outlined several key changes introduced for the 2023 valuation. The key change was the suspension of the Contribution Stability Mechanism for the period 1 April 2024 to 31 March 2027.

3.5 A separate report on the revised FSS is provided on this agenda.

4. Main Report

4.1 The 2023 Actuarial Valuation report for Lothian Pension Fund, as submitted by the actuary, is included at Appendix 1.

Funding Level - Summary

4.2 The table below summarises the financial position of the fund as at 31 March 2023.

Past Service Position	2020	2023
Past Service Liabilities £m	£7,071	6,170
Assets £m	£7,479	9,695
Surplus/(Deficit)	408	3,525
Funding Level	**106%**	**157%**

4.3 The results show the funding level has increased from 106% at the previous valuation to 157% at this valuation, and there was a surplus of £3,525 million at 31 March 2023.

4.4 Section 3.5 of Appendix 1 sets out the various factors that have led to the change in the funding position between the 2020 and 2023 valuations.

4.5 Committee will remember from previous training and briefing sessions that the key driver behind the improvement in results was investment performance over the three-year period and a higher discount rate that reduces the present value of accrued liabilities.

Employer Contribution Rates

Whole Fund

4.6 The table below compares the whole fund Primary and Secondary Contribution Rates at this valuation to those set at the previous valuation as at 31 March 2020:

	Last Valuation 31 March 2020		This Valuation 31 March 2023	
Primary rate (% of pay)	23.1		25.0	
Secondary rate (£)	2021/2022	-11,262,000	2024/25	-73,589,000
	2022/2023	-11,378,000	2025/26	-75,809,000
	2023/2024	-11,530,000	2026/27	-78,095,000

4.7 The increase in the primary rate is primarily the result of increasing the level of prudence in the valuation assumptions, whilst the larger negative secondary rate leading to an overall reduction in total contributions reflects the strong funding position of the fund.

Common Contribution rate

4.8 The rates in the table above show the position of the overall fund, however contribution rates are set for each employer depending on their individual funding position and membership. The minimum contributions to be paid by each employer from 1 April 2024 to 31 March 2027 are shown in the Rates and Adjustments Certificate - Appendix 5 of the actuary's report which is included as Appendix 1.

4.9 The actuary must provide a whole fund common contribution rate in the report. The Primary rate is the payroll weighted average of the underlying individual employer Primary rates, and the Secondary rate is the total of the underlying individual employer Secondary rates, calculated in accordance with the Scheme regulations.

4.10 As the common contribution rates are based on the weighted payroll average, the Primary contribution rate is impacted by the fact that the largest employers have seen a reduction in contribution rates. In addition, there has been a reduction in the number of employers since the 2020 valuation, and some of the employers with the highest Primary rates have left the fund.

Individual employer results

4.11 The rates in the table above show the position of the overall fund, however contribution rates are set for each employer depending on their individual funding position and membership. As noted above, the minimum contributions to be paid by each employer from 1 April 2024 to 31 March 2027 are shown in the Rates and Adjustments Certificate - Appendix 5 of the actuary's report which is included as Appendix 1.

4.12 As previously advised to Committee in previous briefings and training sessions, the improved valuation results have meant that the Contribution Stability Mechanism (CSM) has been suspended for the three-year period from 1 April 2024 to 31 March 2027. The CSM would have led to a reduction of no more than 0.5% per annum from 1 April 2027 for stabilised employers. Due to the improved funding position, the fund and the actuary have been able to reduce rates to a greater extent. The majority of stabilised employers will have a flat rate of 17.6% for the three years from 1 April 2024. Any stabilised employer with rates already below this level will have rates frozen at the 2023/24 level.

4.13 The CSM is only available to certain employers, specifically those which are open to new entrants, have sufficiently strong covenant and, where applicable their guarantor agrees to their participation. Further information is set out in Section 7.5 of the FSS. For non-stabilised employers, consideration of specific employer circumstances, including covenant strength and time horizon have been taken into account when setting employer rates.

4.14 Committee will recall that in setting contribution rates, in order to build in additional prudence, the following steps have been taken:

- Building in an asset shock of 20% to protect the fund against a fall in asset values and future expected investment returns;
- Increasing the likelihood of success to 80%; and
- Making a moderate reduction in the amount of assets invested in more volatile assets. More detailed information on this point is set out in the investment strategy review paper.

4.15 Further details about contribution rates for specific employers are detailed in Appendix 2.

Communication

4.16 Indicative employer results were provided to employers in November 2023, following a presentation from the actuary at an employer seminar. Fund officers met with employers on an individual basis to provide further information on their draft valuation results and proposed employer contribution rates.

4.17 Some employers provided information to their employees about their draft valuation results and indicative employer contribution rates which are lower than those paid in the 2023/24 year. This has led to the fund receiving a number of queries from members concerned about the impact this might have on their pension benefits. Fund officers have responded to these queries providing reassurance that as a statutory defined benefit pension scheme, benefits are not based on the amount of contributions paid, but instead on the rules of the scheme which are set out in law.

4.18 A press release and website update regarding the valuation results have been prepared and these will be published following Committee. In future valuations, employers will be reminded that initial results are draft only and information should not be more widely disclosed prior to the Committee approving the FSS, having sight of the final valuation report and thus confirming the new contribution rates.

Confirmation of affordability

4.19 Section 7.7 of the FSS requires employers to provide written confirmation that minimum contribution rates set by the actuary are not unaffordable.

4.20 At the time of writing, such confirmation has been provided by 45 out of 60 employers. Fund officers are continuing to engage with the remaining employers and a verbal update will be provided to Committee.

Climate change risk

4.21 As noted above, several training and briefing sessions were held for members of Committee and the Pensions Board. At these sessions, Committee asked for additional information on how additional information on how climate change risk was being taken into account within the valuation. This followed publication of the report 'The Emperor's New Climate Scenarios' by the Institute and Faculty of Actuaries and the University of Exeter which questioned whether current economic models underestimated the risks of climate change Climate change. Similar views were also expressed by Carbon Tracker at an event hosted by the City of Edinburgh Council.

4.22 To this end, a paper outlining the risks climate change poses to the funding strategy, and the measures currently being taken to manage these risks is attached as Appendix 3.

5. Financial impact

5.1 The funding strategy should ensure that the fund has sufficient assets in the long term to meet its liabilities.

5.2 The results of the actuarial valuation have significant financial impact on the fund's employers. The actuarial valuation sets the minimum contribution rates payable by the employer over the next 3 years.

5.3 The fund is required by law to carry out an actuarial valuation once every three years. Regular actuarial valuations manage the risk of not meeting funding objectives.

6. Stakeholder/Regulatory Impact

6.1 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.

6.2 Training sessions on the draft valuation results were held for members of the Committee and Pensions Board in October and November 2023. The session in October included a presentation by the fund actuary.

6.3 Employers have been consulted on changes to the Funding Strategy Statement.

6.4 Further meetings and discussions were held with employers in December 2023 and January and February 2024 to consider the valuation results in greater detail.

6.5 The requirements of the Local Government Pension Scheme (Scotland) Regulations 2018 as they pertain to the valuation have been met in full.

7. Background reading/external references

7.1 None.

8. Appendices

Appendix 1: Lothian Pension Fund 2023 Valuation Final Valuation Report

Appendix 2: Employer contribution rates.

Appendix 3: Managing Climate Risk.

This page is intentionally left blank

Appendix 1

HYMANS ROBERTSON

Lothian Pension Fund

Report on the actuarial valuation as at 31 March 2023

March 2024

Richard Warden FFA

Julie Baillie FFA

For and on behalf of Hymans Robertson LLP

Hymans Robertson LLP

One London Wall
London EC2Y 5EA
t 020 7082 6000
f 020 7082 6082

20 Waterloo Street
Glasgow G2 6DB
t 0141 566 7777
f 0141 566 7788

45 Church Street
Birmingham B3 2RT
t 0121 210 4333
f 0121 210 4343

1 Semple Street
Edinburgh EH3 8BL
t 0131 656 5000
f 0131 656 5050

hymans.co.uk

Contents

Report on the actuarial valuation as at 31 March 2023		Page
	Executive summary	1
1	Approach to the valuation	2
2	Valuation results	4
3	Sensitivity and risk analysis	10
4	Final comments	13
Appendix 1: Data		15
Appendix 2: Assumptions		17
Appendix 3: Reliances & limitations		21
Appendix 4: Glossary		22
Appendix 5: Rates and Adjustments Certificate		25
Appendix 6: Section 13 dashboard		31

Executive summary

We have been commissioned by City of Edinburgh Council ("the Administering Authority") to carry out a valuation of Lothian Pension Fund ("the Fund") as at 31 March 2023. This fulfils Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2018. This report is a summary of the valuation.

1. Contribution rates

The contribution rates for individual employers set at this valuation can be found in the Rates and Adjustments certificate. Table 1 shows the combined individual employer rates set at this valuation and the last valuation.

Table 1: Whole fund contribution rates compared with the previous valuation

	31 March 2023		31 March 2020	
Primary rate	25.0% of pay		23.1% of pay	
Secondary rate	2024/25	-£73,589,000	2021/22	-£11,262,000
	2025/26	-£75,809,000	2022/23	-£11,378,000
	2026/27	-£78,095,000	2023/24	-£11,530,000

The primary rate has increased due to a combination of higher prudence in funding plans and higher future inflation expectations at 2023, compared to 2020. Further details of this higher prudence are set out in Section 2.2.3. The secondary rate has reduced due to strong investment performance since the last valuation, and higher future investment return expectations, leading to stronger past service funding positions amongst employers.

2. Funding position

At 31 March 2023, the past service funding position has improved from the last valuation at 31 March 2020. Table 2 shows the single reported funding position at this valuation and the last valuation.

Table 2: Single reported funding position compared with the previous valuation

	31 March 2023	31 March 2020
	(£m)	**(£m)**
Active members	2,272	2,868
Deferred Pensioners	824	1,047
Pensioners	3,074	3,156
Total liabilities	**6,170**	**7,071**
Assets	**9,695**	**7,479**
Surplus (Deficit)	**3,525**	**408**
Fund level	**157%**	**106%**

The required investment return to be 100% funded is 2.2% p.a. (2.7% p.a. at 2020). The likelihood of the Fund's investment strategy achieving the required return is 95% (78% at 2020).

1 Approach to the valuation

1.1 Valuation purpose

The triennial actuarial valuation is an important part of the Fund's risk management framework. Its main purpose is to ensure the Fund continues to have a contribution plan and investment strategy that will achieve the objectives set out in the Funding Strategy Statement.

This report marks the culmination of the valuation process and contains its two key outcomes:

1. Employer contribution rates for the period 1 April 2024 to 31 March 2027
2. The funding level of the whole Fund at 31 March 2023.

Further information on the valuation process, methodology and strategy is set out in the publicly available Funding Strategy Statement, Statement of Investment Principles and published papers of the Fund's Pensions Committee. Additional material is also contained in Hymans Robertson's LGPS 2023 valuation toolkit.

1.2 Setting employer contribution rates

Employer contributions need to be set at a level which ensures the Fund has a reasonable likelihood of having enough money to pay members' benefits. Identifying the amount of benefits that may be paid is complex, as benefits earned today may only start being paid in 50 years' time. Over that period, there is significant uncertainty over factors which affect the cost of benefits eg inflation and investment returns. These uncertainties are allowed for by taking a risk-based approach to setting employer contribution rates. This approach is built around three key funding decisions set by the Fund.

1.2.1 Key funding decisions

Decision 1: What is the funding target for each employer?
Consider: Will the employer remain in the Fund for the long term or exit at some point?

Decision 2: What is the funding time horizon?
Consider: How long will the employer participate in the Fund?

Decision 3: What is the required likelihood of success?
Consider: How much prudence can the employer's covenant support in its funding plan?

1.2.2 Modelling approach

Asset-liability modelling is used to project each employer's assets and benefit payments into the future using 5,000 different economic scenarios. These are generated using Hymans Robertson's Economic Scenario Service (ESS). Further information on this can be found in Appendix 2.

A contribution rate is set for each employer which has (at least) the required likelihood of meeting the funding target over the relevant funding time horizon. The 5,000 projections of the employer's assets and benefits from the asset-liability model are used to quantify the likelihood that a given contribution rate will meet this target.

1.2.3 Risk budgeting

In recognition of uncertainty around climate risk and 'tail risks' in the asset-liability modelling, such as geo-political escalations and rapid reductions to interest rates, the Fund has added prudence into employer funding plans by:

- Increasing the confidence level – the 'likelihood of funding success' parameter described in 1.2.1 above was raised from a minimum of 67% (for some scheduled bodies) at the 2020 valuation to a minimum of 80% across all employers.
- Applying an asset shock – employer assets were reduced by 20% for the purpose of determining contribution rates.

These measures retain money in the Fund to hold as a buffer against future poor experience in the areas mentioned.

1.3 Measuring the funding level

The past service funding level is measured at the valuation date. While it is limited in providing insight into a funding plan, it is a useful high-level summary statistic. A market-related approach is taken to calculate both the assets and the liabilities to ensure they are consistent with one another:

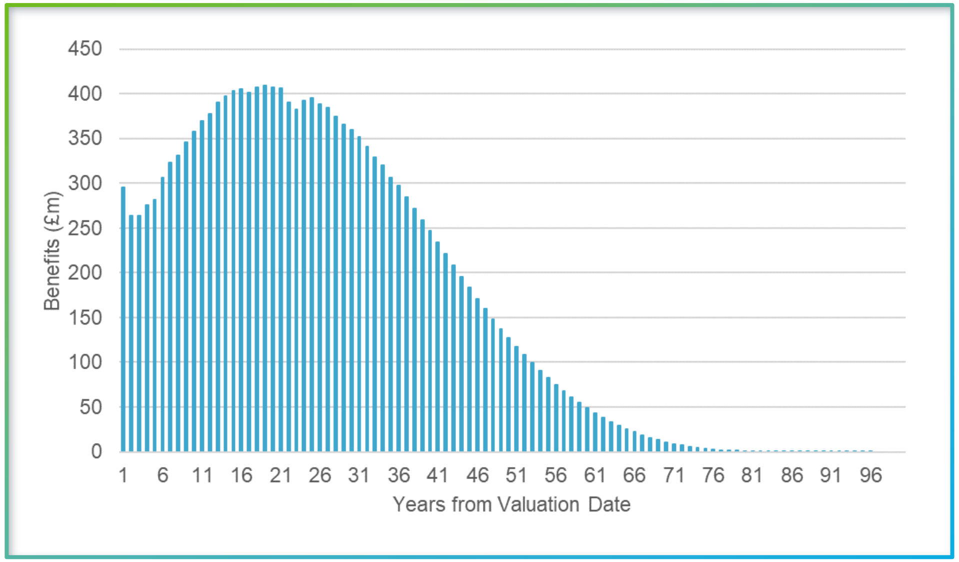
1. The bid-market value of the Fund's assets at the valuation date has been used.
2. The liabilities have been valued using assumptions based on market indicators at the valuation date (these assumptions are detailed in Appendix 2).

1.3.1 Calculating the liabilities

The liabilities are the value of all future payments to members based on all benefits earned up to the valuation date, expressed in today's money.

Chart 1 shows the projected payments for all members in the Fund at the valuation date. The projections are based on the membership data provided for the valuation (Appendix 1), the assumptions (Appendix 2), and our understanding of the LGPS benefit structure as at 31 March 2023 (details at www.scotlgpsregs.org).

Chart 1: Projected benefit payments for all service earned up to 31 March 2023



To express the future payments in today's money, each projected payment is discounted back to the valuation date in line with an assumed rate of future investment return (known as the discount rate').

Page 116

2 Valuation results

2.1 Employer contribution rates

The primary objective of the Fund is to set employer contribution rates that will enable it to pay members' benefits. A secondary objective is to ensure the rates are as stable as possible. The risk-based approach detailed earlier is used to meet both those objectives.

The employer contribution rate is made up of two components.

1. **A primary rate:** the level sufficient to cover benefits that will be accrued in the future.
2. **A secondary rate:** the costs associated with sufficiently funding benefits accrued up to the valuation date.

Each employer has a contribution rate which is appropriate to their circumstances, and these can be found in the Rates & Adjustments Certificate (Appendix 5).

Broadly speaking, primary rates have increased due to a combination of higher prudence in funding plans and higher future inflation expectations at 2023, compared to 2020. Secondary rates have reduced due to strong investment performance since the last valuation, and higher future investment return expectations, leading to stronger past service funding positions amongst employers.

However, all employers will be different, and the contribution rate will reflect the membership and experience of each employer.

Table 3 shows the total of all employer contribution rates to be paid into the Fund at Whole Fund level over the period 1 April 2024 to 31 March 2027.

Table 3: Whole fund contribution rates compared with the previous valuation

	31 March 2023		31 March 2020	
Primary rate	25.0% of pay		23.1% of pay	
Secondary rate	2024/25	-£73,589,000	2021/22	-£11,262,000
	2025/26	-£75,809,000	2022/23	-£11,378,000
	2026/27	-£78,095,000	2023/24	-£11,530,000

The primary rate includes an allowance of 0.3% of pensionable pay for the Fund's expenses (0.3% of pay at the last valuation).

Employees pay a contribution to the Fund in addition to these rates. These rates are set by the LGPS Regulations. The average employee contribution rate at 31 March 2023 is 6.2% of pay (6.3% at 31 March 2020).

Page 117

2.2 Funding level

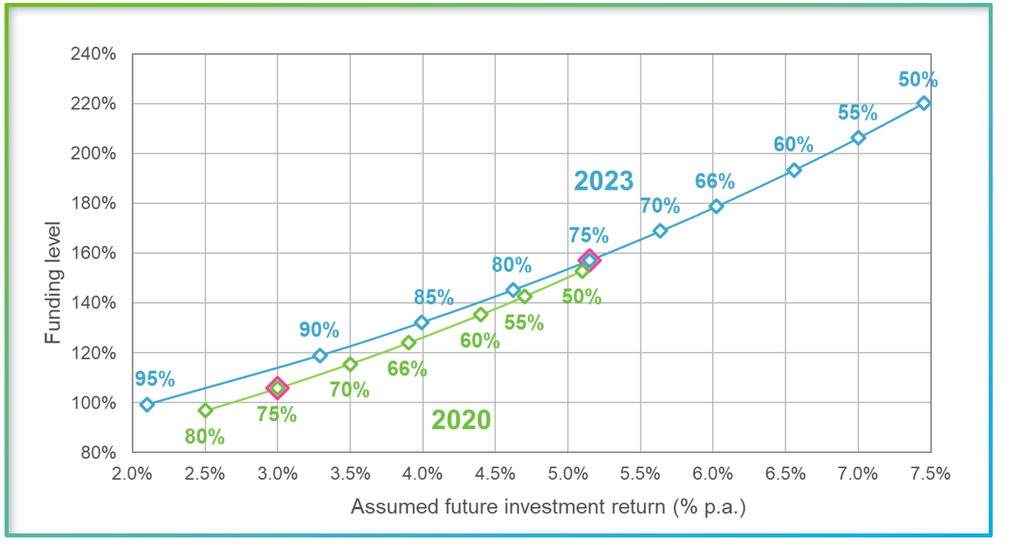
The funding level is the ratio of assets to liabilities. The market value of the assets at the valuation date is known. The value (in 'today's money') of the future benefit payments is uncertain given that the level of future investment returns is unknown.

To help understand funding risk, the liabilities and therefore the funding level have been calculated across a range of different assumptions for future investment returns (also known as 'discount rates'). The likelihood of the Fund's investment strategy (detailed in Appendix 1) achieving those levels of return has also been calculated.

Chart 2 shows how the funding level varies with different future investment return assumptions at 31 March 2023 (blue line). The green line shows the same analysis at 31 March 2020.

- The funding position at 2023 is stronger than it was in 2020.
- The funding level at 2023 will be 100% if future returns are around 2.2% pa. The likelihood of the Fund's assets yielding at least this return is around 95%.
- The comparator at 2020 was a return of 2.7% pa which had a likelihood of 78%.
- There is a 50% likelihood of an investment return of 7.5% pa, so the "best estimate" funding level is 220% at 31 March 2023 (153% at 2020).

Chart 2: Funding level across a range of future investment returns



Figures on each line show the likelihood of the Fund's assets exceeding the level of return over the next 20 years.

Page 118

2.3 Single funding level as at 31 March 2023

While Chart 2 provides a better understanding of the past service funding position, there is still a requirement to report a single funding level at 31 March 2023.

To report a single funding level and funding surplus/deficit for the 2023 valuation, an assumed future investment return of 5.2% pa has been used. There is a 75% likelihood associated with this level of future investment return.

Table 4 sets out the assets and liabilities at the valuation date. The results at the 2020 valuation are shown for comparison.

The funding level and surplus/deficit figures provide a high-level snapshot of the funding position as at 31 March 2023, but there are limitations:

- The liabilities are calculated using a single set of assumptions about the future and so are very sensitive to the choice of assumptions.
- The market value of assets held by the Fund will change daily.

The future progression of the funding position is uncertain. If the financial and demographic assumptions made at this valuation occur in practice, employers pay contributions in line with the R&A certificate, and there are no other changes in the financial or demographic environment, we project that the funding level at the next valuation (31 March 2026) will stay approximately the same at 159%.

The Fund's long-term sustainable rate is 19.3% of pay (excluding expenses). The represents the required primary contribution rate, with a likelihood of success of 75%. This rate is not included in the R&A certificate and does not reflect any employer's current funding profile, only the cost of future service.

Table 4: Single reported funding position compared with the previous valuation

	31 March 2023	31 March 2020
	(£m)	**(£m)**
Active members	2,272	2,868
Deferred pensioners	824	1,047
Pensioners	3,074	3,156
Total liabilities	**6,170**	**7,071**
Assets	**9,695**	**7,479**
Surplus/(Deficit)	**3,525**	**408**
Funding level	**157%**	**106%**

The reported funding level does not directly drive the contribution rates for employers. The contribution rates take into consideration how assets and liabilities will evolve over time in different economic scenarios. They also reflect each employer's funding profile and covenant.

2.4 Changes since the last valuation

2.4.1 Events between 2020 and 2023

The most significant external event to occur since the last valuation has been the Covid-19 pandemic. However, the analysis below shows that mortality experience was broadly as expected over the period with minimal impact on the funding position.

A significant factor which has affected the funding strategy is the Fund's better than expected investment returns. This has had a material positive impact on the funding position.

Financial

Table 5: Analysis of investment return experience between 2020 and 2023 valuations

	Expected	Actual	Difference	Impact on funding position
Investment returns				
3-year period	9.3%	28.4%	19.1%	+£1,469m
Annual	3.0% pa	8.7% pa	5.7% pa	

Membership

Table 6: Analysis of membership experience between 2020 and 2023 valuations

	Expecte d	Actual	Difference	Impact on funding position
Pre-retirement				
Early leavers	8,639	9,441	802	+£3m
Ill-health retirements	458	364	-94	+£25m
Salary increases	3.1% pa	5.4% pa	2.4% pa	-£128m
Post-retirement				
Benefit increases	1.9% pa	4.5% pa	2.5% pa	-£517m
Pension ceasing	£16.8m	£16.3m	-£0.5m	-£8m

2.4.2 Outlook

Expectations about the future, which inform the assumptions used to value the liabilities, have changed since the last valuation. The most significant changes are:

Future inflation: this is expected to be on average higher than at 2020 due to the current high level of inflation.

Investment returns: due to changes in financial markets, future investment returns are now expected to be higher than at the last valuation.

Table 7: Summary of change in outlook

Factor	What does it affect?	What's changed?	Impact on liabilities
Future investment returns	The rate at which you discount back future benefits payments (also known as the 'discount rate' assumption)	Future investment returns are anticipated to be higher than at 2020.	Decrease of £2,625m
Inflation	The rate at which pensions (both in payment and deferment) and CARE pots increase.	Significant increase in short-term future inflation expectations.	Increase of £577m
Salary increases	The rate at which future salaries will increase. This affects benefits that are still linked to final salary, ie accrued before 1 April 2015.	No material change since last valuation given competing factors, eg tighter budgetary conditions vs. strong job market and pressure from National Living Wage increases.	Increase of £30m
Current life expectancy	How long we expect most people to live for based on today's current observed mortality rates.	Slight reduction in life expectancy (not allowing for Covid-related excess deaths)	Decrease of £38m
Future improvements in life expectancy	How we expect life expectancies to change in the future.	Lower rate of improvement in life expectancy through use of updated model of future improvements, including allowance for some recent mortality experience related to the excess deaths from the Covid 19 pandemic.	Decrease of £179m

2.5 Reconciling the overall change in funding position

Tables 8 and 9 provide insight into the funding position change between 31 March 2020 and 31 March 2023. Firstly, the changes expected to happen (Table 8), which relate mostly to assets. Then the impact of actual experience (Table 9), which affects mainly the liabilities.

2.5.1 Expected development

Table 8: Expected development of funding position between 2020 and 2023 valuations

	Assets	Liabilities	Surplus/ deficit
	£m	£m	£m
31 March 2020 valuation	**7,479**	**7,071**	**408**
Cash flows			
Employer contributions paid in	586	0	586
Employee contributions paid in	162	0	162
Benefits paid out	(762)	(762)	0
Other cash flows (eg expenses, transfers in/out)	42	0	42
Expected changes			
Expected investment returns	713	0	713
Interest on benefits already accrued	0	660	(660)
Accrual of new benefits	0	881	(881)
Expected position at 31 March 2023	**8,220**	**7,850**	**370**

2.5.2 Impact of actual events

Table 9: Impact of actual events on the funding position at 31 March 2023

	Assets	Liabilities	Surplus/ deficit
	£m	£m	£m
Expected position at 1 March 2023	**7,479**	**7,071**	**370**
Events between 2020 and 2023			
Salary increases greater than expected	0	128	(128)
Benefit increases greater than expected	0	517	(517)
Early retirement strain (and contributions)	6	0	6
Ill health retirement strain	0	(25)	25
Early leavers more than expected	0	(3)	3
Other membership experience	0	(11)	11
Higher than expected investment returns	1,469	0	1,469
Changes in future expectations			
Investment returns	0	(2,625)	2,625
Inflation	0	577	(577)
Salary increases	0	30	(30)
Longevity	0	(218)	218
Other demographic assumptions	0	(52)	52
Actual position at 31 March 2023	**9,695**	**3,170**	**3,525**

Numbers may not sum due to rounding.

3 Sensitivity and risk analysis

Funding benefits that are going to be paid in the future involves risk and uncertainty. The Fund therefore maintains a risk register which is regularly reviewed. Additionally, as part of the valuation, the Fund reviews sources of risk that may impact its funding position and the contribution rates payable by employers.

This section discusses some of the most significant sources of funding risk (assumptions, regulatory, administration and governance, and climate change). Further information about the Fund's approach to funding risk management, including monitoring, mitigation, and management, is set out in the Funding Strategy Statement.

The valuation results depend on the actual assumptions made about the future. By their nature, these assumptions are uncertain which means it's important to understand their sensitivity and risk levels.

3.1 Contribution rates

The risk-based approach to setting employer contribution rates mitigates the limitation of relying on one set of assumptions. Therefore, there is no need to carry out additional analysis of the sensitivity of contribution rates to changes in financial assumptions, but they are sensitive to changes in demographic assumptions. The results in this section in relation to the funding position can be broadly applied to the contribution rates.

3.2 Funding level

3.2.1 Financial assumptions

In Section 2.2 we set out how the results vary with the assumed future investment return; here we consider inflation in Table 11.

Table 10: Sensitivity of funding position to discount rate assumption

Discount rate assumption	Surplus/Deficit	Funding level
	£m	%
4.6% pa	3,019	145%
5.2% pa	**3,525**	**157%**
5.6% pa	3,957	169%

Table 11: Sensitivity of funding position to inflation assumption

CPI assumption	Surplus/Deficit	Funding level
	£m	%
2.1% pa	3,680	161%
2.3% pa	**3,525**	**157%**
2.5% pa	3,366	153%

The main area of demographic risk is if people live longer than expected. Table 12 shows the impact of longer-term longevity rates improving at a faster pace (1.75% pa vs 1.5% pa used in the headline results).

Table 12: Sensitivity of the funding to longevity assumption

Long-term rate of improvement	Surplus/Deficit	Funding level
	£m	%
1.50% pa	3,525	157%
1.75% pa	3,497	156%

3.3 Other risks

3.3.1 Regulatory, administration and governance risks

Potential risks in this area include change in central government legislation, which alters the future cost of the LGPS, and failures in administration processes leading to incorrect data and inaccuracies in actuarial calculations. At this valuation, specific risks include:

McCloud

Benefits accrued by certain members between 2015 and 2022 may increase following the McCloud case, which ruled that transitional protections introduced in 2015 for older members were discriminatory. We've made an allowance for the cost of these potential improvements, based on the guidance issued by the Scottish Public Pensions Agency on 28 April 2023. Details are set out in guide 12 of [Hymans Robertson's LGPS 2023 valuation toolkit.](https://)

Cost sharing mechanism

Benefits could change because of the 2020 cost cap valuation; the outcome is currently unknown. We have assumed that there will be no changes required to the benefit structure due to the cost cap.

Goodwin

Benefits of certain dependent pensioners could be affected by the outcome of the Goodwin tribunal. As the remedy to this issue is still uncertain, it is difficult to identify who it would apply to. Given that its impact is estimated to be very small for an LGPS fund, we have made no allowance for this change at the 2023 valuation.

GMP Indexation

We have made an allowance for all increases on GMPs for members reaching State Pension age after 6 April 2016 by assuming that all increases will be paid for by LGPS employers in the Fund with no future support from the State (ie the worst-case scenario from an LGPS perspective). The affected members are a diminishing group, and the financial significance of this allowance will reduce over time. This is the same approach that was taken for the 2020 valuation.

3.3.2 Post-valuation events

Since 31 March 2023, there has been continued volatility in financial markets and rises in interest rates by central banks. These events affect the value of the Fund's assets and liabilities.

The Fund's investment return since 31 March 2023 is estimated to be somewhere between 0% and 5%.

Liability valuations are likely to be lower now than at 31 March 2023 due to rises in expected future investment returns and a reduction in long-term inflation expectations.

As an open scheme, with a strong covenant, the Fund takes a long-term view when considering the funding impact of such events. For employers who have a very short time horizon recent volatility may be more immediately impactful, and the Fund has engaged with these employers as appropriate.

No allowance has been made for this volatility in the valuation results or contribution rates detailed in the Rates & Adjustments Certificate. The Fund will continue to monitor changes in the financial and demographic environment as part of its ongoing risk management approach.

Page 124

3.4 Climate change

3.4.1 Background

Climate change is a major source of uncertainty which could affect future investment returns, inflation, and life expectancies. Therefore, the Fund has explicitly considered the resilience of its funding and investment strategy to future potential climate change outcomes.

It is impossible to confidently quantify the effect of climate risk given the significant uncertainty over the impact of different possible climate outcomes, as well as societal and economic impacts and adaptions. Instead, three different climate change scenarios have been considered as a stress test (instead of trying to predict how climate change affects the funding level in the future).

All the scenarios assume that there will be a period of disruption linked either to the response to climate risk (transition risks) or the effect of it (physical risks). This disruption is expected to lead to high volatility in financial markets, and the later the disruption, the more pronounced it will be.

More information about the scenarios detailed below can be found in guide 10 of Hymans Robertson's LGPS 2023 valuation toolkit.

3.4.2 Outcome of analysis

The Fund has set its funding and investment strategy using asset-liability modelling and considering two main risk metrics.

- **Likelihood of success** – the chance of being fully funded in 20 years' time.
- **Downside risk** – the average worst 5% of funding levels in 20 years' time.

When exploring the potential impact of climate change, the Fund has compared how these risk metrics change under each climate change scenario (against the 'core' model used when setting the funding and investment strategy). The stress-test results for the Fund are shown in Table 13. All results are in absolute terms.

Table 13: Modelling results with additional climate risk testing

Scenario	Likelihood of success	Downside risk
In comparison to 'core' modelling results		
Green revolution	2% higher	4% lower
Delayed transition	Marginally lower	1% higher
Head in the sand	Marginally lower	5% higher

The results are generally worse in the climate scenarios. This is to be expected given that they are purposefully stress tests, with the scenarios mainly being bad outcomes. Whilst the risk metrics are mostly weaker, they are not materially so, and not enough to suggest that the funding and investment strategy are unduly exposed to climate change risk. The Fund will continue to monitor this risk as more information emerges and climate change modelling techniques evolve.

Given the major uncertainty, it is possible that the impacts could be worse, potentially materially worse, than the 'head in the sand' scenario.

Page 125

4 Final comments

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

- The Funding Strategy Statement which, in particular, highlights how different employers in different circumstances have their contributions calculated.
- The Statement of Investment Principles, which sets out the investment strategy for the Fund.
- The general governance of the Fund, including meetings of the Pensions Committee and Local Pensions Board, decisions delegated to officers, the Fund's business plan, etc.

4.1 New employers joining the Fund

Any new employers or admission bodies joining the Fund should be referred to the Fund Actuary to assess the required level of contribution. Depending on the number of transferring members the ceding employer's rate may also need to be reviewed.

4.2 Cessation and bulk transfers

Any employer who ceases to participate in the Fund should be referred to the Fund Actuary in accordance with Regulation 61 of the LGPS regulations.

Any bulk movement of scheme members:

- involving 10 or more scheme members being transferred from or to another LGPS fund.
- involving 2 or more scheme members being transferred from or to a non-LGPS pension arrangement.

should be referred to the Fund Actuary to consider the impact on the Fund.

4.3 Valuation frequency

Under the LGPS regulations, the next formal valuation of the Fund is due to be carried out as at 31 March 2026 where contribution rates payable from 1 April 2027 will be set.

Richard Warden FFA
March 2024
For and on behalf of Hymans Robertson LLP

Julie Baillie FFA

Appendices

Page 127

Appendix 1: Data

Membership data

A summary of the membership data provided by the Fund for the 2023 valuation is set out in Table 14. The corresponding membership data from the previous valuation is also shown for reference.

The results of the valuation are dependent on the quality of the data used. We have carried out a series of validation checks on the data supplied to us by the Administering Authority to ensure that it is fit for purpose.

More information on how we verify the quality of the data used in the valuation has been shared with the Administering Authority in our report ‘ Data Report for the 2023 Valuation, dated 1 December 2023.

Asset data

To check the membership data and derive employer asset values, we have used asset and accounting data and employer level cash flow data provided by the Fund.

Table 14: Whole Fund membership data at this valuation compared with the previous valuation

Whole Fund membership data	31 March 2023	31 March 2020
Active members		
Number	37,287	34,857
Total actual pay (£000)	925,100	788,544
Total accrued pension (£000)	185,906	152,531
Average age (liability weighted)	53.7	51.8
Future working lifetime (years)	9.3	9.1
Deferred pensioners (including undecideds)		
Number	26,229	22,028
Total accrued pension (£000)	65,866	51,867
Average age (liability weighted)	52.4	50.5
Pensioners and dependants		
Number	34,069	30,953
Total pensions in payment (£000)	229,909	185,632
Average age (liability weighted)	68.5	67.3

Investment strategy

The Fund operates four investment strategies The allocations used for the calculation of employer contribution rates and to derive the future investment return assumptions are set out in Table 15 .

This information was provided by Fund Officers.

Table 15: Investment strategy allocation used for the calculation of employer contribution rates

% Allocated	Main Strategy	Medium Risk Strategy	Low Risk Strategy	Lothian Buses Strategy
UK equities	4.3%	2.1%	0.0%	2.3%
Overseas equities	54.3%	27.1%	0.0%	29.9%
Private equities	1.2%	0.6%	0.0%	0.6%
Total growth assets	59.8%	29.8%	0.0%	32.8%
Index linked gilts	10.1%	55.1%	100.0%	50.6%
Fixed interest gilts	0.5%	0.3%	0.0%	0.3%
Total protection assets	10.6%	55.4%	100.0%	50.9%
Corporate debt	1.6%	0.8%	0.0%	0.9%
Infrastructure	15.2%	7.5%	0.0%	8.3%
Private lending	2.9%	1.5%	0.0%	1.6%
Property	5.2%	2.6%	0.0%	2.9%
Total income generating assets	24.9%	12.4%	0.0%	13.7%
Cash	4.7%	2.4%	0.0%	2.6%
Total	100%	100%	100%	100%

Appendix 2: Assumptions

To set and agree assumptions for the valuation, the Fund carried out an in-depth analysis and review in June 2023. The final set of assumptions, along with the Funding Strategy Statement, was approved by the Pensions Committee in March 2024.

Financial assumptions

Setting employer contribution rates

An asset-liability model was used to set employer contributions at the 2023 valuation. This model relies on Hymans Robertson's proprietary economic model, the Economic Scenario Service (ESS). The ESS reflects the uncertainty associated with future levels of inflation and asset returns and the interactions and correlations between different asset classes and wider economic variables. In the short term (first few years), the models are fitted with current financial market expectations. Over the longer term, models are built around views of fundamental economic parameters, for example equity risk premium, credit spreads and long-term inflation. The table below shows the calibration of the ESS at 31 March 2023. Further information on the assumptions used for contribution rate setting is included in the Funding Strategy Statement.

Table 16: ESS individual asset class return distributions at 31 March 2023

Time period	Percentile	Asset class annualised total returns							Inflation/Yields		
		Cash	All World ex UK Equity	UK Equity	Index Linked Gilts (medium)	Fixed Interest Gilts (medium)	Property	Corporate Debt	Inflation (CPI)	17 year real yield (CPI)	17 year yield
10 years	16th	2.5%	1.1%	1.3%	0.8%	2.4%	1.2%	2.7%	0.9%	-0.3%	2.7%
	50th	3.6%	7.3%	7.5%	2.8%	3.7%	6.2%	4.3%	2.5%	0.9%	4.1%
	84th	4.7%	13.6%	13.5%	5.1%	4.9%	11.5%	5.8%	4.1%	2.2%	5.9%
20 years	16th	2.3%	2.8%	3.0%	1.0%	3.3%	2.7%	3.7%	0.7%	-0.5%	1.4%
	50th	3.7%	7.4%	7.5%	2.7%	4.1%	6.4%	4.7%	2.3%	1.3%	3.4%
	84th	5.4%	12.2%	12.0%	4.5%	4.8%	10.3%	5.8%	3.9%	2.9%	5.9%
40 years	16th	1.8%	3.7%	3.9%	1.0%	2.9%	3.2%	3.4%	0.6%	-0.6%	1.2%
	50th	3.5%	7.2%	7.4%	2.7%	3.7%	6.2%	4.4%	2.0%	1.3%	3.3%
	84th	5.7%	10.9%	10.9%	4.6%	4.9%	9.5%	5.8%	3.5%	3.2%	6.1%
	Volatility (5yr)	2%	18%	18%	7%	5%	15%	6%	3%	-	-

Calculating the funding level

Table 17 summarises the assumptions used to calculate the funding level at 31 March 2023, along with a comparison of assumptions at the last valuation.

Table 17: Summary of assumptions used for measuring the funding level, compared to last valuation

Assumption	31 March 2023	Required for	31 March 2020
Discount rate	5.2% pa	To place a ‘today’s money’ value on all the benefits promised to scheme members at the valuation date. The Fund’s assets are estimated to have a 75% likelihood of achieving a return that is at least equal the discount rate.	3.0% pa (based on 75% likelihood)
Benefit increases/CARE revaluation	2.3% pa	To determine the size of future benefit payments.	1.95% pa
Salary increases	3.0% pa*	To determine the size of future final-salary linked benefit payments.	2.45% pa†*

*plus a promotional salary scale
†a blended assumption of 2% pa until 2025 followed by CPI + 0.7% thereafter

Demographic assumptions

The same demographic assumptions are used to set contribution rates and to assess the current funding level.

Longevity

Table 18: Summary of longevity assumptions at this valuation compared with the previous valuation

	31 March 2023	31 March 2020
Baseline assumptions	VitaCurves based on member-level lifestyle factors	VitaCurves based on member-level lifestyle factors
Future improvements	CMI 2022 model Initial addition = 0.25% (both Male and Female) Smoothing factor = 7.0 Weighting = 0% (2020 & 2021 data), 25% (2022 data) 1.5% pa long-term rate	CMI 2019 model Initial addition = 0.5% (both Male and Female) Smoothing factor = 7.0 1.5% pa long-term rate of improvement

Other demographic assumptions

Table 19: Summary of other demographic assumptions

Death in service	See sample rates in Table 20
Retirements in ill health	See sample rates in Table 20
Withdrawals	See sample rates in Table 20
Promotional salary increases	See sample rates in Table 20
Commutation	70% of future retirements elect to exchange pension for additional tax-free cash up to HMRC limits
50:50 option	0.0% of members (uniformly distributed across the age, service and salary range) will choose the 50:50 option
Retirement age	The earliest age at which a member can retire with their benefits unreduced
Proportion married	A varying proportion of members are assumed to have a dependant at retirement or on earlier death. For example, at age 60 this is assumed to be 85% for males and 60% for females. The dependant of a male member is assumed to be 2 years younger than him and the dependant of a female member is assumed to be 3.5 years older than her.

Page 132

Sample rates for demographic assumptions

Table 20: Sample rates of male and female demographic assumptions

Males

Age	Salary scale	Death before retirement	Withdrawals		Ill health Tier 1		Ill health Tier 2	
		FT & PT	FT	PT	FT	PT	FT	PT
20	105	0.21	240.12	578.87	0.00	0.00	0.00	0.00
25	117	0.21	158.61	382.37	0.11	0.02	0.13	0.02
30	131	0.26	112.51	271.22	0.21	0.03	0.23	0.03
35	144	0.30	87.89	211.87	0.41	0.14	0.46	0.15
40	154	0.51	70.72	170.49	0.62	0.26	0.69	0.24
45	164	0.86	41.33	139.50	0.99	0.51	1.09	0.49
50	174	1.37	32.02	108.06	1.86	1.31	2.59	1.45
55	179	2.15	30.76	103.80	5.83	4.52	4.67	3.11
60	184	3.86	27.39	92.45	9.91	6.97	3.87	2.65
65	185	6.44	0.00	0.00	18.92	13.49	0.00	0.00

Females

Age	Salary scale	Death before retirement	Withdrawals		Ill health Tier 1		Ill health Tier 2	
		FT & PT	FT	PT	FT	PT	FT	PT
20	105	0.11	256.99	338.79	0.00	0.00	0.00	0.00
25	117	0.11	172.88	227.90	0.16	0.13	0.09	0.10
30	131	0.16	144.88	190.99	0.21	0.18	0.12	0.13
35	144	0.27	89.25	164.73	0.41	0.34	0.24	0.25
40	150	0.44	74.23	137.00	0.61	0.51	0.36	0.37
45	157	0.71	61.11	112.78	0.82	0.68	0.48	0.50
50	162	1.04	46.56	85.94	1.50	1.23	1.11	1.13
55	162	1.37	43.56	80.39	5.47	4.43	2.32	2.35
60	162	1.75	35.02	64.64	11.52	9.30	2.38	2.40
65	162	2.25	0.00	0.00	20.73	16.76	0.00	0.00

Figures are incidence rates per 1,000 members except salary scale.
FT and PT denoted full-time and part-time members respectively.

Appendix 3: Reliances & limitations

We have been commissioned by City of Edinburgh Council ('the Administering Authority') to carry out a full actuarial valuation of Lothian Pension Fund ('the Fund') at 31 March 2023, as required under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2018 ('the Regulations').

This report is addressed to the Administering Authority. It has been prepared by us as actuaries to the Fund and is solely for the purpose of summarising the main outcomes of the 2023 actuarial valuation. It has not been prepared for any other third party or for any other purpose. We make no representation or warranties to any third party as to the accuracy or completeness of this report, no reliance should be placed on this report by any third party and we accept no responsibility or liability to any third party in respect of it.

This summary report is the culmination of other communications in relation to the valuation, in particular:

- our 2023 valuation toolkit which sets out the methodology used when reviewing funding plans
- our paper dated 9 November 2023 which discusses the funding strategy for the Fund's stabilised employers
- our paper dated 7 June 2023 which discusses the valuation assumptions.
- our initial results report dated 1 September 2023 which outlines the whole Fund results and inter-valuation experience
- our data report dated 1 December 2023 which summarises the data used for the valuation, the approach to ensuring it is fit for purpose and any adjustments made to it during the course of the valuation
- the Funding Strategy Statement which details the approach taken to adequately fund the current and future benefits due to members.

The totality of our advice complies with the Regulations as they relate to actuarial valuations.

The following Technical Actuarial Standards apply to this advice and have been complied with where material and to a proportionate degree. They are:

- TAS100 – Principles for technical actuarial work
- TAS300 – Pensions

Hymans Robertson LLP is a limited liability partnership registered in England and Wales with registered number OC310282.

A list of members of Hymans Robertson LLP is available for inspection at One London Wall, London EC2Y 5EA, the firm's registered office. Authorised and regulated by the Financial Conduct Authority and licensed by the Institute and Faculty of Actuaries for a range of investment business activities. Hymans Robertson is a registered trademark of Hymans Robertson LLP.

Page 134

Appendix 4: Glossary

Term	Explanation
50:50 option	An option for LGPS members to pay half contributions and earn half the retirement benefit (pre-retirement protection benefits are unreduced).
Asset-liability modelling	An approach to modelling and understanding risk for a pension fund. The assets and liabilities are projected forwards into the future under many different future scenarios of inflation, investment returns and interest rates. The future scenarios are then analysed to understand the risk associated with a particular combination of contribution rates and investment strategy. Different combinations of contribution rates and/or investment strategies may be tested.
Baseline longevity	The rates of death (by age and sex) in a given group of people based on current observed data.
Club Vita	A firm of longevity experts who Hymans Roberston partner with for longevity analysis. They combine data from thousands of pension schemes and use it to create detailed baseline longevity assumptions at member-level, as well as insights on general longevity trends and future improvements.
Commutation	The option for members to exchange part of their annual pension for a one-off lump sum at retirement. In the LGPS, every £1 of pension exchanged gives the member £12 of lump sum. The amounts that members commute is heavily influenced by tax rules which set an upper limit on how much lump sum can be taken tax-free.
CPI inflation	The annual rate of change of the Consumer Prices Index (CPI). The CPI is the UK government's preferred measure of inflation and is the measure used to increase LGPS (and all other public sector pension scheme) benefits each year.
Deferred pensioner	A former employee who has left employment (or opted out of the pension fund) but is not yet in receipt of their benefits from the fund.
Demographic assumptions	Assumptions concerned with member and employer choices rather than macroeconomic or financial factors. For example, retirement age or promotional salary scales. Demographic assumptions typically determine the timing of benefit payments.

Term	Explanation
Discount rate	An assumption for the annual rate of future investment return. Used to place a single 'today's money' value on a stream of future payments.
Active member	A member who is currently employed by employers who participate in the Fund and are paying contributions into the Fund.
ESS	Economic Scenario Service - Hymans Robertson's proprietary economic scenario generator used to create thousands of simulations of future inflation, asset class returns and interest rates.
Funding position	The extent to which the assets held by the Fund at 31 March 2023 cover the accrued benefits ie the liabilities. The two measures of the funding position are: • the funding level - the ratio of assets to liabilities; and • the funding surplus/deficit - the difference between the asset and liabilities values.
Inflation	Prices tend to increase over time, which is called inflation. Inflation is measured in different ways, using a different 'basket' of goods and mathematical formulas.
Liabilities	An employer's liability value is the single value at a given point in time of all the benefit payments expected to be made in future to all members. Benefit payments are projected using demographic and financial assumptions and the liability is calculated using a discount rate.
Longevity improvements	An assumption about how rates of death will change in future. Typically, we assume that death rates will fall and life expectancies will improve over time, continuing the long-running trend.
Pensioner	A former employee who is in receipt of their benefits from the fund. This category includes eligible dependants of the former employee.
Primary rate	The estimated cost of future benefits, expressed in percentage of pay terms. The primary rate will include an allowance to cover the Fund's expenses.

Term	Explanation
Prudence	To be prudent means to err on the side of caution in the overall set of assumptions. We build prudence into the choice of discount rate by choosing an assumption with a prudence level of more than 50%. All other assumptions aim to be best estimate.
Prudence level	A percentage indicating the likelihood that the assumed rate of investment return will be achieved in practice, based on the ESS model. The higher the prudence level, the more prudent the assumed rate of investment return.
Secondary rate	An adjustment to the primary rate, generally to reflect costs associated with benefits that have already been earned up to the valuation date. This may be expressed as a percentage of pay and/or monetary amount.
Withdrawal	Refers to members leaving the scheme before retirement. These members retain an entitlement to an LGPS pension when they retire but are no longer earning new benefits.

Appendix 5: Rates and Adjustments Certificate

In accordance with Regulation 60(4) of the Regulations, we have assessed the contributions that should be paid into the Fund by participating employers for the period 1 April 2024 to 31 March 2027 to maintain the solvency of the Fund.

The method and assumptions used to calculate the contributions set out in this Rates and Adjustments Certificate are detailed in the Funding Strategy Statement dated March 2024 and in Appendix 2 of the report on the actuarial valuation dated March 2024. These assumptions underpin our estimate of the number of members who will become entitled to a payment of pensions under the provisions of the LGPS and the amount of liabilities arising in respect of such members.

Table 21 summarises the whole Fund primary and secondary contribution rates for the period 1 April 2024 to 31 March 2027. The primary rate is the payroll weighted average of the underlying individual employer primary rates and the secondary rate is the total of the underlying individual employer secondary rates, calculated in accordance with the LGPS regulations and CIPFA guidance. The secondary rate has been shown both as a monetary amount and an equivalent percentage of the projected pensionable pay.

Table 21: Whole fund primary and secondary contribution rates from 1 April 2024 to 31 March 2027

This valuation (31 March 2023)		
Primary rate	25.0% of pay	
Secondary rate	**Monetary amount**	**Equivalent to % of payroll**
2024/25	-£73,589,000	-7.5%
2025/26	-£75,809,000	-7.5%
2026/27	-£78,095,000	-7.5%

The required minimum contribution rates for each employer in the Fund are set out in the remainder of this certificate.

Richard Warden FFA
Julie Baillie FFA
March 2024
For and on behalf of Hymans Robertson LLP

Employer code	Employer name	Primary rate (% of pay)	Secondary rate (% of pay)			Total contributions (Primary rate plus secondary rate)			Notes
			2024/25	2025/26	2026/27	2024/25	2025/26	2026/27	
Scheduled/Contribution Stability Mechanism Bodies (Main Investment Strategy)									
Pool	The City of Edinburgh Council	24.3%	-6.7%	-6.7%	-6.7%	17.6%	17.6%	17.6%	
Pool	Midlothian Council	24.3%	-6.7%	-6.7%	-6.7%	17.6%	17.6%	17.6%	
Pool	West Lothian Council	24.2%	-6.6%	-6.6%	-6.6%	17.6%	17.6%	17.6%	
Pool	East Lothian Council	24.3%	-6.7%	-6.7%	-6.7%	17.6%	17.6%	17.6%	
Pool	Scottish Police Authority	27.5%	-9.9%	-9.9%	-9.9%	17.6%	17.6%	17.6%	
Pool	Heriot-Watt University	25.9%	-8.3%	-8.3%	-8.3%	17.6%	17.6%	17.6%	
Pool	Edinburgh College	29.9%	-12.3%	-12.3%	-12.3%	17.6%	17.6%	17.6%	
21	Audit Scotland	29.2%	-11.6%	-11.6%	-11.6%	17.6%	17.6%	17.6%	
30	Queen Margaret University	25.6%	-8.0%	-8.0%	-8.0%	17.6%	17.6%	17.6%	
51	Edinburgh Napier University	25.4%	-7.8%	-7.8%	-7.8%	17.6%	17.6%	17.6%	
105	West Lothian College	30.4%	-12.8%	-12.8%	-12.8%	17.6%	17.6%	17.6%	
134	Lothian Valuation Joint Board	24.3%	-6.7%	-6.7%	-6.7%	17.6%	17.6%	17.6%	
135	Scottish Water	23.8%	-6.2%	-6.2%	-6.2%	17.6%	17.6%	17.6%	
155	Visit Scotland	29.8%	-12.2%	-12.2%	-12.2%	17.6%	17.6%	17.6%	
209	SESTRAN	30.6%	-3.8%	-3.8%	-3.8%	26.8%	26.8%	26.8%	
210	Improvement Service	29.2%	-11.6%	-11.6%	-11.6%	17.6%	17.6%	17.6%	
218	Scottish Futures Trust	26.5%	-8.9%	-8.9%	-8.9%	17.6%	17.6%	17.6%	
899	Scottish Fire and Rescue Service	27.6%	-10.0%	-10.0%	-10.0%	17.6%	17.6%	17.6%	

Employer code	Employer name	Primary rate (% of pay)	Secondary rate (% of pay)			Total contributions (Primary rate plus secondary rate)			Notes
			2024/25	2025/26	2026/27	2024/25	2025/26	2026/27	
Lothian Buses (Buses Investment Strategy)									
900	Lothian Buses	29.2%	-19.3%	-19.3%	-19.3%	9.9%	9.9%	9.9%	
Transferee Admission Bodies (Main Investment Strategy)									
139	CGI	34.3%	-34.3%	-34.3%	-34.3%	0.0%	0.0%	0.0%	
140	Dacoll	37.0%	-37.0%	-37.0%	-37.0%	0.0%	0.0%	0.0%	
200	Forth & Oban Ltd	30.9%	-18.9%	-18.9%	-18.9%	12.0%	12.0%	12.0%	
207	LPFE Limited	22.9%	-4.8%	-4.8%	-4.8%	18.1%	18.1%	18.1%	
212	Skanska	38.0%	-38.0%	-38.0%	-38.0%	0.0%	0.0%	0.0%	
214	NSL Services Group	38.4%	-38.4%	-38.4%	-38.4%	0.0%	0.0%	0.0%	
220	Mitie PFI CEC PP2	33.4%	-33.4%	-33.4%	-33.4%	0.0%	0.0%	0.0%	
222	Compass-Chartwell	42.3%	-42.3%	-42.3%	-42.3%	0.0%	0.0%	0.0%	
224	BaxterStorey	38.3%	-38.3%	-38.3%	-38.3%	0.0%	0.0%	0.0%	
225	Bellrock	27.5%	-20.1%	-20.1%	-20.1%	7.4%	7.4%	7.4%	
227	Sodexo Ltd	38.6%	-38.6%	-38.6%	-38.6%	0.0%	0.0%	0.0%	
228	BEAR	38.0%	-38.0%	-38.0%	-38.0%	0.0%	0.0%	0.0%	
Open Community Admission Bodies (Main Investment Strategy)									
Pool	Canongate Youth Project	25.6%	-10.0%	-10.0%	-10.0%	15.6%	15.6%	15.6%	
15	Newbattle College	33.7%	-19.8%	-19.8%	-19.8%	13.9%	13.9%	13.9%	

Employer code	Employer name	Primary rate (% of pay)	Secondary rate (% of pay)			Total contributions (Primary rate plus secondary rate)			Notes
			2024/25	2025/26	2026/27	2024/25	2025/26	2026/27	
28	Convention of Scottish Local Authorities	25.2%	1.8%	1.8%	1.8%	27.0%	27.0%	27.0%	
46	Museums Galleries Scotland	25.0%	-5.6%	-5.6%	-5.6%	19.4%	19.4%	19.4%	
64	Citadel Youth Centre	25.7%	-6.4%	-6.4%	-6.4%	19.3%	19.3%	19.3%	
87	Family Advice & Information Resource	26.2%	-1.8%	-1.8%	-1.8%	24.4%	24.4%	24.4%	
90	Handicabs (Lothian) Limited	27.2%	-9.4%	-9.4%	-9.4%	17.8%	17.8%	17.8%	
117	Scottish Schools Education Research	25.3%	1.0%	1.0%	1.0%	26.3%	26.3%	26.3%	
121	Edinburgh Development Group	27.3%	-7.4%	-7.4%	-7.4%	19.9%	19.9%	19.9%	
123	Scottish Adoption Agency	26.9%	-1.5%	-1.5%	-1.5%	25.4%	25.4%	25.4%	
133	Children's Hospice Association Scotland	25.8%	-7.8%	-7.8%	-7.8%	18.0%	18.0%	18.0%	
143	First Step	26.4%	-8.1%	-8.1%	-8.1%	18.3%	18.3%	18.3%	
147	Melville Housing Association	32.7%	-9.0%	-9.0%	-9.0%	23.7%	23.7%	23.7%	
154	St Andrew's Children's Society Limited	27.2%	-7.8%	-7.8%	-7.8%	19.4%	19.4%	19.4%	
157	West Lothian Leisure	27.5%	-11.3%	-11.3%	-11.3%	16.2%	16.2%	16.2%	
172	Homes for Life Housing Partnership	26.4%	-5.8%	-5.8%	-5.8%	20.6%	20.6%	20.6%	
174	Capital City Partnership	25.0%	-6.2%	-6.2%	-6.2%	18.8%	18.8%	18.8%	
196	HWU Students Association	25.2%	-8.0%	-8.0%	-8.0%	17.2%	17.2%	17.2%	
219	Enjoy East Lothian	24.0%	-7.4%	-7.4%	-7.4%	16.6%	16.6%	16.6%	

Employer code	Employer name	Primary rate (% of pay)	Secondary rate (% of pay)			Total contributions (Primary rate plus secondary rate)			Notes
			2024/25	2025/26	2026/27	2024/25	2025/26	2026/27	
223	Children's Hearings Scotland	25.6%	-8.4%	-8.4%	-8.4%	17.2%	17.2%	17.2%	
Closed Community Admission Bodies (Main Investment Strategy)									
78	ELCAP	23.2%	-23.2%	-23.2%	-23.2%	0.0%	0.0%	0.0%	
118	Royal Edinburgh Military Tattoo	33.8%	-10.8%	-10.8%	-10.8%	23.0%	23.0%	23.0%	
159	Edinburgh Leisure	27.1%	-27.1%	-27.1%	-27.1%	0.0%	0.0%	0.0%	
193	Health in Mind	31.4%	-31.4%	-31.4%	-31.4%	0.0%	0.0%	0.0%	
Closed Community Admission Bodies (Medium Risk Investment Strategy)									
9	University of Edinburgh (E.C.A.)	23.4%	0.0%	0.0%	0.0%	23.4%	23.4%	23.4%	
104	SRUC	35.2%	7.3%	7.3%	7.3%	42.5%	42.5%	42.5%	
158	Royal Society of Edinburgh	20.4%	0.0%	0.0%	0.0%	20.4%	20.4%	20.4%	
Closed Community Admission Bodies (Low Risk Investment Strategy)									
89	North Edinburgh Dementia Care	29.2%	-16.2%	-16.2%	-16.2%	13.0%	13.0%	13.0%	
173	Pilton Equalities Project	30.2%	-30.2%	-30.2%	-30.2%	0.0%	0.0%	0.0%	

Page 142

Further comments to the Rates & Adjustments Certificate

- Contributions expressed as a percentage of payroll should be paid into the Fund at a frequency in accordance with the requirements of the Regulations.
- Further sums should be paid to the Fund to meet the costs of any early retirements and/or augmentations or salary growth strains using methods and factors issued by us from time to time or as otherwise agreed.
- Payments may be required to be made to the Fund by employers to meet the capital costs of any ill-health retirements that exceed those allowed for within our assumptions. If an employer has ill health liability insurance in place with a suitable insurer and provides satisfactory evidence to the Administering Authority, then their certified contribution rate may be reduced by the value of their insurance premium, for the period the insurance is in place.
- The certified contribution rates represent the **minimum** level of contributions to be paid. Employing authorities may pay further amounts at any time and future periodic contributions may be adjusted on a basis approved by the Fund Actuary.

Appendix 6: Section 13 dashboard

Metric	Unit	2023 Valuation
2023 funding position – local funding basis		
Funding level (assets/liabilities)	%	157%
Funding level (change since previous valuation)	%	51% increase
Asset value used at the valuation	£m	9,695
Value of liabilities (including McCloud liability)	£m	6,170
Surplus (deficit)	£m	3,525
Discount rate (past service)	% pa	5.2%
Discount rate (future service)	% pa	Past service and future service are consistently valued with the same underlying assumptions, methodologies, and models regarding future expected levels of inflation, interest rates and investment returns.
Assumed pension increase (CPI)	% pa	2.3%
Method of derivation of discount rate, plus any changes since previous valuation		There is a 75% likelihood that the Fund's assets will return at least 5.2% over the 20 years following the 2023 valuation date. The same methodology and likelihood was used for the 2020 valuation.

Metric	Unit	2023 Valuation
Assumed life expectancy at age 65		
Life expectancy for current pensioners – men age 65	Years	20.3
Life expectancy for current pensioners – women age 65	Years	23.1
Life expectancy for future pensioners – men age 45	Years	21.6
Life expectancy for future pensioners – women age 45	Years	24.8
Past service funding position – SAB basis (for comparison purposes only)		
Market value of assets	£m	9,695
Value of liabilities	£m	6,985
Funding level on SAB basis (assets/liabilities)	%	139%
Funding level on SAB basis (change since last valuation)	%	6% increase

Metric	Unit	2023 Valuation	2020 Valuation
Contribution rates payable			
Primary contribution rate	% of pay	25.0%	23.1%
Secondary contribution rate (cash amounts in each year in line with CIPFA guidance)			
1st year of rates and adjustments certificate	£m	-73.589	-11.262
2nd year of rates and adjustments certificate	£m	-75.809	-11.378
3rd year of rates and adjustments certificate	£m	-78.095	-11.530
Giving total expected contributions			
1st year (£ figure based on assumed payroll)	£m	171.442	179.980
2nd year (£ figure based on assumed payroll)	£m	176.613	184.577
3rd year (£ figure based on assumed payroll)	£m	181.940	189.254
Assumed payroll (cash amounts in each year)			
1st year rates and adjustments certificate	£m	981.644	827.889
2nd year rates and adjustments certificate	£m	1,011.251	848.291
3rd year rates and adjustments certificate	£m	1,041.752	869.196
Three-year average	% of pay	21.8%	17.5%
Average employee contribution	% of pay	6.2%	6.3%
Employee contribution rate (£ figure based on assumed payroll of £981.644m)	£m pa	60.4	51.3

Metric	Unit	2023 Valuation	2020 Valuation
Deficit recovery and surplus spending plan			
Latest deficit recovery period end date, where this methodology is used by the fund's actuarial advisor.	Year	Methodology not used	Methodology not used
Earliest surplus spreading period end date, where this methodology is used by the fund's actuarial advisor.	Year	Methodology not used	Methodology not used
The time horizon end date, where this methodology is used by the fund's actuarial advisor	Year	2043	2040
The funding plan's likelihood of success, where this methodology is used by the fund's actuarial advisor.	%	75%	75%
Percentage of liabilities relating to employers with deficit recovery periods of longer than 20 years	%	0%	0%
Additional information			
Percentage of total liabilities that are in respect of Tier 3 employers	%	10%	10%
Included climate change analysis/comments in the 2023 valuation report		Yes	Not applicable
Value of McCloud liability in the 2023 valuation report (on local funding basis)	£m	37.3	Not applicable

by virtue of paragraph(s) 1, 3, 6 of Part 1 of Schedule 7A
of the Local Government(Scotland) Act 1973.

Document is Restricted

This page is intentionally left blank

Appendix 3

Lothian Pension Fund – Managing climate risk

Background

Climate change is a material risk to the fund. It has the potential to significantly disrupt financial markets and economic systems and affect the life expectancy of the fund's members.

Tackling climate change is a global challenge. However, as a holder of significant financial capital, the fund recognises that it has a role to play in the transition to a greener economy. The fund also recognises the need to manage the risks that climate change brings to its funding and investment strategies.

This paper outlines the strategic measures that the fund has taken to tackle climate risk. There are also comments on future developments that are underway, using fresh insights from climate science as it continues to evolve.

1. Funding strategy

1.1 Primary objective

The fund is required to meet all benefit payments as they fall due. Triennial actuarial valuations are used to review and adjust employer contribution rates to meet this objective, after allowing for prudent estimates of future expected investment returns.

1.2 How could climate change affect the funding strategy?

Climate change presents different risks to the funding strategy:

- *Lower economic growth and investment returns* – tackling climate change will require significant capital investment. This may reduce growth and returns on assets during the transition to a greener economy.
- *More climate events* – 'extreme' events, such as heatwaves or flooding, are likely to increase in frequency and adversely affect stock markets and asset valuations.
- *Increased volatility/uncertainty* – the pace of transition to a greener economy is highly uncertain. Financial markets and other economic indicators, such as interest rates and inflation, are likely to be more volatile and unpredictable due to the uncertainty.
- *Life expectancy* – climate change can affect human health and the longevity of the fund's members, possibly either positively or negatively.

1.3 What measures are the fund currently using to manage climate risk?

The 2023 triennial valuation was an opportunity for the fund to review how it manages all key risks and build controls into its Funding Strategy Statement. Climate risk was tackled from two angles.

a) Risk budgeting

With a significant surplus being reported at the 2023 valuation, analysis and modelling was undertaken to 'stress test' the funding position under a range of future contribution scenarios and investment strategies, and scenarios with a sudden permanent loss of assets ('asset shocks'). This provided a risk budget to help fund officers and committee to understand how robust the funding strategy was to future adverse experience, and to make decisions **about the fund's approach to setting employer contribution rates.**

The fund recognised that it was unrealistic and unaffordable for contribution rates to directly target the cost of extreme climate events. Instead, it was agreed to build in extra protection over time against the cost of climate-induced risks. Using the risk budget information, the fund added prudence into its funding strategy by:

- Increasing the confidence level – the 'likelihood of funding success' parameter under the risk-based valuation approach was raised from a minimum of 67% (for some scheduled bodies) at the 2020 valuation to a minimum of 80% across all employers.
- Applying an asset shock – employer assets at the valuation were reduced by 20% for the purpose of determining contribution rates.

Both measures retain money in the fund to hold as shock absorbers against future poor experience. In addition to managing uncertainty around climate risk, they act as a buffer against other 'tail' risks in the modelling, such as geopolitical concerns, or rapid reductions in interest rates.

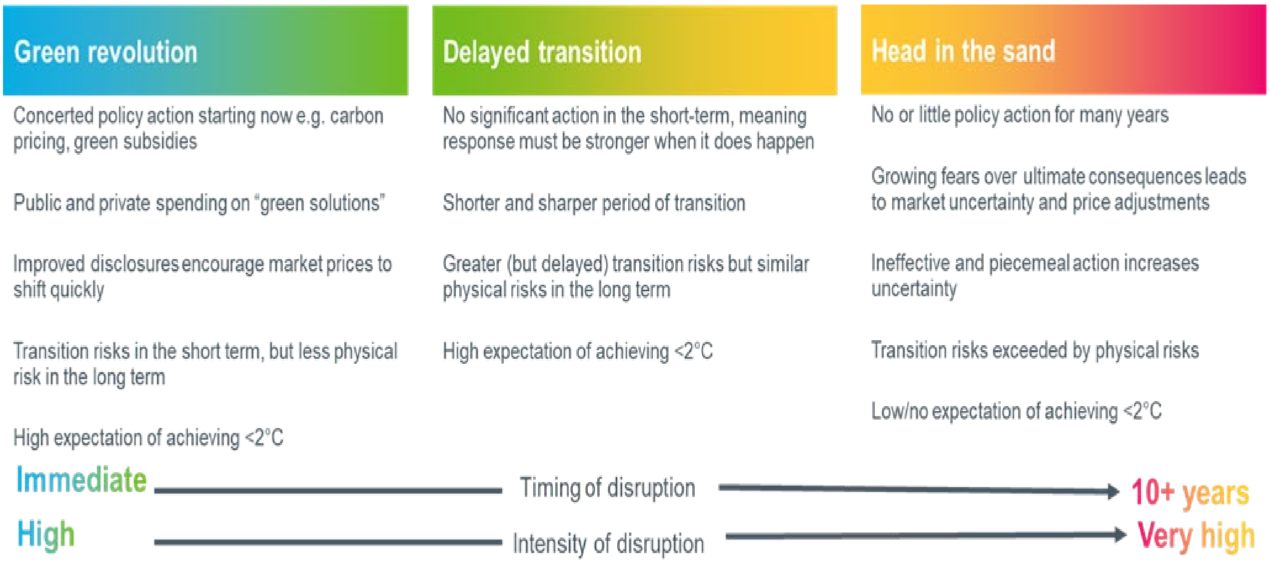
Whilst these measures are prudent and make the fund more resilient to climate risk, the three-yearly valuation process also offers the opportunity to review the funding strategy and make changes in reaction to evolving circumstances eg to recent research from the actuarial profession and other bodies that suggests that modelling techniques may be underestimating the impacts of extreme climate events. The funding strategy ultimate relies on the ability of the fund's employers to pay contributions so that the fund can pay pensions. Overall, the fund's employers have a strong financial covenant and a low risk of failing.

b) Climate scenario modelling

Description of climate scenarios

The impact of climate change is too uncertain to build directly into the valuation modelling. Instead, the results of the core valuation model were 'stress tested' under three different climate change scenarios. This was intended to test the resilience of the modelling, as required under Task Force on Climate-Related Financial Disclosures (TCFD), rather than rerunning the full analysis.

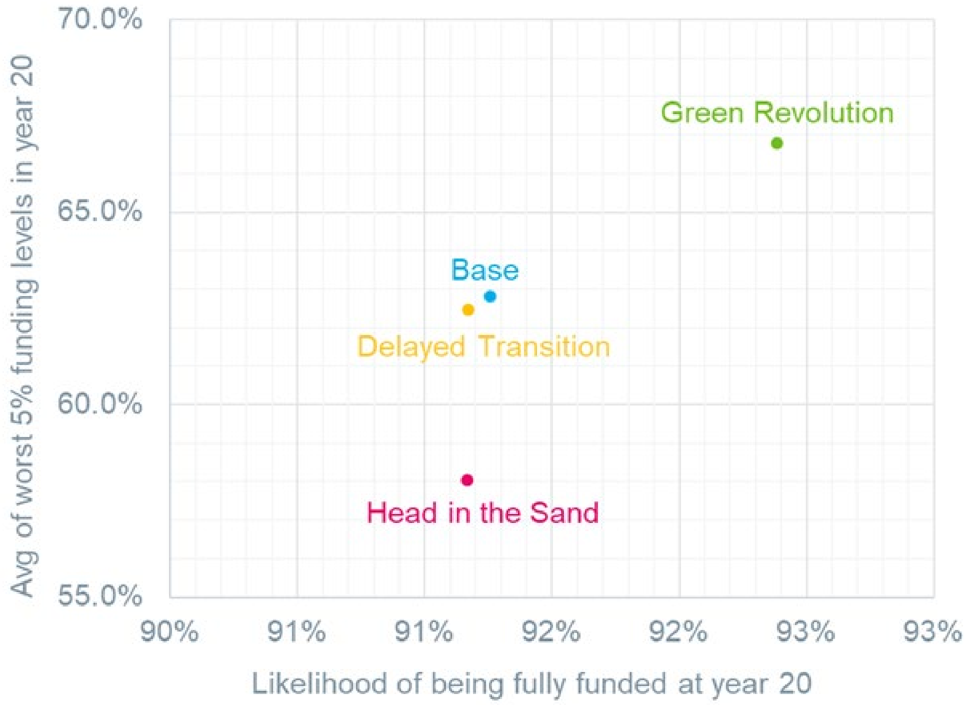
The three climate scenarios considered had differing speeds and strengths of response on climate transition:



Each scenario assumed a period of disruption linked either to the impact of measures to combat climate change (transition risks) or to the fallout from it (physical risks), with the disruption leading to high volatility in financial markets and economic variables such as inflation. The later the period of disruption, the more pronounced it would be.

Stress test results for the fund

The three climate scenarios were stress tested against the results of the core valuation modelling (referred to as the 'Base' scenario). The following chart, which assumes a fixed contribution rate of 20% of pay for modelling purposes, summarises the results:



The chart shows that:

- On the upside, the likelihood of the fund being fully funded in 20 years' time remains high, with little movement in the likelihood percentages across the different scenarios.
- However, on the downside, the differences are more marked. There is less downside risk under the 'Green Revolution' scenario (an average worst-case funding level of 67% at year 20) compared to the 'Base' (63%) and 'Delayed Transition' (62%) scenarios. The downside risk worsens under the 'Head in the Sand' scenario (58%).

Whilst the results differ across scenarios, the differences are not sufficiently material to suggest that the fund's strategy is not resilient to climate change risk. Or, put another way, the results provide assurance that the core valuation model does not appear to be significantly underestimating climate risk. However, it is important to monitor the risk and how it may evolve (see next section). This illustrative modelling uses a fixed contribution rate of 20.0% for 20 years. In practice, the fund would respond to a changing funding environment by varying the employer contributions at each valuation.

1.4. Future measures to manage climate risk

Section 1.3 discussed the measures taken at the 2023 valuation to manage climate risk. Climate science is, however, a rapidly evolving area. Further work is already underway to enhance the information available to the fund for decision making. This is outlined below and will become available during 2024, giving time for officers and the committee to consider ahead of the 2026 valuation.

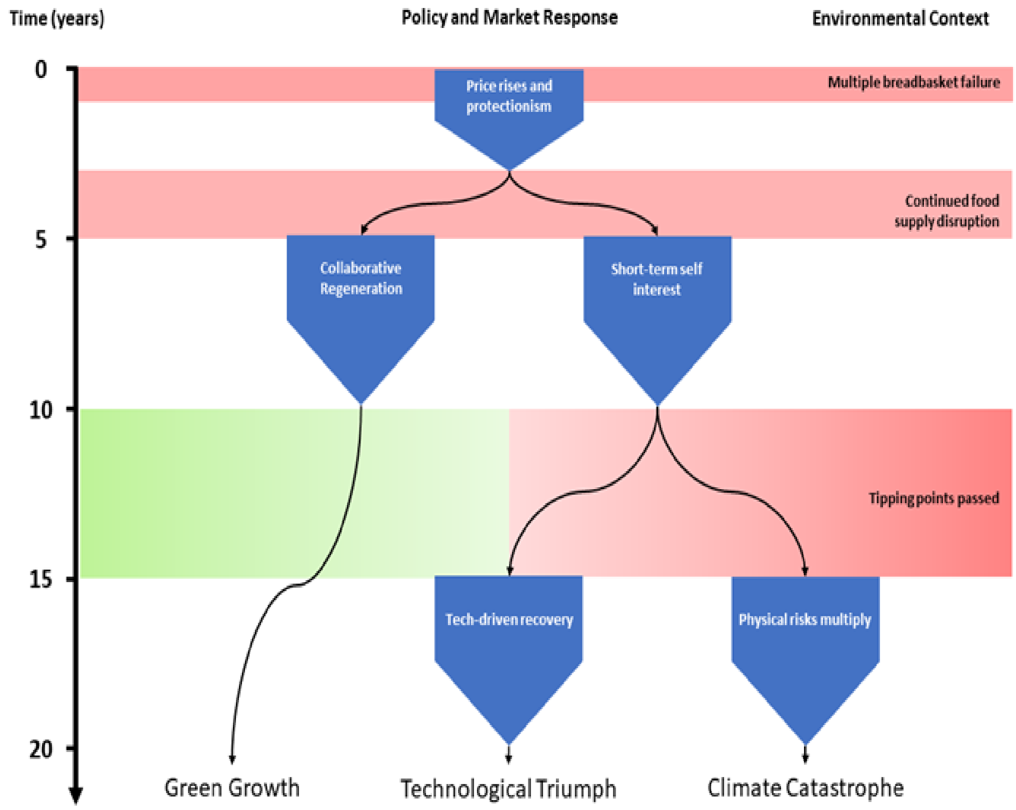
a) Narrative-based climate modelling

The approach at the 2023 valuation stress tested the core model and explored what outcomes might arise if we took account of greater variability. However, it didn't provide detail of what may be going on underneath. Furthermore, when developing climate scenarios, past data may be of limited value. There is no guarantee that the traditional relationships between economic variables will hold under extreme climate change.

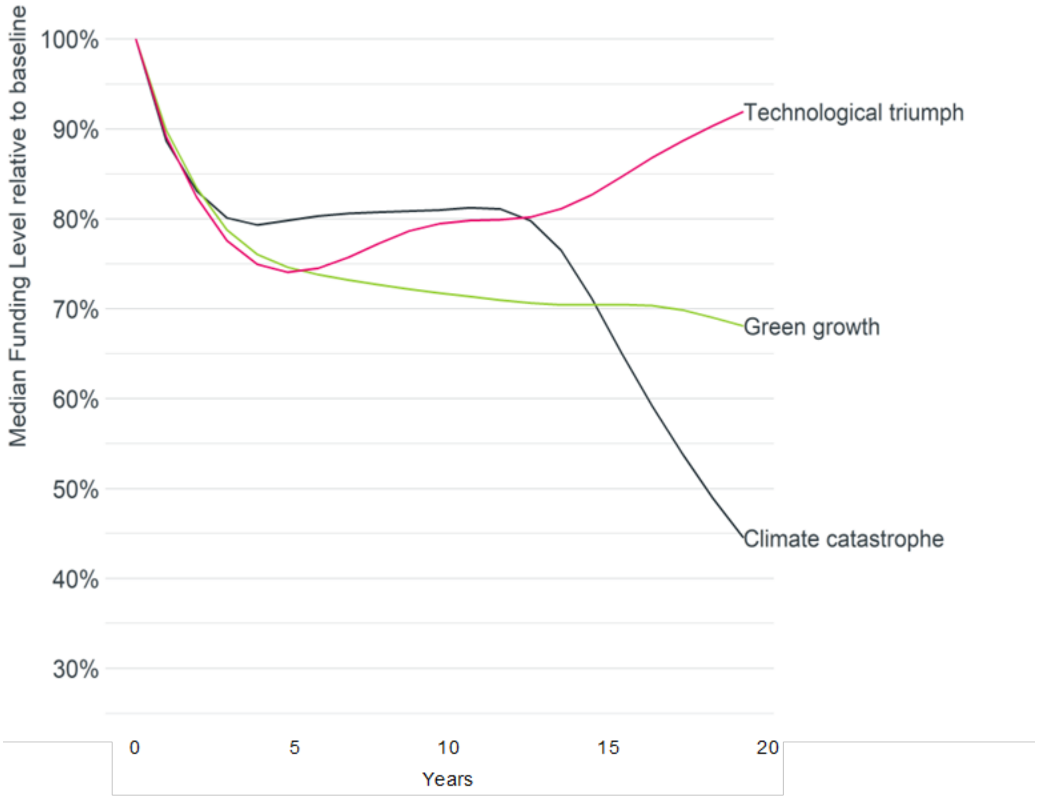
When developing more realistic and useful climate scenarios, consideration needs to be given to how different actors within our global system respond to stress. This adds in the 'human response' i.e. it recognises that different entities may not always take decisions that lead to an optimal outcome. In particular, the actions of global powerhouses such as the EU, China and the US will be influenced by other risk factors and could lead to unexpected outcomes. The risk drivers that are likely to influence policymakers are:

- Environmental severity and feedback
- Energy usage
- Technology progression
- Social policies and adaptation
- Geopolitical tension

Our real-world climate narrative scenario assumes an extreme event acts as a catalyst, changing the dynamics of the global economy. For example, a climate-induced food shock, where adverse weather in a small number of breadbasket regions that produce a disproportionate amount of the world's food leads to chronic crop failures. The diagram below explores the narrative in a step-wise manner, moving along each pathway from the initial catalyst, through two possible medium-term responses and on to potential long-term outcomes.



An example of the output available from this narrative modelling is shown below, based on data from the fund's 2023 valuation. This summarises the impact of our scenario on funding levels, relative to our baseline assumptions. It reports changes in the median funding level along each pathway as a proportion of the baseline median funding level, highlighting the downside risks associated with the scenario. However, care should also be taken when interpreting this output as it omits uncertainty associated with funding levels by focussing on the median outcomes only.



Current climate science provides confidence that scenarios such as this are more likely, but we can't say how much more likely. The broad-ranging nature of the scenarios, and the breadth of possibilities for the nature of the shock, suggest that the risks are "undiversifiable". i.e. they aren't specific to only those entities which seem to be obviously relevant to climate change, rather they are relevant to all entities.

b) Longevity modelling

The fund uses Club Vita, a longevity data analytics company, to help its actuary to set life expectancy assumptions.

Vita produced 'Hot and Bothered?' research in 2018 which examined the impact of climate change on longevity patterns across the same three climate scenarios mentioned in section 1.3 above. The diagram below summarises the research.

This was provided with indicative life expectancies and liability impacts to help funds to stress test their funding plans.

With climate change scenario modelling moving on in recent years, Vita are refreshing their research. Whilst the key features of each scenario will be retained, updates will be made by:

- Allowing for observed longevity experience since 2018
- Refreshing the time horizons and potential magnitude of impacts in light of global events, pledges and initiatives since 2018. For example, allowance will be made for the world being off-track on reaching the target of the Paris Agreement.
- Reflecting the direct impact of Covid-19 on mortality levels, and the potential impact of vector-borne diseases in general.

2. Investment strategy

The Statement of Investment Principles guides the fund's investment objectives and policies including high-level strategic asset allocation decisions which define risk and return objectives and that owning a diversified portfolio of assets reduces exposure to any particular contingency. The SIP confirms that whilst the fund's fiduciary duty is the pursuit of financial returns, non-financial considerations can be taken into account, that exercising ownership rights in a responsible way can reduce risk and may improve returns.

The supplementary Statement of Responsible Investment Principles (SRIP) expands on this, highlights the importance of the Paris Agreement of the United Nations Framework Convention on Climate Change, and the risks and opportunities for the fund and sets out a series of commitments to climate monitoring and action.

The methodology used in the valuation considers expected returns and volatilities of asset classes in future but cannot directly model the impacts of climate risk at asset class or geographic level. This same modelling is used to set the strategic asset allocation and for the investment strategy and cannot enable direct capture of investment risk and opportunity at this granular level.

Therefore, the investment strategy, more accurately the strategic asset allocation, is not directly impacted by nor account for the recognition of climate change risk. This undiversifiable and unhedgeable risk this can only be recognised by adopting a more prudent funding strategy and as set out above has been. Even then, the tail risk ie the low likelihood/high impact outcomes cannot be allowed for within an acceptable funding strategy.

The implementation of the investment strategy involves making decisions at the level of stock, bond, property and transaction level. Each decision needs to take account of the full range of risks and opportunities and an assessment of the expected risk adjusted return. Diversification across geographies, industries and investment is intended to reduce both idiosyncratic and systemic risk and provide the expected long-term return required to support the funding assumptions and contribution levels.

The investment holdings will evolve over time seeking to earn an appropriate return for the risks incurred as companies and economies evolve and adapt. Throughout this period the portfolio managers will seek to engage with companies, partner funds and organisations in line with the SRIP to meet the fund’s objectives as a good steward of capital whilst seeking an appropriate risk adjusted investment return and enable the Committee to meet it’s fiduciary duty.

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Actuarial Valuation for Scottish Homes Pension Fund

Item number 6.5

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 Note the results of the 2023 actuarial valuation for the Scottish Homes Pension Fund;

1.2 Note that the funding level of the Scottish Homes Pension Fund at 31 March 2023 was 127%. This Actual Funding Level (AFL) of 127% is greater than the Target Funding level (TFL) of 95.5%, as specified in the Scottish Government Guarantee. Therefore, no deficit contributions are required from the Scottish Government (as Guarantor) for the period form 1 April 2024 to 31 March 2027; and

1.3 Note that the Scottish Government is required to paya total of £90,000 per annum towards the cost of administration expenses over the three years from 1 April 2024 to 31 March 2027.

Alan Sievewright

Chief Finance Officer, Lothian Pension Fund

Contact: Erin Savage, Senior Pensions Employer and Member Manager, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Actuarial Valuation for Scottish Homes Pension Fund

2. Executive Summary

2.1 An actuarial valuation of the Scottish Homes Pension Fund must be carried out every three years. The fund's actuary assesses the financial health of the fund and sets the employer contribution rates required for the next three years.

2.2 This report presents the results of the actuarial valuation of the Scottish Homes Pension Fund as at 31 March 2023.

2.3 The funding level at 31 March 2023 was 127%, an improvement from 118% at the 2020 actuarial valuation. The Actual Funding Level (AFL) of 127% is greater than the Target Funding Level (TFL) of 95.5% specified in the Scottish Government Guarantee. Therefore, no deficit contributions are required from the Scottish Government (as Guarantor) for the period 1 April 2024 to 31 March 2027.

2.4 The Scottish Government is however, required to pay £90,000 per annum towards the cost of administration expenses for the three years from 1 April 2024 to 31 March 2027

3. Background

3.1 The City of Edinburgh Council took over the administration of the deferred and pensioner liabilities of the Scottish Homes Pension Fund on 1 July 2005. An agreement between the Scottish Government and the City of Edinburgh Council ('the Guarantee') was put in place in June 2005. The Scottish Government acts as the guarantor for these liabilities.

3.2 An actuarial valuation of the Scottish Homes Pension Fund must, by law take place every three years. The 2023 valuation is based on data as at 31 March 2023 and must be completed by 31 March 2024.

3.3 The actuarial valuation of a pension fund has three main purposes:

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

3.4 The funding strategy for the Scottish Homes Pension Fund and the valuation methodology is set out in the Guarantee. The strategy assesses the funding level using prudent financial assumptions and sets target funding levels for the fund at each actuarial valuation. It is designed to reduce investment risk as the fund is closed to new entrants and the liabilities will mature over time. It also sets out the conditions which will trigger contributions to be payable by the Scottish Government.

3.5 At a funding level in excess of 100%, the Guarantee requires that investments should be fully invested in index-linked gilts to reduce funding level volatility and 'lock-in' the surplus. It should be noticed however, that whilst this represents a low-risk investment strategy, index-linked gilts cannot provide an exact match for the liabilities and longevity risks remain.

3.6 The Guarantee is included at Appendix 2.

4. Main Report

4.1 The 2023 Actuarial Valuation report is included at Appendix 1.

4.2 Liability cashflows (projected benefit benefits) have been estimated based on financial and demographic assumptions, as detailed in the report.

4.3 The table below summarises the financial position of the fund at 31 March 2023, with the result of the 2020 formal valuation shown for comparison.

Valuation Date	2023	2020
	£M	**£M**
Past Service Liabilities	99	141
Assets	126	166
Surplus/(Deficit)	27	25
Actual Funding Level	**127%**	**118%**
Target Funding Level	**95.5%**	**94.5%**

4.4 The valuation includes the assets and liabilities of Homeless Action Scotland which transferred into the Scottish Homes Pension Fund following its exit from Lothian Pension Fund on 12 July 2018.

4.5 With an actual funding level in excess of 100%, the investment strategy of the fund is to be fully invested in index-linked gilts in accordance with the Scottish Government guarantee.

4.6 The TFL, as set out in the Guarantee is 95.5% at 31 March 2023. The AFL is greater than the TFL at the 2023 valuation date, and therefore no deficit contributions are required from the Scottish Government for the period 1 April 2024 to 31 March 2027.

4.7 The Guarantor should however, meet the cost of administration expenses. The CIPFA definition of costs includes:

- Oversight and Governance;
- Administration; and
- Investment Management.

4.8 Following consideration of administration and oversight and governance costs for the Scottish Homes Pension Fund for the 2022/23 financial year, the Guarantor is required to pay a total of £90,000 per annum for the 3 years from 1 April 2024. Investment expenses will be met from the current funding surplus.

5. Financial impact

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

6. Stakeholder/Regulatory Impact

6.1 The investment strategy of the pension fund is one of the main determinants of risk in terms of volatility of funding level and contributions payable by the Scottish Government.

6.2 The valuation report has been provided to the Scottish Public Pensions Agency on behalf of the Scottish Government.

6.3 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. Background reading/external references

7.1 None.

8. Appendices

Appendix 1 – Scottish Homes Pension Fund 2023 Valuation Final Valuation Report.
Appendix 2 – Lothian Pension Fund Scottish Homes Pensioner Transfer: Operation of Scottish Executive Guarantee.

LPF PUBLIC DATA

HYMANS ROBERTSON

Appendix 1

Scottish Homes Pension Fund

Report on the actuarial valuation as at 31 March 2023

March 2024

Richard Warden FFA

Julie Baillie FFA

For and on behalf of Hymans Robertson LLP

Hymans Robertson LLP

One London Wall	20 Waterloo Street	45 Church Street	1 Semple Street
London EC2Y 5EA	Glasgow G2 6DB	Birmingham B3 2RT	Edinburgh EH3 8BL
t 020 7082 6000	t 0141 566 7777	t 0121 210 4333	t 0131 656 5000
f 020 7082 6082	f 0141 566 7788	f 0121 210 4343	f 0131 656 5050

hymans.co.uk

Contents

Report on the actuarial valuation as at 31 March 2023	Page
Executive summary	1
1 Background	2
2 Approach to the valuation	2
3 Valuation results	4
4 Sensitivity and risk analysis	9
5 Final comments	11
Appendix 1: Data	13
Appendix 2: Assumptions	17
Appendix 3: Reliances & limitations	21
Appendix 4: Glossary	22
Appendix 5: Rates and Adjustments Certificate	24
Appendix 6: Section 13 dashboard	25

Page 163

Executive summary

We have been commissioned by City of Edinburgh Council ("the Administering Authority") to carry out a valuation of Lothian Pension Fund ("the Fund") as at 31 March 2023. This fulfils Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2018. This report is a summary of the valuation.

1. Contribution rates

The contribution rates for individual employers set at this valuation can be found in the Rates and Adjustments certificate. Table 1 shows the combined individual employer rates set at this valuation and the last valuation.

Table 1: Whole fund contribution rates compared with the previous valuation

	31 March 2023	31 March 2020
Expense requirement	£90,000 p.a.	£90,000 p.a.

2. Funding position

At 31 March 2023, the past service funding position has improved from the last valuation at 31 March 2020. Table 2 shows the single reported funding position at this valuation and the last valuation.

Table 2: Single reported funding position compared with the previous valuation

	31 March 2023	31 March 2020
	(£m)	**(£m)**
Deferred Pensioners	15	32
Pensioners	84	109
Total liabilities	**99**	**141**
Assets	**126**	**166**
Surplus (Deficit)	**27**	**25**
Fund level	**127%**	**118%**

1 Background

1.1 History

The deferred pensioner and pensioner members of the Fund were transferred to the Administering Authority prior to the wind-up of the Scottish Homes Residuary Body. The Administering Authority assumed the management of its assets and liabilities from 1 July 2005. The Scottish Government (formerly the Scottish Executive) acts as the Guarantor for the transferred liabilities. The Guarantor's intention is that over time the transferred assets together with any additional contributions required should be sufficient to fund the former Scottish Homes Pension Fund liabilities.

1.2 Homeless Action Scotland

The results shown in this paper include the assets and liabilities of Homeless Action Scotland which transferred into the Fund following its cessation from the Lothian Pension Fund on 12 July 2018.

1.3 Contribution rates

The Funding Agreement sets out how payments from the Guarantor should be determined.

2 2 Approach to the valuation

2.1 Valuation purpose

The triennial actuarial valuation is an important part of the Fund's risk management framework. Its main purpose is to ensure the Fund continues to have a contribution plan and investment strategy that will achieve the objectives set out in the Funding Strategy Statement.

This report marks the culmination of the valuation process and contains its two key outcomes:

1. Reviewing the current funding plan
2. Setting the contribution rate for the period 1 April 2024 to 31 March 2027

The Funding agreement with the Scottish Government, as Guarantor, sets out how contribution payments should be determined.

Further information on the valuation process, methodology and strategy is set out in the publicly available Funding Strategy Statement, Statement of Investment Principles and published papers and minutes of the Fund's Pensions Committee.

Page 165

2.2 Measuring the funding level

The past service funding level, referred to as the Actual Funding Level in the Funding Agreement, is measured at the valuation date. To measure the funding level, a market-related approach is taken to calculate both the assets and the liabilities to ensure they are consistent with one another:

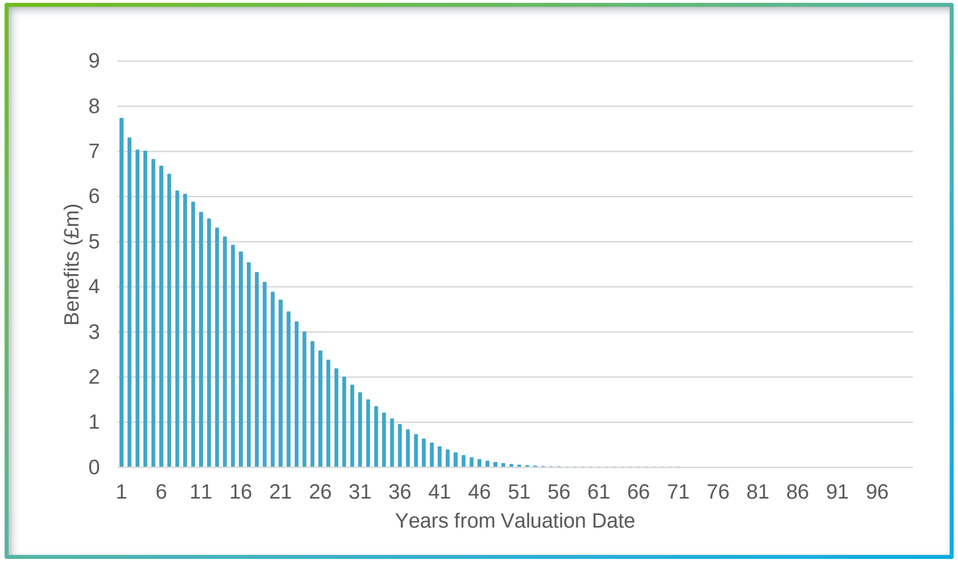
1. The bid-market value of the Fund's assets at the valuation date has been used.
2. The liabilities have been valued using assumptions based on market indicators at the valuation date (these assumptions are detailed in Appendix 2).

2.2.1 Further detail on the liabilities

The liabilities are the value of all future payments to members based on all benefits earned up to the valuation date, expressed in today's money.

Chart 1 shows the projected payments for all members in the Fund at the valuation date. The projections are based on the membership data provided for the valuation (Appendix 1), the assumptions (Appendix 2), and our understanding of the LGPS benefit structure as at 31 March 2023 (details at www.scotlgpsregs.org).

Chart 1: Projected benefit payments for all service earned up to 31 March 2023



To express the future payments in today's money, each projected payment is discounted back to the valuation date in line with an assumed rate of future investment return (known as the discount rate).

3 Valuation results

3.1 Single funding level as at 31 March 2023

Table 3 sets out the assets and liabilities at the valuation date. The results at the 2020 valuation are shown for comparison.

The overall result has been an improvement in the Actual Funding Level (AFL), from 118% to 127% with a larger funding surplus than was reported in 2020.

The funding level and surplus/deficit figures provide a high-level snapshot of the funding position as at 31 March 2023, but there are limitations:

- The liabilities are calculated using a single set of assumptions about the future and so are very sensitive to the choice of assumptions.
- The market value of assets held by the Fund will change daily.

Table 3: Single reported funding position compared with the previous valuation

	31 March 2023	31 March 2020
	(£m)	(£m)
Deferred pensioners	15	32
Pensioners	84	109
Total liabilities	**99**	**141**
Assets	**126**	**166**
Surplus/(Deficit)	**27**	**25**
Funding level	**127%**	**118%**

3.1.1 Projection of the funding position

If the financial and demographic assumptions we have made at this valuation are borne out in practice, and there are no changes to the valuation assumptions, we project that the funding level at the 2026 valuation date will be broadly unchanged.

3.2 Changes since the last valuation

3.2.1 Events between 2020 and 2023

The most significant external event to occur since the last valuation has been the Covid-19 pandemic However, the analysis in Table 5 shows that mortality experience was broadly as expected over the period with minimal impact on the funding position.

CPI inflation was much higher than anticipated by the long-term assumption at the 2020 valuation.

The Fund experience much worse than expected investment returns. This has had a material negative impact on the funding position (Table 4).

Financial

Table 4: Analysis of investment return experience between 2020 and 2023 valuations

	Expected	Actual	Difference	Impact on funding position
Investment returns				
3-year period	0.4%	-13.9%	-14.5%	-£20m
Annual	0.15% pa	-4.9% pa	-5.05% pa	

Membership

Table 5: Analysis of membership experience between 2020 and 2023 valuations

	Expected	Actual	Difference	Impact on funding position
Post-retirement				
Benefit increases	1.3% pa	4.5% pa	3.2% pa	-£14m
Pension ceasing	£1.1m	£1.1m	£0.0m	-£0m

3.2.2 Outlook

Expectations about the future, which inform the assumptions used to value the liabilities, have changed since the last valuation. The most significant changes are:

Future inflation: this is expected to be on average higher than at 2020 due to the current high level of inflation.

Investment returns: due to changes in financial markets, future investment returns are now expected to be higher than at the last valuation.

Table 6: Summary of change in outlook

Factor	What does it affect?	What's changed?	Impact on liabilities
Future investment returns	The rate at which you discount back future benefits payments (also known as the 'discount rate' assumption)	Future investment returns are anticipated to be higher than at 2020.	Decrease of £42m
Inflation	The rate at which pensions (both in payment and deferment) and CARE pots increase.	Significant increase in short-term future inflation expectations.	Increase of £18m
Current life expectancy	How long we expect most people to live for based on today's current observed mortality rates.	Slight increase in life expectancy (not allowing for Covid-related excess deaths)	Increase of £4m
Future improvements in life expectancy	How we expect life expectancies to change (increase) in the future.	Lower rate of improvement in life expectancy through use of updated model of future improvements, including allowance for some recent mortality experience related to the excess deaths from the Covid 19 pandemic..	Decrease of £4m

3.3 Reconciling the overall change in funding position

Tables 7 & 8 provide insight into the funding position change between 31 March 2020 and 31 March 2023. Firstly, the changes expected to happen (Table 7), which relate mostly to assets. Then the impact of actual experience (Table 8), which affects mainly the liabilities.

3.3.1 Expected development

Table 7: Expected development of funding position between 2020 and 2023 valuations.

	Assets	Liabilities	Surplus/ deficit
	£m	£m	£m
31 March 2020 valuation	**166**	**141**	**25**
Cash flows			
Employer contributions paid in	0	0	0
Employee contributions paid in	0	0	0
Benefits paid out	(21)	(21)	0
Other cash flows (eg expenses, transfers in/out)**	0	0	0
Expected changes			
Expected investment returns	1	0	1
Interest on benefits already accrued	0	1	(1)
Expected position at 31 March 2023	**146**	**121**	**25**

***This includes the contributions paid by the Scottish Government each year to cover the administration expenses of the Fund.*

3.3.2 Impact of actual events

Table 8: Impact of actual events on the funding position at 31 March 2023

	Assets	Liabilities	Surplus/ deficit
	£m	£m	£m
Expected position at 31 March 2023	**146**	**121**	**25**
Events between 2020 and 2023			
Benefit increases greater than expected	0	14	(14)
Other membership experience	0	(6)	6
Lower than expected investment returns	(20)	0	(20)
Changes in future expectations			
Investment returns	0	(42)	42
Inflation	0	18	(18)
Longevity	0	0	0
Other demographic assumptions	0	(6)	6
Actual position at 31 March 2023	**126**	**99**	**27**

Numbers may not sum due to rounding.

3.4 Contribution rate payable by the Guarantor

3.4.1 Deficit Recovery Contributions

The Funding Agreement sets out how payments from the Guarantor should be determined. The Target Funding Level (TFL), is 95.5% at 31 March 2023. The AFL (127%) is greater than the TFL at the 2023 valuation date and therefore no deficit contributions are required from the Guarantor for the period from 1 April 2024 to 31 March 2027.

3.4.2 Expense Requirement

The Guarantor has a responsibility to pay towards the cost of the following expenses:

- Administration (including oversight and governance) – estimated to be £90,000 per annum
- Investment management

As required by the Funding Agreement, the liabilities are valued using yield curves that make no allowance for investment returns above gilts. To maintain prudence in future valuations, the Guarantor should also pay for investment expenses otherwise these would act to reduce the returns expected from the gilts-based strategy to below those implied by the yield curves. However, given the Fund is currently in surplus, we and the Administering Authority are comfortable for these expenses to continue to be met by the Fund over the next three years, in line with the approach adopted at the 2020 valuation.

The total Expense Requirement is therefore £90,000 p.a. from 1 April 2024 to 31 March 2027.

3.4.3 Certified contributions

The Guarantor would pay the total of these items to the Fund over the three years from 1 April 2024. This contribution requirement is set out in the Rates and Adjustments Certificate on page 24.

4 Sensitivity and risk analysis

The valuation results depend on the actual assumptions made about the future. By their nature, these assumptions are uncertain which means it's important to understand their sensitivity and risk levels.

4.1 Funding level

4.1.1 Financial assumptions

Future investment returns and future inflation will always be uncertain. The impact of varying levels is set out below.

Table 9: Sensitivity of funding position to discount rate assumption

Discount rate assumption	Surplus/Deficit	Funding level
Per annum	**£m**	**%**
Gilts plus 0.5%	32	134%
Gilts	**27**	**127%**
Gilts less 0.5%	22	121%

Table 10: Sensitivity of funding position to inflation assumption

CPI assumption	Surplus/Deficit	Funding level
	£m	**%**
2.1% pa	29	130%
2.3% pa	**27**	**127%**
2.5% pa	25	125%

It is worth noting that, because the Fund is invested entirely in government bonds, the surplus / (deficit) position is largely immunised against any changes in government bond yields. That is, any increase (decrease) in liabilities as a result of changing bond yields will be offset (partially or fully) by an increase (decrease) in the value of the government bonds held. The extent of this immunisation will depend on how closely the duration and inflation-linkage of the bonds match the characteristics of the Fund's liabilities.

4.1.2 Demographic assumptions

The main demographic risk is that people live longer than expected. A 1-year improvement in life expectancy will result in an increase in the liabilities of around 5%.

4.2 Other risks

4.2.1 Regulatory, administration and governance risks

Potential risks in this area include change in central government legislation, which alters the future cost of the LGPS, and failures in administration processes leading to incorrect data and inaccuracies in actuarial calculations. At this valuation, specific risks include:

McCloud

Benefits accrued by certain members in the LGPS between 2015 and 2022 may increase following the McCloud case, which ruled that transitional protections introduced in 2015 for older members were discriminatory. We've made an allowance for the cost of these potential improvements, based on the guidance issued by the Scottish Public Pensions Agency on 28 April 2023.

Other legal rulings

Benefits could change because of other legal challenges (eg the Goodwin case affecting partner pensions). Given the lack of information about possible benefit changes and their relatively small impact, we have made no allowance for these changes.

Cost cap

This is not relevant since members are no longer accruing benefits.

GMP Indexation

We have made an allowance for all increases on GMPs for members reaching State Pension age after 6 April 2016 by assuming that all increases will be paid for by LGPS employers in the Fund with no future support from the State (ie the worst-case scenario from an LGPS perspective). The affected members are a diminishing group, and the financial significance of this allowance will reduce over time. This is the same approach that was taken for the 2020 valuation.

4.2.2 Post valuation events

Since 31 March 2023, there has been continued volatility in financial markets and rises in interest rates by central banks. These events affect the value of the Fund's assets and liabilities.

However, as mentioned above, the Fund's gilts-based investment strategy provides significant protection against volatile market conditions.

No explicit allowance has been made for this volatility in the valuation results or contribution rates detailed in the Rates & Adjustments certificate. The Fund will continue to monitor changes in the financial and demographic environment as part of its ongoing risk management approach.

4.2.3 Climate change risk

Results may materially change due to the impact of climate change, because of transition and physical risks. We have not quantified the risk exposure here as the Funding Agreement with the Scottish Government as Guarantor means the Fund's exposure to climate risk is reduced.

5 Final comments

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

- The Funding Agreement with the Guarantor
- The Funding Strategy Statement
- The Statement of Investment Principles, which sets out the investment strategy for the Fund
- The general governance of the Fund, such as meetings of the Pensions Committee and Local Pensions Board, decisions delegated to officers, the Fund's business plan, etc.
- The Fund's risk register.

5.1 Valuation frequency

Under the LGPS regulations, the next formal valuation of the Fund is due to be carried out as at 31 March 2026 where contribution rates payable from 1 April 2027 will be set.

Richard Warden FFA | Julie Baillie FFA

March 2024

For and on behalf of Hymans Robertson LLP

Appendices

Appendix 1: Data

Membership data

A summary of the membership data provided by the Fund for the 2023 valuation is set out in Table 11. The corresponding membership data from the previous valuation is also shown for reference.

The results of the valuation are dependent on the quality of the data used. We have carried out a series of validation checks on the data supplied to us by the Administering Authority to ensure that it is fit for purpose.

Asset data

To check the membership data, we have used asset and cashflow data provided by the Fund.

Table 11: Whole Fund membership data at this valuation compared with the previous valuation

Whole Fund membership data	31 March 2023	31 March 2020
Active members		
Number	-	-
Total actual pay (£000)	-	-
Total accrued pension (£000)	-	-
Average age (liability weighted)	-	-
Future working lifetime (years)	-	-
Deferred pensioners (including undecideds)		
Number	264	369
Total accrued pension (£000)	566	801
Average age (liability weighted)	57.7	55.7
Pensioners and dependants		
Number	1,089	1,165
Total pensions in payment (£000)	6,859	6,601
Average age (liability weighted)	73.5	72.2

Investment strategy

A summary of the investment strategy allocation used for the calculation of employer contribution rates and to derive the future investment return is set out in Table 12. In practice, the actual allocation may include some holdings in cash.

This information is as set out in the Fund's Statement of Investment Principles.

Table 12: Investment strategy allocation used for the calculation of employer contribution rates

% Allocated	This Valuation 31 March 2023	Last Valuation 31 March 2020
UK gilts	100%	100%
Total	100%	100%

Appendix 2: Assumptions

Financial assumptions

The Scottish Government acts as the 'Guarantor' for the Fund's liabilities. The valuation of these mature liabilities uses more prudent assumptions than those applied to other employers in the Lothian Pension Fund, as set out in the agreed Scottish Executive Guarantee dated June 2005 ('the Funding Agreement').

The terms of the Funding Agreement impose restrictions on the discount rate that is used to calculate the value of the past service liabilities. The Funding Agreement states that there will be no allowance for anticipated outperformance resulting from investment in assets that are riskier than government bonds, and there will be no deduction for investment expenses.

The yield curve used for the discount rate is the Bank of England nominal yield curve. This is the same discount rate that was adopted for the 2020 valuation of the Fund (albeit updated for market conditions as at 31 March 2023). Cash holdings aside, as at 31 March 2023 the Fund is invested entirely in government bonds, which means the discount rate assumption may be considered as a 'best estimate' of the future investment performance. While the Regulations require the funding basis to be prudent, given the low-risk nature of the Fund's investment portfolio, and the associated low-risk nature of the funding strategy, we believe this discount rate is appropriate for the purposes of the valuation.

Table 13: Summary of assumptions used for measuring the funding level, compared to last valuation on 31 March 2020

Assumption	31 March 2023	Required for	31 March 2020
Discount rate	Bank of England nominal yield curve	To place a present value on all the benefits promised to scheme members at the valuation date.	Bank of England nominal yield curve
Benefit increases	Bank of England implied RPI inflation curve less 1% pa before 2030 and 0.1% pa thereafter*	To determine the size of future benefit payments.	Bank of England implied RPI inflation curve less 0.9% pa

** The change in RPI-CPI gap assumption is to reflect changes to RPI from 2030, when it will be redefined to match CPIH. CPIH inflation is historically very similar to CPI inflation hence the gap of only 0.1% pa after that point.*

Yield Curves

Chart 2 shows the nominal spot yields for a Government-backed loan (ie the yield to maturity of a zero-coupon bond) as at 31 March 2020 and 31 March 2023 (Source: Bank of England). Chart 3 shows the implied inflation curve (RPI) over a range of maturities at 31 March 2020 and 31 March 2023. This is derived from the yields on both fixed and index linked gilts (Source: Bank of England).

All other assumptions adopted are intended to represent our best estimate of future experience. Taken in aggregate, the funding basis results in a ‘best estimate’ of the Fund’s pension liabilities, which are being funded in a prudent manner.

Chart 2: Gilts nominal yield curve

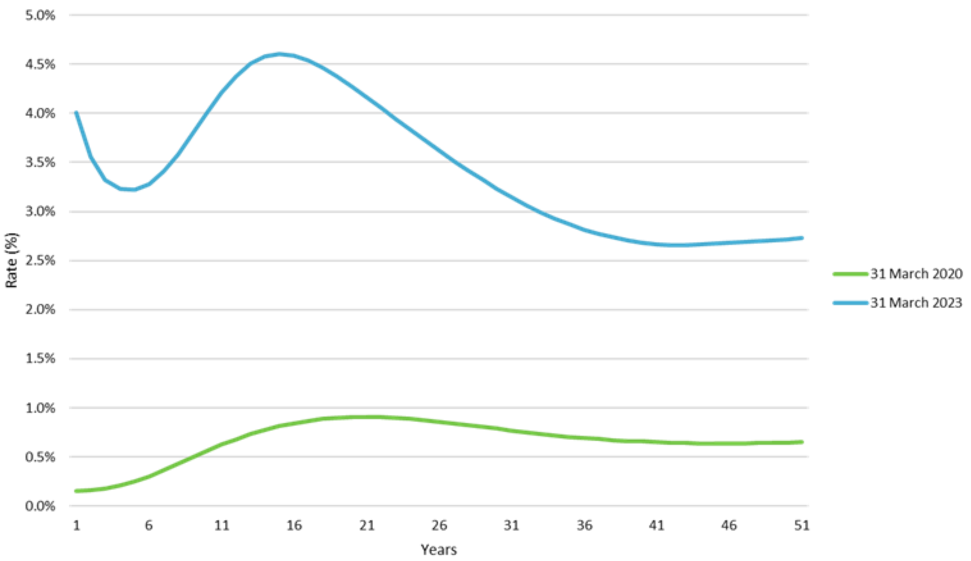
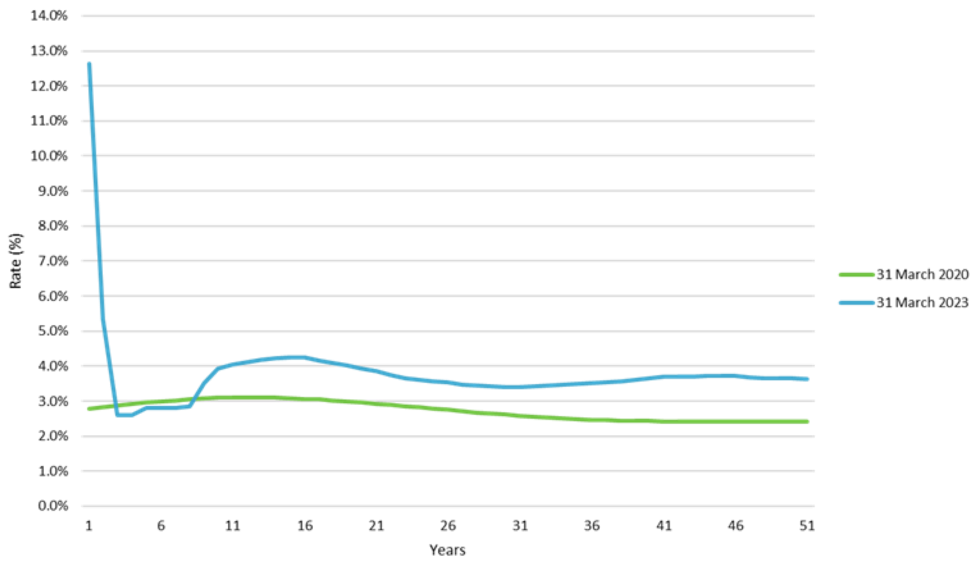


Chart 3: Gilts implied RPI inflation curve



Demographic assumptions

The same demographic assumptions are used to set contribution rates and to assess the current funding level.

Longevity

Table 14: Summary of longevity assumptions at this valuation compared with the previous valuation

	31 March 2023	31 March 2020
Baseline assumptions	Club Vita	Club Vita
Future improvements	CMI 2022 model Initial addition = 0.25% (both Male and Female) Smoothing factor = 7.0 Weighting = 0% (2020 & 2021 data), 25% (2022 data) 1.5% pa long-term rate	CMI 2019 model Initial addition = 0.5% (Male) 0.25% (Female) Smoothing factor = 7.0 2.0% pa long term rate of improvement

Other demographic assumptions

Table 15: Summary of other demographic assumptions

Death in deferment	See sample rates in Table 16
Commutation	70% of future retirements elect to exchange pension for additional tax-free cash up to HMRC limits
Retirement age	The earliest age at which a member can retire with their benefits unreduced
Family details	A varying proportion of members are assumed to have a dependant at retirement or on earlier death. For example, at age 60 this is assumed to be 85% for males and 60% for females. The dependant of a male member is assumed to be 2 years younger than him and the dependant of a female member is assumed to be 3.5 years older than her.

Page 180

Sample rates for demographic assumptions

Table 16: Sample rates of male and female demographic assumptions

Age	Death in Deferment	
	Males	Females
	FT & PT	FT & PT
20	0.21	0.11
25	0.21	0.11
30	0.26	0.16
35	0.30	0.27
40	0.51	0.44
45	0.86	0.71
50	1.37	1.04
55	2.15	1.37
60	3.86	1.75
65	6.44	2.25

Age	Salary scale	Death before retirement	Withdrawals		Ill health Tier 1		Ill health Tier 2	
		FT & PT	FT	PT	FT	PT	FT	PT
20	105	0.11	256.99	338.79	0.00	0.00	0.00	0.00
25	117	0.11	172.88	227.90	0.16	0.13	0.09	0.10
30	131	0.16	144.88	190.99	0.21	0.18	0.12	0.13
35	144	0.27	89.25	164.73	0.41	0.34	0.24	0.25
40	150	0.44	74.23	137.00	0.61	0.51	0.36	0.37
45	157	0.71	61.11	112.78	0.82	0.68	0.48	0.50
50	162	1.04	46.56	85.94	1.50	1.23	1.11	1.13
55	162	1.37	43.56	80.39	5.47	4.43	2.32	2.35
60	162	1.75	35.02	64.64	11.52	9.30	2.38	2.40
65	162	2.25	0.00	0.00	20.73	16.76	0.00	0.00

Figures are incidence rates per 1,000 members
FT and PT denoted full-time and part-time members respectively.

Appendix 3: Reliances & limitations

We have been commissioned by City of Edinburgh Council ('the Administering Authority') to carry out a full actuarial valuation of Scottish Homes Pension Fund ('the Fund') at 31 March 2023, as required under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2018 ('the Regulations').

This report is addressed to the Administering Authority. It has been prepared by us as actuaries to the Fund and is solely for the purpose of summarising the main outcomes of the 2023 actuarial valuation. It has not been prepared for any other third party or for any other purpose. We make no representation or warranties to any third party as to the accuracy or completeness of this report, no reliance should be placed on this report by any third party and we accept no responsibility or liability to any third party in respect of it.

This summary report is the culmination of other communications in relation to the valuation, in particular:

- Correspondence relating to data including the Data Report dated 1 December 2023
- Our Initial Results Report dated 12 October 2023 which outlines the whole Fund results and inter-valuation experience
- The operation of the Scottish Executive Funding Agreement which is dated 29 June 2005, confirming the approach to determine contributions payable to the Fund by the Scottish Government.as Guarantor.
- The Funding Strategy Statement which details the approach taken to adequately fund the current and future benefits due to members

The totality of our advice complies with the Regulations as they relate to actuarial valuations.

The following Technical Actuarial Standards apply to this advice, and have been complied with where material and to a proportionate degree. They are:

- TAS100 – Principles for technical actuarial work
- TAS300 – Pensions

Hymans Robertson LLP is a limited liability partnership registered in England and Wales with registered number OC310282.

A list of members of Hymans Robertson LLP is available for inspection at One London Wall, London EC2Y 5EA, the firm's registered office. Authorised and regulated by the Financial Conduct Authority and licensed by the Institute and Faculty of Actuaries for a range of investment business activities. Hymans Robertson is a registered trademark of Hymans Robertson LLP.

Appendix 4: Glossary

Term	Explanation
Baseline longevity	The rates of death (by age and sex) in a given group of people based on current observed data.
Club Vita	A firm of longevity experts who Hymans Roberston partner with for longevity analysis. They combine data from thousands of pension schemes and use it to create detailed baseline longevity assumptions at member-level, as well as insights on general longevity trends and future improvements.
Commutation	The option for members to exchange part of their annual pension for a one-off lump sum at retirement. In the LGPS, every £1 of pension exchanged gives the member £12 of lump sum. The amounts that members commute is heavily influenced by tax rules which set an upper limit on how much lump sum can be taken tax-free.
CPI inflation	The annual rate of change of the Consumer Prices Index (CPI). The CPI is the UK government's preferred measure of inflation and is the measure used to increase LGPS (and all other public sector pension scheme) benefits each year.
Demographic assumptions	Assumptions concerned with member and employer choices rather than macroeconomic or financial factors. For example, retirement age or promotional salary scales. Demographic assumptions typically determine the timing of benefit payments.

Term	Explanation
Discount rate	An assumption for the annual rate of future investment return. Used to place a single 'today's money' value on a stream of future payments.
Funding position	The extent to which the assets held by the Fund at 31 March 2023 cover the accrued benefits ie the liabilities. The two measures of the funding position are: • the funding level - the ratio of assets to liabilities; and • the funding surplus/deficit - the difference between the asset and liabilities values.
Inflation	Prices tend to increase over time, which is called inflation. Inflation is measured in different ways, using a different 'basket' of goods and mathematical formulas.
Liabilities	An employer's liability value is the single value at a given point in time of all the benefit payments expected to be made in future to all members. Benefit payments are projected using demographic and financial assumptions and the liability is calculated using a discount rate.
Longevity improvements	An assumption about how rates of death will change in future. Typically, we assume that death rates will fall and life expectancies will improve over time, continuing the long-running trend.
Prudence	To be prudent means to err on the side of caution in the overall set of assumptions.

Appendix 5: Rates and Adjustments Certificate

In accordance with regulation 62(4) of the Regulations we have assessed the contributions that should be paid into the Fund by the Guarantor for the period 1 April 2024 to 31 March 2027 to maintain the solvency of the Fund.

The method and assumptions used to calculate the contributions set out in the Rates and Adjustments certificate are detailed in our report on the actuarial valuation dated March 2024. These assumptions underpin our estimate of the number of members who will become entitled to a payment of pensions under the provisions of the LGPS and the amount of liabilities arising in respect of such members.

The required minimum contribution rates are set out in Table 17.

Table 17: Whole fund primary and secondary contribution rates from 1 April 2024 to 31 March 2027

This valuation - 31 March 2023	
Period	Guarantor's minimum contribution rate
1 April 2024 to 31 March 2025	£90,000
1 April 2025 to 31 March 2026	£90,000
1 April 2026 to 31 March 2027	£90,000

Richard Warden FFA | Julie Baillie FFA
March 2024
For and on behalf of Hymans Robertson LLP

Appendix 6: Section 13 dashboard

Metric	Unit	2023 Valuation
2023 funding position – local funding basis		
Funding level (assets/liabilities)	%	127.5%
Funding level (change since previous valuation)	%	9.8%
Asset value used at the valuation	£m	126
Value of liabilities (including McCloud liability)	£m	99
Surplus (deficit)	£m	27
Discount rate (past service)	% pa	Bank of England nominal yield curve
Discount rate (future service)		Past service and future service are consistently valued with the same underlying assumptions, methodologies and models regarding future expected levels of inflation, interest rates and investment returns.
Assumed pension increase (CPI)	% pa	Bank of England implied RPI inflation curve less 1% pa before 2030 and 0.1% pa thereafter
Method of derivation of discount rate, plus any changes since previous valuation		No change to method of derivation of discount rate since previous valuation

Metric	Unit	2023 Valuation
Assumed life expectancy at age 65		
Life expectancy for current pensioners – men age 65	Years	20.2
Life expectancy for current pensioners – women age 65	Years	23.0
Life expectancy for future pensioners – men age 45	Years	20.7
Life expectancy for future pensioners – women age 45	Years	24.9
Past service funding position – SAB basis (for comparison purposes only)		
Market value of assets	£m	126
Value of liabilities	£m	88
Funding level on SAB basis (assets/liabilities)	%	143%
Funding level on SAB basis (change since last valuation)	%	-46%

Metric	Unit	2023 Valuation	2020 Valuation
Contribution rates payable			
Primary contribution rate	% of pay	0.0%	0.0%
Secondary contribution rate (cash amounts in each year in line with CIPFA guidance)			
1st year of rates and adjustments certificate	£m	0.09	0.09
2nd year of rates and adjustments certificate	£m	0.09	0.09
3rd year of rates and adjustments certificate	£m	0.09	0.09
Giving total expected contributions			
1st year (£ figure based on assumed payroll)	£m	0.0	0.0
2nd year (£ figure based on assumed payroll)	£m	0.0	0.0
3rd year (£ figure based on assumed payroll)	£m	0.0	0.0
Assumed payroll (cash amounts in each year)			
1st year rates and adjustments certificate	£m	0.0	0.0
2nd year rates and adjustments certificate	£m	0.0	0.0
3rd year rates and adjustments certificate	£m	0.0	0.0
Three-year average	% of pay	0.0%	0.0%
Average employee contribution	% of pay	0.0%	0.0%
Employee contribution rate (£ figure based on assumed payroll of £0m)	£m pa	0.0	0.0

Metric	Unit	2023 Valuation	2020 Valuation
Deficit recovery and surplus spending plan			
Latest deficit recovery period end date, where this methodology is used by the fund's actuarial advisor.	Year	Methodology not used	Methodology not used
Earliest surplus spreading period end date, where this methodology is used by the fund's actuarial advisor.	Year	Methodology not used	Methodology not used
The time horizon end date, where this methodology is used by the fund's actuarial advisor	Year	2043	2040
The funding plan's likelihood of success, where this methodology is used by the fund's actuarial advisor.	%	Methodology not used	Methodology not used
Percentage of liabilities relating to employers with deficit recovery periods of longer than 20 years	%	Methodology not used	Methodology not used
Additional information			
Percentage of total liabilities that are in respect of Tier 3 employers	%	0.0%	N/A
Included climate change analysis/comments in the 2023 valuation report		Yes	N/A
Value of McCloud liability in the 2023 valuation report (on local funding basis)	£m	0.01	N/A

Appendix 2

→ LOTH / SAP / Scottish Homes Pensioner Transfer

Operation of Scottish Executive Guarantee

Preamble

The Scottish Homes Pension Fund[1] (SHPF) is to be transferred to the Lothian Pension Fund (LPF) prior to the wind up of the Scottish Homes residuary body, with the LPF assuming responsibility for the management of its assets and liabilities with effect from 1 July 2005.

This note documents the funding objective for the transferred liabilities and particularly how any requirement for Scottish Ministers to make payments under the Local Government Pension Scheme (Scotland) Regulations 1998 (as amended by the Local Government Pension Scheme (Scotland) Amendment (No. 2) Regulations 2005) will be determined. Nothing in this note over-rides the regulations. This note has been prepared for the City of Edinburgh Council, as Administering Authority to the LPF, after consultation with the Scottish Executive and Scottish Homes.

Liabilities for payment of the pensions in payment and deferred pensions of the SHPF at 30 June 2005 are being transferred to the LPF along with the residual assets of the SHPF. The first pension instalment being paid by LPF will be on 15 August 2005 in respect of the month from 16 July[2]. The bulk transfer of the assets held in the SHPF will be transferred on 1 July 2005. The transferred assets from the SHPF will be assimilated within the LPF, albeit invested on a different strategy to that used for open ongoing employers.

The Scottish Executive will act as the Guarantor for the transferred SHPF liabilities. The Guarantor's intention is that over time the transferred assets together with any additional contributions that may be made under this agreement should be sufficient to fund the SHPF liabilities. This guarantee will continue until all liabilities of the former SHPF are extinguished.

Notes: All administration costs, including the cost of administering this guarantee will be charged directly to the Scottish Homes element of the LPF. The ongoing contact for operational issues (for example, exercising discretions under the Local Government Pension Scheme (Scotland) Regulations 1998, as amended) will be with Communities Scotland (or its successor) and for funding / guarantee issues will be the Scottish Executive (or its successor).

Any future legislative/regulatory changes affecting the operation of this guarantee should not have an adverse impact on the LPF.

Actuarial valuation procedure and further contributions

The liabilities relating to the SHPF element of the LPF will be valued at 1 July 2005, at 31 March 2008 and subsequently at three yearly intervals. The valuation assumptions, including the assumed future yields on different asset classes, will be set by the LPF actuary and will be demonstrably consistent with those used for the balance of the LPF, except to the extent that the SHPF liabilities exhibit peculiar characteristics that are not already reflected in the valuation assumptions.

However, the funding target for the SHPF element will be different in recognition of the nature of the liabilities and the existence of the guarantee.

[1] Both the SHPF and LPF operate under the Local Government Pension Scheme (Scotland) Regulations 1998
[2] The final SHPF pension payment will be made on 28 June 2005 in respect of the period from 1 June 2005 to 15 July 2005.

Funding Targets

The Target Funding Level (TFL) is expressed in terms of the valuation of liabilities without anticipating any excess returns from equities. The TFL will rise over time as the liabilities become more mature, as shown in the table below.

Valuation Date	Target Funding Level
2005	85.0%
2008	87.5%
2011	89.5%
2014	91.5%
2017	93.0%
2020	94.5%
2023	95.5%
2026	96.5%
2029	97.5%
2032	98.0%
2035	98.5%
2038	99.0%
2041	99.5%
2044 & thereafter	100.0%

At each three yearly valuation point, regardless of the actual investment strategy by the LPF for the former SHPF liabilities, the LPF actuary will calculate the ratio of the value of the assets to the remaining liabilities discounted using the real redemption yield on index-linked government bonds of appropriate term to the undischarged liabilities. This quantity is called the Actual Funding Level (AFL). There will be no anticipated out-performance from non Government bonds nor any deduction for investment expenses in the valuation of the liabilities.

Guarantor's Payments

The AFL and the TFL will be compared at each triennial valuation to assess whether contributions are required from the Guarantor. Where contributions are required the amortisation period will be determined by the LPF. The initial amortisation period is expected to be 8 years, but this may reduce in future.

Funding Scenario		Guarantor's Contributions (effective from one year after valuation date)
1.	AFL greater than or equal to TFL at current valuation date	No contributions
2.	AFL greater than or equal to TFL at previous valuation date, but less than TFL at current valuation date	Contributions are the lesser of: • current level of contributions; or • the contributions that would result from current AFL if calculated by reference to TFL at this valuation date, as in (3) below.
3.	AFL less than TFL at previous valuation date	Shortfall relative to current target (i.e. TFL at this valuation x capitalised value of liabilities minus assets) is spread over period not exceeding 8 years[3]

Whatever the outcome of the valuation as at 1 July 2005, there would be no contributions levied on the Guarantor. The 2008 valuation would be the first assessment that could lead to the Guarantor making extra contributions in the 2009/10 financial year.

The LPF will use its best endeavours to give the Guarantor at least 2 (two) months notice of any change in contributions.

A worked example illustrating how the funding objective is expected to work in practice is included in Annex A.

[3] shortfall would be amortised over 8 years (or less) assuming level monthly payments starting one year after effective date of valuation.

Investment Strategy

The investment strategy of the LPF is set by the City of Edinburgh Council, as administering authority. The LPF will consult the Guarantor on any changes to investment strategy.

Initially, the intention is to adopt an investment strategy comprising of broadly:

	Proportion of Total Assets
Global Equities	45%
Bonds	45%
Property	10%
Total	100%

It is expected that the global equities component will be reduced over time, by around five percentage points every three years. These reductions need not be linked to triennial valuations. Indeed, the desire of the Guarantor is to lock away any *surpluses* that may occur over time by accelerating the transfer of assets into bonds. Here a surplus is defined as assets in excess of the Target Funding Level as defined above.

The Administering Authority will consider how this objective may be implemented in practice.

W Douglas B Anderson FIA
Actuary to the Lothian Pension Fund
For and on behalf of Hymans Robertson LLP
29 June 2005

Signed on behalf of City of Edinburgh Council:

Name: GEIK DREVER

Position: HEAD OF INVESTMENT & PENSIONS

Date: 1 July 2005

Signed on behalf of Scottish Executive:

Name: Malcolm Chisholm

Position: Minister for Communities

Date: 6-7-05

Annex – Worked Example of Funding Objectives

Consider the position at the 2008 valuation. The figures used below are hypothetical and do not represent the extremes of the range of outcomes which could occur.

The Target Funding Level (TFL) would be 87.5% of the then liabilities valued on a minimum risk discount rate (i.e. based on Government bond yields of appropriate duration to the liabilities).

Suppose, for simplicity, that bond yields remain the same at around 4.7% pa. The value of the undischarged liabilities in 2008 might be around £128m.

The TFL in 2008 is therefore £128m x 87.5% = £112m

Consider these scenarios for actual assets:-

Scenario 1 (AFL>TFL in 2008)

Assets are £115m in 2008, giving an AFL of 115/128 = 89.8%

As this is higher than the TFL of 87.5% (£112m), no contributions are payable

Scenario 2 (AFL<TFL in 2008, but AFL>TFL in 2005)

Assets are £110m in 2008, giving an AFL of 110/128 = 85.9%

This is lower than the TFL at 2008, but is higher than the TFL at 2005 of 85%. There are therefore no contributions payable. This position will be reviewed at the 2011 valuation. For no contributions to continue beyond 2011/12, the AFL would have to rise to be at least 87.5%. (since 87.5% is the TFL for 2008).

Scenario 3.0 (AFL<TFL in 2008 and AFL<TFL in 2005)

Suppose assets fall to £90m by 2008, giving an AFL of 90/128 = 70.3%

This is less than the TFL in 2008 of 87.5% and the TFL in 2005 of 85%. Therefore contributions become payable from April 2009.

The shortfall relative to the TFL is £112m - £90m = £22m

The recovery of this deficit is to be targeted over 8 years. It is assumed that monthly contributions will be made and allowance is included for the "lost" investment returns on the deficit.

Assuming bond yields of 4.7%, the monthly contributions would be calculated to be

$\frac{£22m \times 1.047}{12 \times 6.69^{4}}$ = £287,000 per month

The funding position would be reviewed again at the 2011 valuation, against a TFL of 89.5%. Thus these contributions from the Guarantor would be payable for at least 3 years (2009/10 to 2011/12), but may be reduced (or increased) following the 2011 actuarial valuation.

Scenario 3.1 (AFL<TFL in 2011 and AFL>TFL in 2008)

Suppose there is a dramatic improvement in the AFL from 2008 to 2011, but not sufficient for the AFL to exceed the TFL in 2011 (89.5%).

Suppose in 2011, that the undischarged liabilities are valued at £126m. The assets are £108m in 2011, giving an AFL of 85.7% and a deficit relative to the 2011 TFL of £4.8m.

Again, assuming that bond yields remain at 4.7%pa, the monthly contributions would be calculated to be:

$\frac{£4.8m \times 1.047}{12 \times 6.69}$ = £62,600 per month payable from April 2012 for 8 years, but reviewed again at. 2014 valuation

Notes – these examples assume:

(a) bond yields remain unchanged

(b) we make no allowance for the shape of the yield curve today

(c) demographic experience and pension increases are in line with assumptions

[4] 6.69 is derived as the value of a level annuity payable for eight years at 4.7%pa interest. The actual annuity would be calculated at the prevailing redemption yield on bonds of appropriate duration.

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Investment Strategy Review

Item number 6.6

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 Approve amendments to the investment strategy as outlined in paragraphs 4.7 to 4.8 and 4.25.

1.2 Subject to approval of the amendments above, also approve updates to the Fund's Statement of Investment Principles (SIP) to reflect the agreed changes to strategy (separately included in Appendix 1).

David Vallery

Chief Executive Officer, Lothian Pension fund

Contact: Emmanuel Bocquet, Chief Investment Officer, Lothian Pension fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Investment Strategy Review

2. Executive Summary

2.1 The purpose of this report is to provide the conclusions of the review of the investment strategy of the Lothian Pension Fund ("the Fund") and to ask Committee to approve the long-term investment strategy, more specifically the strategic asset allocation ("SAA") of the fund's assets.

2.2 The proposed SAA makes minor amendments to the current one, including name changes for two policy groups (paragraphs 4.7 to 4.8) and changes to the policy group weightings and permitted ranges (paragraph 4.25), including a 5% reduction in Equities, a 5% increase in Sovereigns (formerly LDI), and a 2% increase in Cash offset by a 2% reduction in Credit (formerly Non-Gilt Debt).

2.3 The SAA review has been undertaken in cooperation with the Falkirk and Fife Pension funds, taking advice from the Joint Investment Forum (JIF) and Hymans Robertson.

2.4 There are two sources for growing the assets to fund future pension payments: contributions and investment returns. The proposed SAA aims to balance the Committee's assumed aim for affordable contributions and contribution stability (which is affected by the actuarial assessment of funding level every three years), against the need to generate positive real returns from invested assets to pay pensions over a long time horizon.

2.5 The JIF independent advisers note that decisions on strategy should be taken with a long-term perspective, and that changes to SAA involve trade-offs between different risks.

2.6 The change in policy group weightings is in line with the views expressed by the Committee during consideration of the valuation results and proposed updated contributions and consistent with these.

3. Background

3.1 The fund undertakes an in-depth review of its investment strategy in conjunction with the completion of its triennial actuarial valuation. This enables consideration of the actuary's updated assumptions and any changes to contribution rates. The Committee is also reviewing the completed actuarial valuation dated 31 March 2023 at its meeting in March 2024.

3.2 The investment strategy of a pension fund has a significant impact on its investment performance, funding level and employer contribution rates. Setting SAA is therefore a major decision for the Pensions Committee.

3.3 The review has been undertaken in collaboration with Falkirk and Fife Pension funds, working with the JIF and Hymans Robertson. Initial results were presented and discussed at the JIF on 8 September 2023. This was followed by a joint training session for the Committees and Boards of the three funds on 15 September 2023 to provide information on the approach of Hymans Robertson to the asset liability modelling being undertaken. Additional results from Hymans Robertson were considered at the December 2023 JIF, with a subsequent joint training session for the three funds on 6 February 2024 to provide background information on policy groups, asset liability modelling and to discuss this review.

3.4 The Pensions Committee of each fund is responsible for determining its own investment strategy and monitoring implementation of that strategy and its success. Given that the funding position and cash flow outlook of each fund is different, the investment strategy of each fund may be different.

3.5 LPF ’s Committee delegates implementation of investment strategy through a scheme of delegation to the CEO of LPF who in turn delegates to the Fund’s Chief Investment Officer.

3.6 The Fund constituted the JIF to provide strategic advice. Its two external independent advisers, Kirstie MacGillivray and Stan Pearson, have been supported by Lothian’s internal investment team and Hymans Robertson in this investment strategy review. Hymans Robertson undertook asset liability modelling, which tests potential investment strategies and quantifies the probabilities of achieving objectives.

3.7 To provide suitable investment programmes for the differing requirements of employers, the Fund currently operates the four investment strategies detailed in Table 1.

Table 1

Investment Strategy	**Assets (£m)**	**Weight***
Main	9,075	94.1%
Buses	513	5.3%
50/50	37	0.4%
Mature Employers	15	0.1%
Total	9,640	100%

Source: Northern Trust as of 31 March 2023
*Does not sum to 100% due to rounding

3.8 Most employer liabilities are funded under the Main strategy. This strategy maintains a significant exposure to real investments such as equities, which have a history of protecting and enhancing real purchasing power. This reflects the fact that the Fund is open to new entrants, so these employers have long duration liabilities that continue to grow. Indeed, without real investment growth, contributions would need to be significantly higher to meet these new liabilities. Volatility of returns associated with these real investments is less important when liabilities are long in duration and so funding level variability is less important.

3.9 The other three strategies are maintained because the duration of liabilities of some employers are shorter than those of the employers in the Main strategy.

3.10 The Mature Employer strategy is invested entirely in index-linked gilts and cash to match assets and liabilities and eliminate funding level variability as much as possible.

3.11 The 50:50 strategy combines the Main and Mature Employers strategies in 50:50 proportion, reflecting the relative maturity of those employers and the duration of their liabilities.

3.12 The Buses company has closed to new entrants and so the fund is maturing, and its strategy combines the Main and Mature Employers strategies in 55:45 proportion. Separate discussions have been held with the Buses company to agree a modest reduction in investment risk to change the proportion to 50:50.

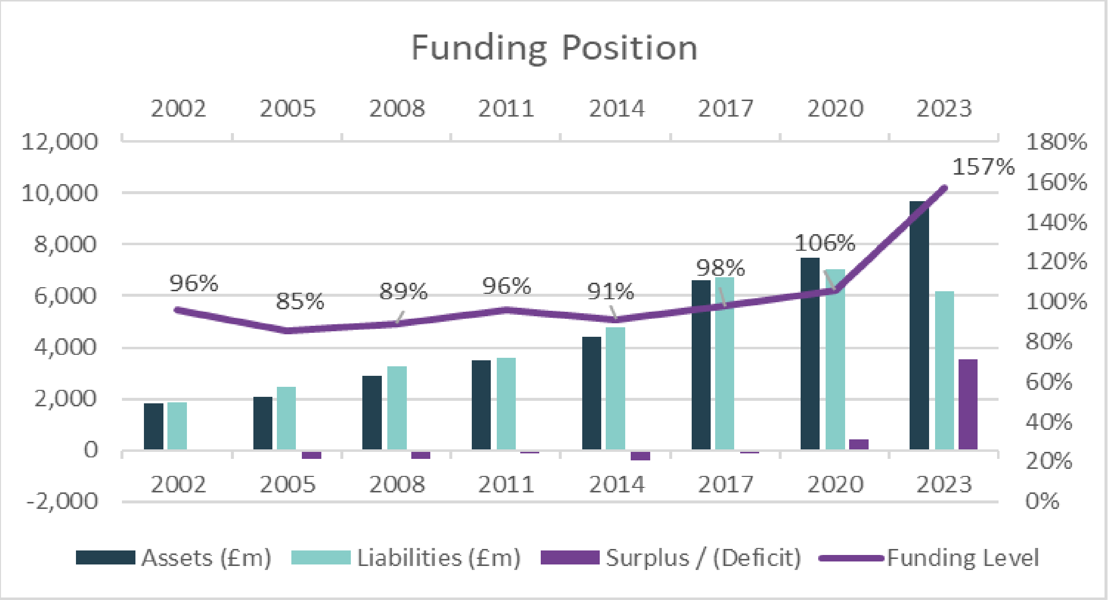
4. Main Report

Funding Position

4.1 The investment strategy (or strategic asset allocation, “SAA”) of a pension fund has a significant impact on its investment performance, funding level and employer contribution rates. Setting SAA is therefore a major decision for the Fund.

4.2 Figure 1 below shows the actuary’s assessment of the funding position over the last several actuarial valuations. This SAA review has been conducted alongside the 2023 actuarial valuation.

Figure 1



4.3 The actuary estimates that the funding level was 157% as of 31 March 2023, a significant improvement on the 106% as of 31 March 2020. Figure 1 shows that the improvement in funding level has been driven by both an increase in the value of assets (due to investment returns) and a reduction in the value of liabilities (due to higher interest rates).

4.4 Table 2 shows the cashflows into and out of the fund to 31 March 2023. It illustrates that net cashflow from dealing with members has been neutral to modestly negative. Income from investments has averaged £253m over the last five years, which means that the fund is cash flow positive on an overall basis.

Table 2

Cash Flow (net additions / withdrawals from dealing with members)

	2017/18	2018/19	2019/20	2020/21*	2021/22	2022/23
Income	196	227	240	305	271	265.8
Expenditure	214	241	279	247	265	284
Net Cash Flow	(18)	(15)	(39)	58	6	(18)

* A one-off transfer in of assets by Visit Scotland amounted to £58.3m in 2020/21

Policy Groups

4.5 To support effective strategy determination, the JIF continues to recommend that Committee defines the fund's SAA using five policy groups. These classify assets into categories with similar risk and return characteristics, which are not completely correlated with one another. The weighting of these groups in a portfolio is the key determinant of expected return and risk. Table 3 below shows the policy groups in descending order of expected return and risk.

4.6 The JIF has recommended minor amendments to the existing five policy groups which condense the vast array of investment choices into a manageable number of investment groups. The proposed policy groups are shown in Table 3.

4.7 The name of the LDI policy group has been amended to **Sovereigns** to reflect the fact that this policy group may invest in high quality sovereign bonds (e.g. UK and US government bonds) which offer diversification to the equity policy group. These assets provide interest rate and potentially inflation exposure that offsets similar exposures within the fund's liabilities.

4.8 The name of the Non-Gilt Debt policy group has been changed to **Credit** to reflect the fact that this policy group has exposure to debt issued by non-sovereign issuers (e.g. corporates) that typically offer a higher rate of return (via a 'credit' spread) than sovereign government bonds.

Table 3

Policy Group	Objective	Permitted Assets
Equities	The principal driver of the Fund's growth and, in the long term, expected to outperform liabilities, albeit with periods of volatility.	Listed equities; private equities; forward currency contracts; equity futures.
Real Assets	Positive real returns with an income stream, in some way, linked to inflation. Likely to deliver some diversification from equity returns.	Property; infrastructure; timberland; agriculture; commodities.
Credit (formerly Non-Gilt Debt)	Assets likely to offer diversification from equity returns, strategic funding level protection and/or a superior yield to that available from, and where returns may have a positive correlation to, sovereign bonds.	Investment grade bonds; high yield bonds; loans; private credit; emerging market bonds.
Sovereigns (formerly LDI)	Assets likely to offer diversification from equity returns and strategic funding level protection by having interest rate and potentially inflation exposure that offsets exposures of the liabilities and so reduces funding level variability.	Index-linked gilts; nominal gilts; gilt futures; overseas sovereign bonds.
Cash	Liquidity function mostly avoiding credit and duration risks.	UK Treasury assets; overseas Treasury assets; local authority loans; bank or building society deposits (all short term).

4.9 Under the governance structure of the Fund, the implementation of the investment strategy within these policy groups is delegated by Committee to nominated officers with advice from the JIF.

4.10 The modelling results from Hymans Robertson indicate that the size of the allocation to equities is by far the key determinant of investment risk and return. Variation in the types of investment managers within each policy group is typically less significant to the overall risk and return than strategic policy group allocations over the long term.

Asset Liability Modelling

4.11 An Asset Liability Model (ALM) is a tool which projects how the Fund’s assets and liabilities might perform in the long term. The primary aim is to indicate the degree of uncertainty associated with a particular strategy; the ALM is not a forecasting tool. It describes how likely different investment strategies are to deliver returns that achieve the Fund’s objective of paying pensions as they fall due. Investment strategies with higher expected returns are likely to require lower employer contributions. However, such strategies will be accompanied by more variability in funding level and the risk that employers will be required to make larger contributions if investments experience significant downside movements.

4.12 ALMs include many assumptions about how the economy and investment markets might change in the future, highlighting the uncertainty in projecting future outcomes. Hymans Robertson has tested the current and potential SAA, which are expected to deliver sufficient returns with a high probability of success over an 18-year timeframe (2 years on from the past review conducted as of March 2021). There is, however, a wide range of possible outcomes, which reflects the need to generate returns in excess of the return generated by gilts, the matching asset for a pension fund. There is less certainty associated with the future returns from other financial assets.

4.13 The assumption for future gilt yields is one of the most critical inputs to the model. The level of gilt yields does not impact the actual pensions which will fall due. But it greatly affects the current value of these liabilities calculated by the actuary, as discounted by this rate. The higher the assumed discount rate (or level of gilt yields), the lower the current value of liabilities, as calculated by the actuary’s model.

4.14 Hymans Robertson’s asset liability model assumes, on average, that nominal gilts will return c.4.1% p.a. over the next 20 years, with nominal 17-year yields falling from 3.9% (at 31 March 2023) to 3.4% at the end of the projection period. This is a major assumption because nominal 15-year gilt yields as of 13 February 2024 are c.4.4% and expected to decline. Nominal 30-year gilt yields are c.4.6%, consistent with 15-year gilt yields in 15 years’ time rising to 4.8% pa. The difference between the Hymans model calibrated at the valuation date and current market levels illustrates the limitation of single point in time valuations and supports the need for a long-term approach and moderate changes.

4.15 The ALM helps to demonstrate, on its assumptions, whether the SAA is likely to deliver the funding objectives, associated risks, and the impact of amending the SAA. However, model assumptions need to be considered when interpreting the results.

Results

4.16 Results from Hymans showed that the strong funding position provides a high degree of flexibility in terms of adjusting the SAA and/or the approach to contributions, due to the large past service liability surplus.

4.17 However, we and Hymans Robertson have highlighted that the funding position can vary materially between measurement dates because of changes in market conditions, with the results being particularly sensitive to gilt yields and the implied future expected returns from asset classes and policy groups.

4.18 As part of the review, Hymans Robertson state that “a key consideration is therefore to set an investment strategy and contribution rate that is sustainable in the long term”.

4.19 They suggest that a suitable SAA (on a sustainable basis) is one that meets future service accrual only, at an affordable level of contributions, without relying on the past service funding surplus.

4.20 On this basis, the Fund’s actuary has confirmed that the current SAA (60% equity weight) is consistent with a long term 19.3% contribution rate (excluding 0.3% allowance for administration expenses). Because the assets to pay benefits can only be generated by a combination of investment returns and contributions, adopting a SAA with a lower expected investment return would entail higher sustainable contributions, and vice versa.

Recommended Strategy (Main Strategy)

4.21 The proposed SAA for the Main Strategy is presented in Table 4 below. It is based on expectations that the asset mix will generate long-term returns comfortably in excess of liabilities.

4.22 The proposed strategy considers the expected reduction in contributions resulting from the actuarial valuation. It modestly reduces overall investment risk, via a 5% reduction in the weight of the Equity policy group and a 5% increase in the allocation to the Sovereigns policy group, while maintaining sufficient levels of investment return to support a long-term affordable contribution rate.

4.23 The 5% reduction in central equity weighting is lower than the 10% reduction discussed during the valuation consultations. However, it is consistent with the Committee’s desire to modestly reduce equity risk as well as the long-term return requirements of the Fund.

4.24 The modest 2% allocation to the Cash policy group recognises the operational cash requirements of the Fund.

4.25 The permitted ranges are the constraints within which nominated officers can implement strategy under delegated authority without referral to the Committee.

These ranges are wide enough to avoid unnecessary and potentially costly rebalancing under normal financial conditions but enable prompt action in fast moving markets.

Table 4

Policy Group (%)	Current Strategy	Proposed Strategy	Current Permitted Ranges	Proposed Permitted Ranges
Equities	60	55	50 -70	45 - 65
Real Assets	20	20	10 - 30	10 - 30
Credit	10	8	0 - 20	0 - 20
Sovereigns	10	15	0 - 20	5 - 25
Cash	0	2	0 - 15	0 -15
Total	**100**	**100**		

4.26 The investment team will continue to monitor actual asset weightings and adjust policy group exposures within the constraints of the permitted ranges where required or to make tactical investment decisions, with regular reporting on strategy implementation at the quarterly JIF meetings. The team will refer to Committee for direction should there be a recommendation to operate out with the permitted ranges or to adjust the strategic weights. The Committee will continue to receive periodic updates on asset allocation and performance.

Updates to Statement of Investment Principles

4.27 Subject to the above changes being approved, Committee is also asked to approve updates to the Fund's Statement of Investment Principles (SIP) to reflect the agreed changes. These changes are provided in a separate Appendix 1, which shows:

4.27.1 Changes to the policy group names and underlying asset classes (pages 7 and 8 of the SIP), and

4.27.2 Changes to the target allocation and permitted range for the Main strategy, and the consequent target allocation changes for 50:50 and Buses strategy (Appendix A of the SIP, pages 13 and 14).

4.28 The proposed updates to the SIP only include those changes being approved as part of this review. A full review of the entire SIP document (as part of the annual SIP review cycle) will be included for consideration at the June Committee.

5. Financial impact

5.1 The investment strategy has a significant impact on the investment returns of the pension fund and hence impacts on the funding level and employer contribution rates.

6. Stakeholder/Regulatory Impact

6.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the fund and are invited to comment on relevant matters at Committee meetings.

6.2 There are no adverse health and safety, governance, compliance, or regulatory implications as a result of this report.

7. Background reading/external references

7.1 None

8. Appendices

Appendix 1 – SIP proposed changes

This page is intentionally left blank

LOTHIAN PENSION FUND

submitted a report in October 2021, which met the high stewardship standards that the FRC sets. The Funds' Stewardship Report is published as a standalone document.

FUNDS' OBJECTIVES

The **primary objective** of the Funds is to ensure that there are sufficient funds available to meet all pension and lump sum liabilities as they fall due for payment.

The **funding objectives** for each Fund are documented in the Committee's Funding Strategy Statement, which is reviewed at least triennially. The funding objectives, together with the rates of return being targeted and levels of risk to be tolerated, are central to each Fund's investment strategy and govern the allocation across various asset classes.

The **investment objectives** of the Funds are to achieve a return on Fund assets which is sufficient over the long term to meet the funding objectives as outlined in the Funding Strategy Statement. Investment returns are generated by a combination of income (from dividends, interest and rents) and gains or losses on capital.

In effect, the Funds' objectives are to generate sufficient long term returns to pay promised pensions and to make the scheme affordable to employers now and in the future, while minimising the risk of having to increase contribution rates in the future.

Committee has set investment strategy with reference to the following **policy groups,** which are regarded as the key determinants of risk and return. The policy groups condense the vast array of investment choices into a manageable number of investment groups with broadly similar characteristics:

- **Equities** provide an equitable share in the assets and profits of companies. Income is provided through discretionary share dividends. Equities are listed in the UK or overseas, or are unlisted (private equity). Equities have historically produced returns above inflation.

- **Other Real Assets** are typically investments in a share of income and capital appreciation of tangible assets, including **property** (land and/or buildings for commercial or residential use), **infrastructure** (assets deemed essential to the orderly functioning of daily life, such as renewable energy generation and transmission assets, water utilities, airports and toll roads) and **timberlands**. Income comes from dividends and rents.

- **Credit~~Non-Gilt Debt~~** instruments are issued by a range of non-sovereign borrowers to finance their activities in various sectors of the economy, which means that they carry varying degrees of credit risk. Income is provided through interest, which is typically paid to the lender on a regular basis until the loan capital is repaid, generally at par by the issuer at a pre-determined date. Bonds can pay a fixed, variable or inflation-linked rate of interest. Bonds are either listed in the UK or overseas or are unlisted (private debt).

- **Sovereigns~~LDI~~** are bonds, which are debt instruments issued by sovereign governments (such as the UK and US). Typically, these provide interest payments on a regular basis over the life of the loan until capital is repaid at maturity. Some bonds provide interest payments and capital repayment value that is directly linked to price inflation (e.g. the Retail Price Index (RPI) in the UK). These are known as Index Linked Gilts and they provide the closest match to the Funds' liabilities, most of which are inflation-linked, albeit to a different measure of price inflation (the Consumer Price Index (CPI)). Some other governments (such as the US) also issue this type of debt, but in different currencies tied to price inflation in their own countries.

- **Cash** is also a form of investment used to provide instant or short-term liquidity, and can be held in both sterling and foreign currencies (including Treasury Bills, Money Market Funds and Secured Investments). Cash generates interest income, but typically at a lower rate than bonds and other debt.

As the returns of the above investments aren't completely correlated, the Funds expect to achieve diversification and better risk-adjusted returns by investing in assets from each policy group.

FUNDS' STRATEGIES

The Committee's agreed investment strategies (presented in Appendix A) are expressed in terms of allocations to various policy groups (or asset classes). These reference portfolios are expected to generate the required return with a reasonable probability of success. The rate of return being targeted and the level of risk to be tolerated are central to the determination of the investment strategy (or asset mix) of each Fund.

To provide suitable investment strategies for differing requirements of employers, **Lothian Pension Fund** currently operates four investment strategies, as follows:

- **Main Strategy** is a diversified portfolio, mostly invested in long-term, return-seeking assets, such as equities, due to the long-term nature of the pension liabilities. Approximately 94% of employers' assets are invested in the Main Strategy.

- **MEG ("Mature Employers Group") Strategy** invests in a portfolio entirely invested in UK gilts and cash to reduce investment risk for employers (except for Transferee Admitted Bodies) that are close to leaving the Fund. These employers have a low tolerance for risk and this

APPENDIX A – INVESTMENT STRATEGIES (~~21 JUNE 2023~~20 March 2024)

Lothian Pension Fund: Main Strategy

Investment Objectives: to generate returns sufficient to pay pensions as they fall due.

Investment Strategy:

Policy Group	Target Weight 2024 - 2027	Permitted Range
Equities	55%	45 - 65%
Real Assets	20%	10 - 30%
Credit	8%	0 - 20%
Sovereigns	15%	5 - 25%
Cash	2%	0 - 15%
Total	**100%**	

Lothian Pension Fund: MEG ("Mature Employers Group") Strategy

Investment Objective: to achieve a return in line with gilts that match the duration of the liabilities.

Investment Strategy: the MEG Strategy invests exclusively in UK Gilts and Cash matching the duration of employer liabilities with the duration of the invested assets.

Lothian Pension Fund: 50/50 Strategy

Investment Objective: to achieve a return in line with a 50:50 investment in the Main Strategy and the MEG Strategy and generate a return that pays pensions as they fall due.

Investment Strategy:

Policy Group	Target Weight 2024 - 2027	Permitted Range
Equities	27.5%	17 - 37%
Real Assets	10%	5 - 15%
Credit	4%	0 - 8%
Sovereigns	57.5%	47 - 67%
Cash	1%	0 - 10%
Total	**100%**	

Lothian Pension Fund: Buses Strategy

Investment Objective: to generate sufficient returns to pay pensions as they fall due.

Investment Strategy: to achieve its objective, the Buses Strategy invests in a proportion of the MEG Strategy and the Main Strategy that reflects the maturity of liabilities. This is currently ~~45:55~~50:50. Based on the Main Strategy above, the Buses Strategy will have the following exposures.

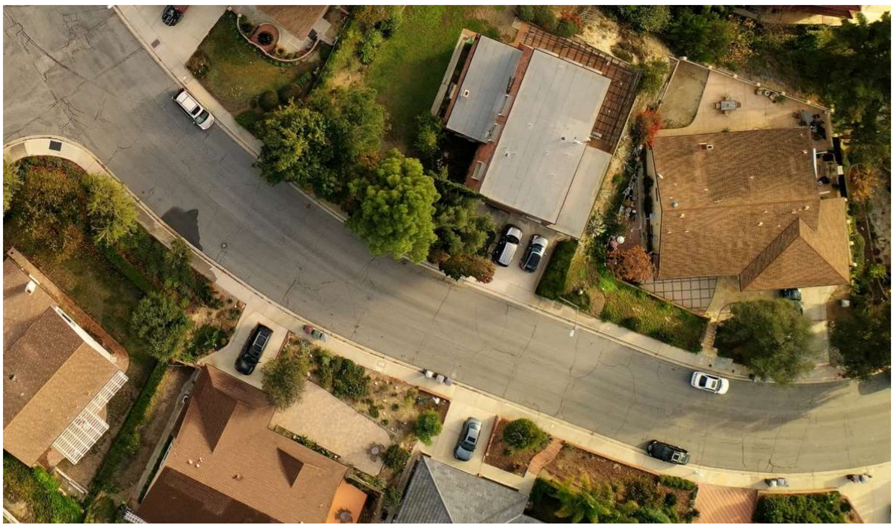
Investment strategy:

Policy Group	Target Weight 2024 - 2027	Permitted Range
Equities	27.5%	17 - 37%
Real Assets	10%	5 - 15%
Credit	4%	0 - 8%
Sovereigns	57.5%	47 - 67%
Cash	1%	0 - 10%
Total	**100%**	

Scottish Homes Pension Fund

Investment Objective: to match cash flows from gilt income and redemption payments as closely as possible with the expected liability payments of the Fund to minimise the risk of additional employer contributions being required.

Investment Strategy: all assets are invested in UK gilts and cash. As some liabilities are fixed in nature and some are inflation-linked, the Fund invests in both nominal and index-linked gilts to match cash flows with liability payments one year beyond the next actuarial valuation. Longer dated liability payments are duration matched.



Pensions Committee

2.00pm, Wednesday, 20 March 2024

2023/24 Business Plan and Budget Update

Item number 6.7

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 note progress of the Fund against the 2023-2024 Business Plan, together with specific updates on:

1.1.1. performance indicators

1.1.2. membership and cashflow monitoring

Alan Sievewright
Chief Finance Officer, Lothian Pension Fund

Contact: Jason Koumides, Financial Controller, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk| Tel: 0333 996 1900

2023/24 Business Plan and Budget Update

2. Purpose

2.1 The purpose of this report is to provide an update on progress against the 2023-2024 Strategy and Business Plan, performance indicators and the actions to enable the Fund to meet its key objectives.

3. Executive Summary

3.1 The 2023-2024 Strategy and Business Plan centres around four broadly defined strategic goals, each with more detailed objectives and accompanying targets and measures to allow us to monitor our progress and identify where interventions may be required.

3.2 They are:

- Develop and deliver a member and employer proposition for service excellence.
- Earn an appropriate risk adjusted investment return as responsible investors.
- Extend collaboration and services to existing partners and deepen where possible.
- Achieve greatness in our people, teams and culture.

3.3 The plan set out the work plans, budget and targets for 2023-24 and formed the base line against which performance would be and has been judged.

3.4 Matters to highlight in the main body of the report are:

3.4.1 All KPIs are on target as at 31 December 2023, with the exception of the pensions administration work where the performance is trending upwards, but still marginally below YTD target. ***(discussed in 4.3).***

3.4.2 Progress continues on process enhancements and accreditations. Additional committee papers provided detailed results of Actuarial Valuation (6.3-6.4) and resulting Investment Strategy review (6.6).

3.4.3 The quarter to December continued the trend in increasing the asset allocation to Gilts from Cash and Equities (4.23-4.27].

3.4.4 Sub-division work on the new office is complete, with fit-out work underway. The expected move date continues to be in Spring 2024 (4.37).

3.4.5 Forecasted financial outturn to 31 March 2024 (section 5) shows a projected £2,235k saving against the original budget. The two main contributors are savings from in-housing an investment management mandate from Harris and the reduction in costs from the cessation of Project Forth.

4. Main Report

4.1 LPF's year to date progress against its key performance metrics, laid out in 2023-2024 Strategy and Business plan, are detailed below.

	Q1 April to June	Q2 July to Sept	Q3 Oct to Dec	Target	Status
Customer Satisfaction, as measured by employers and members through survey results > 90% (12 month rolling)	93.9%	91.3%	91.5% (YTD 91.5%)	90%	✔
>92% of pensions administration work completed within standards	87.92%	87.43%	91.15% (YTD 89.01%)	92%	⚠
Data Quality, as defined by the Pensions Regulator achieve "common" and "conditional" data scores in excess of 95% and 95% respectively. The data is assessed as at 31 August 2022 (members' Annual Benefit Statements)	Pass			Pass	✔
The Fund operates within the approved budget	Within	Within	Within (YTD Within)	Within	✔
The audit of the Annual Report is unqualified	Unqualified			Unqualified	✔
Rolling 10-year fund return is >+5% pa unless the benchmark is <+5%pa, in which case, the relative return is positive	Pass	Pass	Pass (YTD Pass)	Pass	✔
Publish ENGAGE, Revised SIP and SRIP	Pass	Pass	Pass (YTD Pass)	Pass	✔
Mandatory LMS training completion rate >90%	100%	100%	100% (YTD 100%)	90%	✔
The Employee Engagement index KPI of 70% or above	79%	74%	74% (YTD 74%)	70%	✔

	Q1 April to June	Q2 July to Sept	Q3 Oct to Dec	Target	Status
Less than 10% unplanned employee turnover	9.2%	6.1%	6.1% (YTD 6.1%)	10%	✔

4.2 The Business plan also lays out functional plans for each team. Below provides further insight of each team's progress towards these goals.

Operations - Pension Administration performance indicators

4.3 Overall, Pension Administration have achieved 92.04% on a rolling 12-month calendar year basis. They are marginally below the year-to-date target (89.01% v 92%) and several factors have contributed to this including:

- The team is currently operating below the target headcount due to recruitment challenges. There are currently 4 open unfilled roles.
- Additionally, our teams currently consist of many trainees who require daily support, time out to study towards exams, to attend training and coaching sessions and need to have their work checked by a senior administrator which results in delays to cases being completed. The appointment of 2 new coaching roles is proving beneficial to assisting our trainees with queries and are a dedicated training resource to assist in upskilling our less experienced staff.
- Furthermore, due to internal secondments, creation of coach roles from our qualified administrator pool and some leavers, the administration team has lost some experienced colleagues. This has impacted our available resources to administer our most complex cases. Active recruitment activity and training are underway to backfill these gaps and we are making solid progress towards both our operational service targets as well as developing capability and contingency within the teams. Improved workflows have been introduced alongside a case ownership model, providing a single point of contact for customers and a more efficient use of our resources. Daily check ins by each team manager are helping to address any workload issues and to ensure work priorities are being met.

Accreditation

4.4 The Fund has held the Customer Service Excellence (CSE) standard for several years. To achieve CSE accreditation an independent assessment takes place against 5 sets of criteria and 57 separate elements. These are then assigned a rating – non-compliant, partial compliant, compliant, or compliant plus.

4.5 LPF's on-site assessment last took place in March 2023. The assessor evaluated evidence with regards to processes and service delivery, observing the interaction the Fund has with its members and employers. Not only did the Fund retain its fully compliant status but an additional 2 compliance plus levels were awarded bringing its total to 9 at the highest recognition level. We are currently finalising this year's evidence for submission and an independent assessor will visit LPF on 26 March as part of this accreditation process.

4.6 LPF has held the Pensions Administration Standards Association (PASA) accreditation since 2017. To achieve the award, an independent assessment against 10 sets of criteria and standards takes place. In October, a comprehensive submission was provided to the independent assessors as per the requirements of the triannual review with detailed supporting evidence. This was followed by a site visit in November to validate this evidence through observation and interviews with a random selection of colleagues from across all teams. A final review with recommendations was expected by the end of the calendar year, however, due to assessor absence there has been a delay in receiving their decision on our accreditation position. We will update the Committee as soon as this has been received.

Customer Experience Team

4.7 As a result of reviewing the experience of bereaved members and the use of Customer Journey Mapping, improvements and efficiencies have been introduced within the death procedure, including the option to upload documents securely on-line our website which links directly to the pension system itself and the associated member's record. A new customer satisfaction survey has been launched to gather insights and to help identify opportunities to improve their experience when interacting with us, across all channels.

4.8 The Member Services Coaches provide training, guidance and coaching to Member Administrators, Trainees and Assistants. The coaches updated existing and created new training slides and procedure manuals, delivering around 50 training sessions since August 2023, which covered key processes such as retirements and deaths. The coaches respond to all queries, whilst observing and assessing work activities and developing capability on an individual basis.

A training matrix combined with a skills and development plan has been created for all members of staff within the Operations Team to maintain a schedule of training needs, meet and track training requirements as well as support resource management decisions.

The coaches were used as a dedicated resource for McCloud remedy underpin checks; that all identified cases had a positive underpin and we can now progress with individual calculations for those in scope.

Digital Enhancements

4.9 Last year a digital process, in partnership with Crown Agents Bank (CAB), was introduced for our overseas pensioners to complete their annual existence check. The new process using biometric facial recognition allows members to complete the exercise from home using their laptop or mobile device by taking a live photo of themselves and their photo ID such as a passport. This year's exercise is almost complete, and the results again have been extremely encouraging with 87% of members using the digital process method so far.

4.10 We have recently completed the process of transferring our overseas payment services to CAB in December 2023. Prior to the change of provider, our overseas pensioners would not receive their monthly payment until a few days after the standard payment date. Our new arrangement has allowed us to align the pension payment date for overseas members with that of our UK-based members, ensuring that all pensioners now receive their payment on the 15th of each month. We are currently working on the set up of a self-service portal to allow overseas pensioners to view their payments online.

Actuarial Valuation

4.11 The Local Government Pension Scheme (Scotland) Regulations 2018 require the 2023 Actuarial Valuations to be completed within one year of the valuation date, i.e. by 31 March 2024. Specific papers and final valuation reports are included under Agenda items 6.4 and 6.5.

Employer Performance

4.12 The Fund's Pensions Administration Strategy (PAS) sets out employer roles and responsibilities under the Regulations and timescales for provision of information to the Fund. Fund officers continue to provide training to employers so that they have the knowledge required to meet these requirements. An employer guide which provides more detailed guidance on administration processes has been produced and at the time of writing is under final review.

4.13 Officers continue to refine processes and following software upgrades and enhancements in 2023, which streamlined the early leaver process for employers, are now reviewing the retirement process. A change to the portal will allow similar efficiencies and lead to an improvement in performance.

AVC Review

4.14 Committee will be aware that the Fund's current provider for Additional Voluntary Contributions (AVCs) is Prudential. Some members also contribute to AVCs with Standard Life, but no new members are permitted to join the Standard Life scheme. A review of the current provision will be carried out in 2024, and it is intended that this review will utilise a framework currently being developed by the

National LGPS Frameworks. Committee will be updated on progress of this review later in the year.

McCloud

4.15 Since the employer data collection was completed, we have interfaced service changes and breaks as provided by the employers followed by preparations for the bulk underpin calculation. We have identified and updated records for all those in scope.

4.16 As McCloud is a material change to the scheme, we were required to contact those who are or could be affected. In December 2023, we contacted approximately 38,000 members to provide information about the remedy and to request other public sector service to bring more members into scope.

4.17 The first bulk underpin reports identified 500 records where additional pension may be due under McCloud. Many of these records have been checked by the member services coaches and then by the data analysts. In addition, the coaches have provided training for member services teams on this topic. Once the checking is complete, we will be able to run the actual underpin calculation and start recalculating pensions.

Pensions Dashboard

4.18 The UK Government's vision is that the Pensions Dashboard will enable individuals to assess their pensions information online, securely, and in one place to support better planning for retirement and growing financial well-being. Lothian Pension Fund, as a data provider will be compelled to supply data to the ecosystem once live.

4.19 The ministerial statement in June 2023 delaying the deadline connection date by one year to 31 October 2026 was ratified by amendment regulations that came into force in August 2023. However, the DWP (Department for Work and Pensions) have still to announce revised staged connection dates for each pension scheme type, the previous regulations having stated this as 30 September 2024 for all public sector schemes.

4.20 To connect to the Pensions Dashboard ecosystem, schemes will need to procure an Integrated Service Provider (ISP), their services include connection to the ecosystem and data analytics. We are currently awaiting on National LGPS Frameworks launching the procurement framework for the ISP. Their last communication indicated they hoped to deliver this early in the New Year and this is still currently awaited.

4.21 In the meantime, we continue to monitor the quality of our data using other tools such as that used for the Pensions Regulator data quality checks. When the Pensions Dashboards are live, it is a requirement that in-house Additional

Voluntary Contribution providers return their value data at the same time to the end user as the value data to the pension scheme. We plan to contact both our providers and undertake a data cleanse between the sets of data.

Investments - Asset Allocation

4.22 The Fund's assets broken down by policy group at 30 September and 31 December 2023 are shown in the table below.

30 September 2023 £'000	Policy Groups	31 December 2023 £'000
5,362,801	Equities	5,547,450
2,101,409	Real Assets	2,113,337
575,406	Non-Gilt Debt	582,462
836,455	LDI (Gilts)	1,076,508
232,502	MEG (Mature Employers)	254,443
392,222	Cash	322,193
9,500,795	**Total**	**9,896,392**

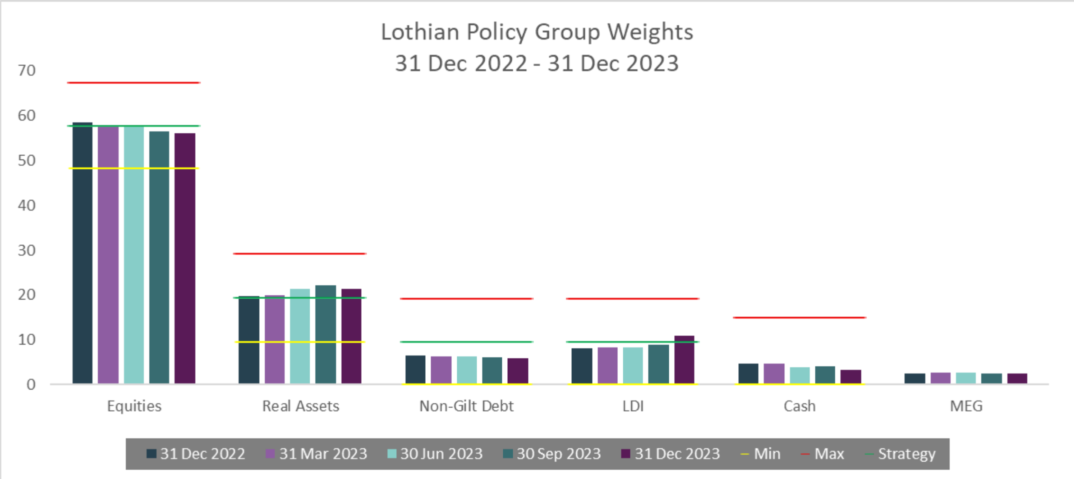
Source Northern Trust

4.23 The Fund's long term performance is strong compared to benchmark, demonstrated in the table below detailing the 3, 5, 10 year and since inception (Oct 93) returns against benchmark.

	3 Yrs	5 Yrs	10 Yrs	ITD
Performance	5.51%	6.04%	8.04%	7.91%
Benchmark	-1.17%	5.01%	6.86%	7.27%

4.24 Total Fund assets increased by c.4% over the quarter as both equity and bond prices rose. The Fund continued to reduce exposure to equities and cash to allocate c.£100m/1% of total assets to Index-Linked Gilts during the quarter. At 31 December 2023, relative to the strategic asset allocation, the fund was underweight Equities and Non-Gilt Debt, and overweight Real Assets, Gilts and Cash.

4.25 The green lines in the bar chart below represent the strategic allocation to each policy group and the yellow and red lines show the ranges within which officers are permitted to operate. The bars show the trends in allocation weights to the five policy groups (and the mature employer group) over the last five quarters to end December 2023. All policy groups remain comfortably within the agreed ranges. Should policy group weights move outwith those ranges, officers are required to report this to the Pensions Committee.



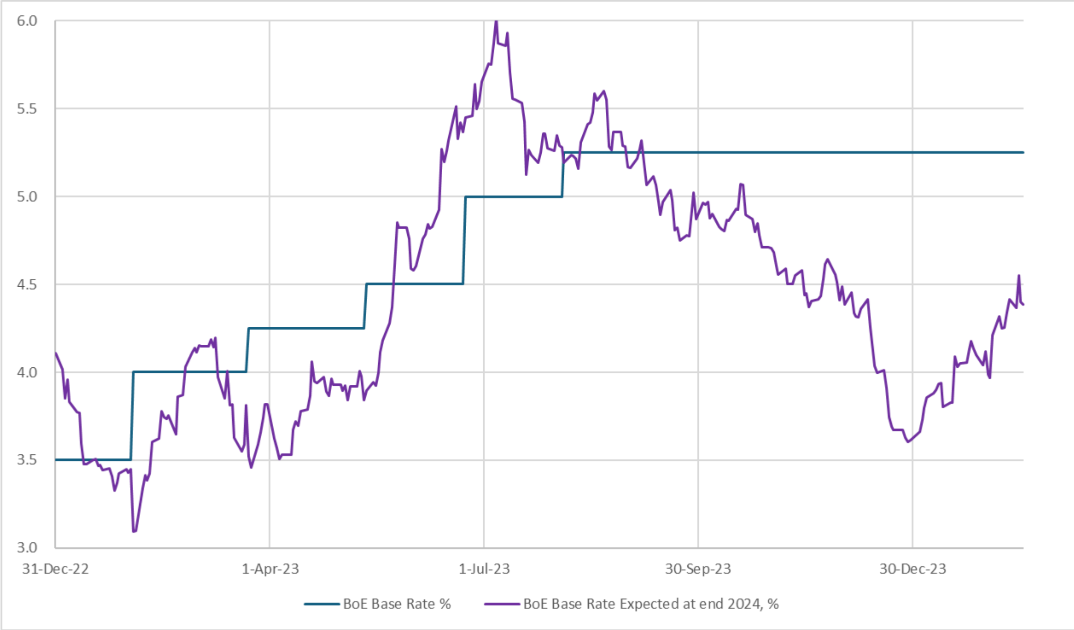
Source Northern Trust, LPF calculations

Activity

4.26 The main changes to asset allocation over the last several quarters have been increases in the weights of Index-Linked Gilts and Real Assets and the reductions in Equities and Cash.

4.27 After a long period of being underweight Index-Linked Gilts, prices have weakened very significantly and now offer a reasonable long term real yield, hence the increased weight. In the Real Asset policy group, the Fund has continued to invest consistently in a diverse range of infrastructure and property assets with some prices having weakened in recent quarters as a result of the sharp rise in interest rates.

4.28 Major central banks are now expected to cut interest rates during 2024 as inflation pressures reduce. As an example, the chart below shows the Bank of England (BoE) base rate (blue line) as well as market expectations for this rate at the end of 2024 (purple line) throughout 2023; the large fall in the latter during the last quarter of 2023 drove the increase in equity and bond prices. Any reduction in this rate is likely to be reflected in the increase in the valuation of scheme liabilities, thereby reducing the surplus, all other things being equal.



Source Bloomberg

Investment Strategy Review

4.29 The investment strategy review has run in parallel with the actuarial valuation and proposals for updating the strategic asset allocation are covered at agenda item 6.6.

Risk & Compliance - Risk Management Framework

4.30 The plan to improve and embed the risk management framework continues to progress with the development of the suite of LPF operational functional risk profiles. Completion of these risk profiles will help determine a controls assurance programme which will compliment other existing oversight activity. Additional resource with a broad remit to review and improve the existing Investment and Front Office Compliance environment has also been onboarded into the R&C team. Enhancements to the existing universe of compliance tests within the Investment Management System ("CRIMS") have been introduced. A full review of the completeness and accuracy of these compliance tests is underway and will help drive improvements around operational efficiency and resiliency. More details are provided in the Risk and Compliance update to committee covered in agenda item 6.13.

Information Governance and Supplier Management

4.31 With support from Legal, the Information Governance framework has been improved with the development and embedding of refreshed policies and procedures which in-line with legal and regulatory requirements and CEC's expectations. The Risk Management Group have oversight of compliance with key obligations such as: data breaches, subject access requests, data protection assessments, and freedom of information requests.

4.32 Supplier performance and third party oversight arrangements continue to be improved through changes made to the supplier management framework recommended from the internal audit review in 2023. Further work is required to review and enhance the basis of arrangements and oversight between CEC as service provider and LPF. The Risk Management Group's terms of reference now also include oversight of critical suppliers and operation of the framework. General training will be delivered to all Fund staff shortly, with dedicated training for owners of critical supplier relationships.

Finance - General Ledger System

4.33 As a result of a competitive tender process and an independent assurance review the Fund awarded X-Ledger a contract to provide a finance system for LPF and its 2 companies LPFE and LPFI. Oracle (provided by CEC) is used to record LPF's financial transactions.

4.34 A 2-stage process for implementation was agreed, with the onboarding of LPFE/I completed in September. The Fund is targeting to onboard LPF and SHPF on to X-Ledger from 1 April 2024. Discussions are taking place with CEC to agree timing in relation to the handover and provision of information to meet this deadline.

4.35 Year to date financial transactions have been imported to Xledger for LPFE/I so full financial statements can be produced for the 2023/24 financial year. Staff training has been rolled up, with efficiencies and improvements being investigated for financial and budget monitoring.

4.36 LPF and SHPF 2023/24 financial year end reporting will be completed on Oracle before opening balances are transferred to X-Ledger.

Projects - Project Forth

4.37 As a result of previous Committee decisions, work on Project Forth has ceased. For 2023/24 financial projection associated costs/income have been removed.

4.38 The collaborative relationship with Falkirk remains in place, with an additional equities mandate onboarded during Q3 bringing total assets under management of LPFI to over £1.8b.

Office Relocation

4.39 The lease for the new premises began on 8 December 2023 when the sub-division work completed, triggering the commencement of a rent-free period. A building contractor is currently undertaking the fit-out of the new office. Final costing are expected to be in line with budgeted assumptions and work is scheduled to complete by April 2024, with occupation from Spring 2024 as expected Progress is underway to secure a new tenant for the current office in Atria One. The landlord's scheduled rent review has hampered the re-let exercise but the review process is nearing completion, and this will provide clarity on the rent payable by any new tenant.

5. Financial impact

5.1 A projected underspend of £2,235k is expected for the year as per the projected and year-to-date financial outturn compared to the approved 2023/24 budget shown in the table below:

Category	Budget	Projected Outturn	Projected Variance	Budget to date	Actual to date	Variance to date
	£'000	£'000	£'000	£'000	£'000	£'000
Employees	8,344	8,243	(101)	6,258	5,121	(1,137)
Transport & Premises	577	577	-	433	374	(59)
Supplies & Services	2,768	2,638	(130)	2,076	2,022	(54)
Investment Managers Fees -Invoiced	3,850	2,500	(1,350)	2,888	1,600	(1,288)
Other Third-Party Payments	2,583	1,518	(1,065)	1,938	921	(1,017)
Central Support Costs	732	732	-	549	549	-
Depreciation	227	227	-	170	138	(32)
Gross Expenditure	**19,081**	**16,646**	**(2,646)**	**9,541**	**7,394**	**(3,587)**
Income	(2,621)	(2,210)	411	(1,966)	(1,171)	795
Total Cost to the Funds	**16,460**	**14,225**	**(2,235)**	**12,346**	**9,554**	**(2,792)**

5.2 The financial outturn includes year to date budget, actual expenditure and variance as at the end of December 2023. Year to date actual expenditure includes provision for services incurred but for which no invoice has yet been received.

5.3 The key variances against budget remain unchanged from previous quarter, and are:

5.3.1 Investment Managers Fees - Invoiced - £1,350k underspend. In July the Fund terminated the externally managed mandate of Harris bringing the resulting funds into inhouse management. It is important to highlight that this was an investment led rather than cost led decision. The CIO will review the impact of this on internal resources/staffing headcount which will be quantified in forecasting for 2024/25. As the investment strategy paper sets out the mix of internal and external fund management is kept under constant review with a clear framework to guide decisions on the mix.

5.3.2 Other Third-Party Payments - £1,065k underspend. Due to the pausing of Project Forth all related costs have been removed from the forecasted outturn for the year. This accounts for a majority of the underspend.

5.3.3 Income - £411k below budget. As with Other Third-Party Payments below budgeted income is expected due to the pause on Project Forth. Additional costs associated with the project were expected to be shared and recharged back to Falkirk. This income has been removed from projections.

5.3.4 Supplies & Services – £130k underspend. Miscellaneous underspends expected for system, legal, and other costs.

5.4 A number of factors have contributed to a variance to date underspend of £2,792k. As above the pausing of Project Forth and the termination of the external managed Harris mandate have led to underspends in Third- Party Payments and Investment Manager Fees. Although Employee costs are forecasted to be broadly in line with budget, year to date there is a variance £1,137k, a majority of which is a timing difference relating to variable pay arrangements. The current budget allocates an even proportion of costs to each period of the year, rather than based on when expenses are due. The Fund will introduce a phased approach to budgeting in the new financial year where budget will be allocated to periods expenses due.

Membership and Cashflow monitoring

5.5 A high-level summary of the cashflows from dealing with members as at the end of December 2023 and projections for the rest of year are shown below. These have been prepared on a cashflow basis (compared to the accruals basis of the year-end financial statements and budget projections) with prior year figures for comparison.

2022/23 Actual £'000		2023/24 YTD £'000	2023/24 Projected £'000
265,122	Contributions Received	205,153	290,000
(282,713)	Benefits Paid	(235,152)	(308,000)
(17,591)	**Net Additions/(Deductions) From Dealings with Members**	**(29,999)**	**(18,000)**

5.6 2023/24 projected cashflow is broadly in line with expectations. With Lothian Pension Fund's maturing membership profile, pensioner payments are expected to increase over the period as pensioner numbers grow. This coupled with the pensions increase award in April of 10.1% an increase in expenditure compared to the prior year was expected.

5.7 While for the foreseeable future Lothian Pension Fund expects to have a negative cash flow position, whereby pension payments exceed total contributions received, current levels of investment income provide multiple cover for negative net pensions cash flow. Therefore, no asset sales will be required for the foreseeable future to fund on going pensioner payments.

5.8 The expectation is the contributions for 2024-2027 will be lower than current levels, an initial estimate is that deductions from dealing with members will be c£70m in 2024/25 We are looking to review and improve cashflow monitoring and liquidity management. This becomes more important as the gap between contributions and benefits grows.

6. Stakeholder/Regulatory Impact

6.1 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. Background reading/external references

7.1 LPF Strategy and Business Plan 2023/24

7.2 LPF Investment Strategy

8. Appendices

None.

Pensions Committee

2.00pm, Wednesday, 20 March 2024

2024-5 Strategy & Business Plan

Inc. Functional Plan and Budget

Item number 6.8

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 approve the Strategy and Business Plan for 2024-25;

1.2 approve the respective budgets, as detailed in the Financial Projections section of appendix 1, for:

1.2.1 LPF Group business as usual 2024-25; net expenditure of £15,790k (2023/4: £15,267k).

1.2.2 Strategic project costs relating to the office relocation of £125k (2023/4: £1,193k relating to office relocation and Project Forth).

1.3 note the indicative budget for 2025-26; net expenditure of £16,711k.

David Vallery
Chief Executive Officer, Lothian Pension Fund

Contact: Jason Koumides, Senior Finance Manager, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Strategy and Business Plan for 2024 – 25

2. Executive Summary

2.1 The Strategy and Business Plan sets out the proposed medium-term strategy for LPF and the business priorities for calendar years 2024-25. It also sets the budget and performance targets for the financial year 2024-25.

2.2 The indicative budget for 2025/26 shows the anticipated full year costs of changes proposed in 2024/25 primarily recruitment, pay reviews and office costs.

2.3 The overall strategy remains the same and articulated in four strategic goals:

2.3.1 Develop and deliver a member and employer proposition for service excellence

2.3.2 Earn an appropriate risk adjusted investment return as responsible investors

2.3.3 Extend collaboration and services to existing partners and deepen where possible

2.4 Foster great teams and a great work environment. Section 4.7 collates the key priorities under these strategic goals, the key themes of the priorities are:

2.4.1 Reviewing the team structures and resourcing needs, and recruit and retain well trained staff to meet evolving needs and build in additional resilience across the teams.

2.4.2 Continuing to focus on service and investment excellence.

2.4.3 Furthering investment alignment with Fife and Falkirk pension funds to simplify operations and gain further efficiencies to the benefit of all 3 funds.

2.4.4 Continuing to evolve and improve governance standards and our approach to risk management.

2.5 The Key Performance metrics in appendix 1 and the Service Performance Indicators set out in appendix 2 of the 2024 – 2025 Strategy and Business plan are consistent with the 2021-23 plan. Some of these targets are being reviewed and although no major changes are expected any revisions will be tabled at the Pension Committee in June for approval.

3. Main Report

Strategy

3.1 The proposed Strategy and Business Plan for 2024-25 is provided as Appendix 1.

3.2 The Boards of LPFE and LPFI have been consulted during the development of this plan and are supportive of it. If approved by the Committee, then the relevant aspects will be considered formally by the Boards of LPFE and LPFI with the expectation that they will be approved. This includes the update of the regulatory business plan of LPFI.

3.3 The Plan opens with an articulation of the Purpose, Vision and Values (“PVV”) of LPF. We regard these as being enduring and there is no change being made. The aim is that all colleagues can articulate the PVV and understand the role they play in delivering them for the benefit of our members and employers. We recognise further work is required to achieve this.

3.4 The Strategic section articulates the strategic goals, and within these strategic priorities for LPF. Again, these remain substantially the same:

3.4.1 Develop and deliver a member and employer proposition for service excellence
3.4.2 Earn an appropriate risk adjusted investment return as responsible investors
3.4.3 Extend collaboration and services to existing partners and deepen where possible
3.4.4 Foster great teams and a great work environment.

3.5 The last goal has been re-articulated from “Achieve greatness in our people, teams and culture”.

3.6 Attention is drawn to the maintaining the goal of collaboration. It is worth highlighting that this is where collaboration benefits LPF in the pursuit of its purpose. Collaboration is not a goal in itself.

3.7 The Business Plan document provides an overview of the planning process followed and includes a recap of 2023 to provide context.

Business Plan

3.8 Whereas the strategy, purpose, vision and values are expected to remain constant, the Business Plan is intended to capture specific projects and initiatives designed to deliver the strategy and set out the operating parameters.

3.9 The business plan document sets out what are described as functional plans. These describe the key priorities and initiatives of each function and department and summarise more comprehensive functional plans that have been created for use within the teams. Collectively these ensure there is clarity of the priorities of each team and alignment both up and down and across the business. These have then been grouped under the strategic priorities noted above.

3.10 Strategic Priorities

3.10.1 **Develop and deliver a member and employer proposition for service excellence**

- Project delivery: complete McCloud and be ready for the launch of the Pensions Dashboard
- Recruit experienced administrators, improve capability and upskill teams
- Work with employers to improve performance and collaboration
- Continue service improvements: eliminating complexity and unnecessary friction in internal processes, explore automation, and operate with clear information accessible across multiple channels.
- Maintaining PASA and CSE accreditation; utilise insights from CEM benchmarking

3.10.2 **Earn an appropriate risk adjusted investment return as responsible investors**

- Implementation revised strategic asset allocation and complete review and any rebalancing within policy groups
- Team structure and resourcing
- Continue and enhance our approach to Responsible Investment
- Continue to support partner funds via LPFI and further alignment of portfolios
- Maintain FRC Stewardship Accreditation
- **Foster great teams and a great work environment** Re-locate to our new office; better suited to the needs of our colleagues
- Recruitment and retention; training and development; talent management and succession planning
- Supporting organisational design to support evolving needs
- Continuing to support a fully inclusive culture and providing our colleagues with the tools, education and capacity to do so

- Supporting our communities, making sure each of our colleagues have two days annually to spend giving back to their communities in the manner they chose.

3.10.3 **Governance, Legal, Risk and Compliance**

- Review and operate to the requirements of the new tPR General Code of Practice (and other governance reforms)
- Continue the development and improvement to governance operating model, frameworks and practices
- Complete risk management framework uplift
- Undertake a comprehensive governance review
- Maintain Cyber Essentials Plus accreditation

3.11 The Plan sets out financial forecasts and the assumptions on which these are based. This is described in the following section.

Functional Plan and Service Metrics

3.12 The Plan includes as appendix 1 the 'Key Performance Metrics'. These were previously labelled the operational goals and measures. These form a focused 'balanced scorecard' covering all aspects of LPFs performance. They also form the basis for the variable pay component for colleagues.

3.13 Appendix 2 lists the 'Service Performance Indicators'. These remain unchanged from 2023/24. It is recognised that delivery against these can be impacted by the performance of employers, for example late delivery of notification of leavers and joiners, as well as by our performance.

4. Financial impact

4.1 The respective budgets for LPF Group are detailed in the Financial Projections section of appendix 1.

4.2 The proposed total business as usual budget represents a £523k increase to the comparable 2023/24 budget, however with the inclusion of strategic project costs, then the total budget represents a £545k reduction on last year. This is broken down in the below table -

	Budget 2023/24 £000	Movement £000	Budget 2024/25 £000	Indicative 2025/26 £000	Indicative 2026/27 £000
Employees	7,997	1,589	9,586	10,275	10,789
Plant and transport	306	475	781	820	861
Supplies and services	2,742	158	2,900	3,045	3,197
Third party payments	1,519	100	1,619	1,700	1,785
Investment managers fees – invoiced	3,850	(1,150)	2,700	2,835	2,977
Support costs	732	36	768	806	847
Capital funding	197	51	248	248	260
Gross expenditure	**17,343**	**1,259**	**18,602**	**19,730**	**20,716**
Income – collaboration	(1,966)	(736)	(2,702)	(2,909)	(3,054)
Income – other	(110)	-	(110)	(110)	(110)
Total income	**(2,076)**	**(736)**	**(2,812)**	**(3,019)**	**(3,164)**
Net expenditure	**15,267**	**523**	**15,790**	**16,711**	**17,552**
Percentage movement			**3.43%**	**5.83%**	**5.03%**
Strategic project costs	**1,193**	**(1,068)**	**125**	**-**	**-**
Total net planned expenditure	**16,460**	**(545)**	**15,915**	**16,711**	**17,552**

4.3 Key changes from previous year's budget comprise the following:

Employees

4.3.1 £1,589k increase on last year's budget. Changes of note being –

4.3.1.1 Inclusion of 9 vacancies including Investment and Research Analysts, additional resource in the Employer Services Team, Project resource for Data/Cyber and Business Continuity and Supplier Management. These roles are a response to the increasing requirements within the business. Any new role requires completion of a business case prior to the commencement of recruitment.

4.3.1.2 Full year provision for roles recruited in 2023/24 to improve the resilience of the fund and pay reviews. These are in line with the recommendations and approvals made by the LPFE Board.

4.3.1.3 The indicative budget for 2025/26 shows an increase of £689k. This provides for a full year salary for new roles anticipated in 2024/25 and a full year of salary uplifts assumed to be around 5%.

Investment Management

4.3.2 £1,150k decrease in relation to invoiced fees as a result of in-housing the Harris equity mandate. Externally managed mandate fees are based on market value. Changes in mandate and internal / external mix are driven by investment strategy and objectives, and consider expected investment return after fees. They are not made on narrow cost grounds.

4.3.3 The Fund continues to benefit from the cost savings associated with the majority of assets being managed inhouse. We continue to estimate these savings as being in excess of £25m per annum. This amount is annotated within the plan as being contingency costs if the internal model was to cease.

Transport and Premises

4.3.4 A majority of the £475k increase reflects the move to the new office. The annual costs are in line with the costs previously highlighted to committee.

Strategic Project Costs

4.3.5 £1,068k decrease in overall budget, due to –

4.3.5.1 Project Forth costs being removed from the budget following the cessation of the project.

4.3.5.2 Office relocation – due to the timing of the office move some project costs have been carried forward into the new financial year. Removal, dilapidation and Atria overlap costs are expected in Q1 2024/25.

4.4 Increases in supplies and services, third party payments and support costs can mostly be explained by increased headcount which has a knock-on effect on training, system license etc. This coupled with CPI uplifts on existing contracts has caused slight increases in these budgets.

Membership and Cashflow monitoring

4.5 High-level projections of cashflows from dealing with members for 2023/24 to 2026/27 are shown below –

	2023/24 £000	2024/25 £000	2025/26 £000	2026/27 £000
Contributions Received	290,000	252,000	264,600	277,830
Benefits Paid	(308,000)	(329,000)	(352,030)	(376,672)
Net Additions/(Deductions) From Dealings with Members	**(18,000)**	**(77,000)**	**(87,430)**	**(98,842)**

4.6 As a result of the improvement in funding level in the most recent triennial valuation a decrease in employers' contributions has been forecast. The proposed contributions are subject to Pension Committee approval on 20th March. This coupled with the annual pensions increase exercise and the aging profile of the pension fund (increasing number of pensioners) the net deductions from dealing with members is expected to increase to around £77m in 2024/25.

4.7 The investment income anticipated from assets will cover this shortfall with ease.

5. Stakeholder/Regulatory Impact

5.1 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.

5.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report.

6. Background reading/external references

6.1 None.

7. Appendices

Appendix 1 – Key changes to the Business Plan document from prior year
Appendix 2 – Draft Lothian Pension Fund Strategy and Business Plan 2024-2025

Appendix 1 - Key changes to the Business Plan document from prior year

To aid review and approval of the document a list of key changes from prior year has been provided. This is not an exhaustive list of amendments but should focus the reader on the key parts of the document.

- Pages 5 & 6 - David has fully updated the review of the year to reflect the key achievements in 2023.
- Page 7 - There have been minor amendments to the planning process to reflect the updated status of Project Forth
- Pages 8-11 - The strategic goals have been updated to reflect the key priorities for the year under each of the strategic goals and the title of the 4th strategic goal has been re-worded to "Foster great team and a great work environment" (from "Achieve greatness in people, teams, and culture").
- Pages 12 & 13 - The strategic priorities have been updated to remove references to Project Forth and to reflect the current status of office move, McCloud and pension dashboard developments. Good governance and embedding best practise have been added as a strategic priority, this was discussed at the training on 7th March.
- Pages 14 & 15 - Minor amendments have been made to the narrative relating to LPFI and LPFE. LPFI narrative has been updated to reflect the change in FCA classification as well as the intentions for 2024/25.
- Pages 16 & 17 - operating budget and cash flow forecasts have been updated to reflect current positions.
- Pages 18–22 – functional plans updated to reflect priorities for the year.
- Page 23 – Projects & Change – updated to reflect current status of projects.
- Page 24 – Organisational Design – breakdown of functions amended to reflect reporting to LPFE board and narrative. The updated figures were discussed at the sessions in February and March.
- Pages 25 & 26 – substantially changed with narrative which reflects risks to current plan and external factors/developments.

This page is intentionally left blank

Appendix 2

LOTHIAN PENSION FUND

STRATEGY AND BUSINESS PLAN

2024 - 2025

CONTENTS

Foreword	2
Introduction	4
Purpose, vision and values	
A review of 2023	
Our planning process	
Strategy	8
Strategic goals	
Strategic priorities	
Corporate entities	
Financial projections	16
Functional plans	18
Investments	
Pension Administration & Member Services	
IT & Change	
Governance, Legal, Risk and Compliance	
Finance	
People & Communications	
CEC Shared Services	
Projects and change	23
Organisational design	24
Risks	25
Appendix 1: Key performance metrics	27
Appendix 2: Service performance indicators	28

FOREWORD

About us

Lothian Pension Fund (LPF) has been around in its current form since 1975 and has helped more than 75,000 local government workers and their families to experience a financially secure retirement. We expect to be here to provide for the beneficiaries of the youngest members of our Fund today, so we need a plan that sets out how we'll achieve the sustainability that such multi-generational obligations require.

Through our service and employment company LPFE, we administer the LGPS in Edinburgh and the Lothians and are one of approximately a hundred local government pension scheme (LGPS) funds in the UK, and the second largest LGPS fund in Scotland. We're an asset-backed and multi-employer scheme with around £10 billion of assets and we were 157% funded at our last valuation in 2023. We're proud to serve over 90,000 members and 65 contributing employers.

LPFI, our regulated asset management company, provides investment advice and management to partner LGPS funds sharing costs and expertise to the benefit of both LPF and these partners.

Secure benefits

The benefits that we administer are protected by statutory provisions. That means earned pension benefits from past service are as secure as other Government-backed commitments. The future benefits could be amended by changes to the LGPS and this could result from: a change in policy towards public sector pensions; affordability concerns; or to ensure they remain fair for all beneficiaries.

A changing world

The world surrounding us is changing and the opportunities to become more efficient and easier to interact with are increasingly attainable through technology advances. Our members have high expectations of all organisations they interact with when it comes to being straightforward to deal with, courteous, professional, and consistent in delivering on the promises we make. Although membership of the LGPS is bundled with their eligible employment, we must never become complacent or believe that members will tolerate second best service for guaranteed benefits.

The employers who sponsor our members are changing too. The benefits of LGPS are valuable, but come at considerable cost to employers, many of whom are contending with financial constraints. The benefit to employers of providing the LGPS to their people must continue to be greater than the cost to them of that membership or we face a threat to the long-term future of the LGPS.

But it's in the investment markets where we continue to see great changes. The activity of investing in assets for returns that will exceed inflation in the long-term has always relied on judgement, manager skill, diversification, and patience. Today is no different, but judgement, management and patience are especially challenged by climate risk assessment, other environmental, social and governance issues, and the distribution of information and misinformation in this age of social media. We must exercise our fiduciary duty with due awareness of the complex dynamics of investing in a changing world to be able to provide benefits for members and their sponsoring employers.

We remain aware of the potential for structural review of the LGPS in Scotland that might have implications on pension provision. We shall respond positively to any developments, whilst also noting the potential consolidation of multi-fund LGPS employers where there is a case for rationalisation. Conversely, we'll consider the risks of employers and members through such exercises and understanding the potential impact on LPF and possible risk mitigants and defensive strategies.

Our Strategy and Business Plan

Our passion and energy come from our motivation to deliver for our members. The following pages set out a summary of our Strategy and Business Plan.

INTRODUCTION

We have a clear purpose, vision, and values.

Our purpose

To administer the LGPS in Edinburgh and the Lothians. By paying pensions and benefits to members, we help with the financial well-being of members and their families in retirement.

We invest the scheme's assets, seeking to earn an appropriate return that will reduce the cost of the scheme to employers and improve the sustainability of the LGPS. By investing responsibly, we seek to ensure that companies meet and manage environmental, social and governance standards, including those relating to the climate change threat and the need to transition to a net zero world.

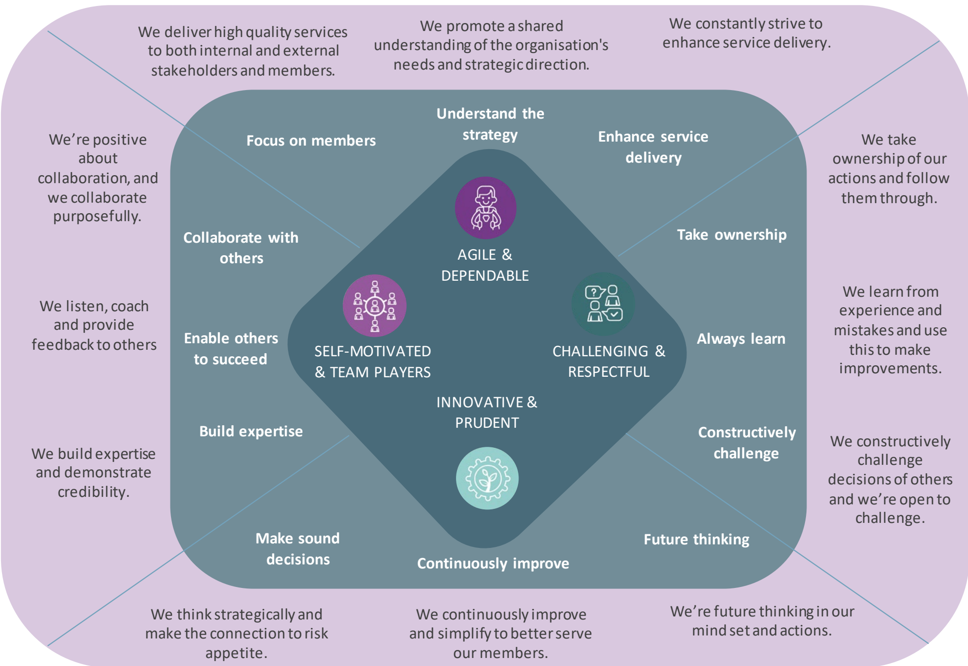
Our vision

To deliver outstanding pension and investment services for the benefit of members and employers.

Beyond this we aspire to be the best LGPS in Scotland, if not the UK, in terms of meeting the needs of members and employers, in using our influence as a leading responsible investor, and offering a superior employment proposition to our colleagues.

Our core values

We're passionate about pensions and our values are enduring principles that inform, inspire and instruct our day to day behaviour.



A REVIEW OF 2023

2023 was a successful and award winning year for LPF. In September we were proud to win the LGPS Fund of the Year at the LAPF Investment Awards 2023. Shortly after, we were recognised by the Sustainable Finance Disclosure Rewards for Asset Owners (SFDR4AO) as a leading pension fund for our approach and disclosure on gender. Being recognised by peers and external specialists helps affirm we're on the right path to achieving our vision: "*to deliver outstanding pension and investment services for the benefit of members and employers."*

During the year we retained the Pension Association Standards Award (PASA) accreditation, maintained our Customer Service Excellence award with increased scores, and reported 94.7% overall customer satisfaction in our annual surveys.

We made great progress towards our vision of delivering outstanding pension and investment services, as confirmed by independent benchmarking and industry accreditations:

- CEM's pension administration analysis shows that LPF delivers a high level of above benchmark service at below benchmark cost
- Meanwhile its investment benchmarking continues to report that LPF's investment costs are significantly lower than its global peer group and CEM Local Government Pension Scheme (LGPS) universe. Over the long-term, LPF has delivered investment returns above its peer group with a lower level of risk and at lower cost.

'Continuously improve' is one of our core values, and each of our teams have lists of achievements and improvements in 2023. In July we delivered 100% of the 56,930 benefit statements to our members and did so three weeks earlier than the previous year. We continue to invest in our risk management processes, recognising the responsibilities we have and the multitude of financial and operational risks we face. Cyber attacks are extremely likely and can cause tremendous damage, so we were pleased to achieve our Cyber Essentials Plus accreditation in March, which gives confidence in our defences. We won't be complacent in this area.

As important as strong benchmarking is, our core purpose is paying benefits to members and their dependents. During 2023 we paid out £172m in pensions to 36,504 members, a further £46m in retirement lump sums and £8m in death grants and we were delighted to welcome 5,426 new members. We're delighted that our members reported 91.3% overall customer satisfaction whilst again continuing to invest in improvements. During the year we introduced biometric facial technology and a payments portal which simplifies and improves the process for overseas pensioners.

The triennial actuarial valuation of the scheme at 31 March 2023 shows a strong funding position of 157% (107% 2020). The funding position improved through higher achieved investment returns over the period, as well as higher expected future investment returns which increased the discount rate used to calculate the value of the liabilities. Whilst recognising this is a point in time valuation, the strong position has enabled the Pensions Committee to propose a reduction in contribution levels for the majority of employers. A review of the investment strategy has been running concurrently and we'll propose some modest changes to strategic asset allocation whilst maintaining the core tenets of a large majority of return seeking assets, predominately invested in global lower volatility equities.

In 2023 the Fund achieved an overall investment return of +4.5%, giving a three year and five-year annualised return of +5.5% and +6.0% respectively. This was achieved in the context of double-digit listed equity returns for the year (broad market +15.3%) but negative returns from index-linked Gilts (the over 15 year index return was -4.3%). The Fund return in 2023 is in line with expectations given our asset allocation and strategy.

LPFI continued to provide advisory services to the LGPS's of Fife, Falkirk, Borders, and Northern Ireland, as well as managing an increasing amount of assets for Falkirk and Fife. In total, we're advising and managing around £3bn for these partner funds to both their benefit and to LPF through a shared cost model.

Our focus and commitment to being a responsible investor continued. In March, we retained the Financial Reporting Council's Stewardship Code accreditation following the publication of our Stewardship Report. This report sets out how we're delivering against the 12 principles set out by the Financial Reporting Council and includes case studies of our activities. We published Issue 6 of our ESG ezine, *ENGAGE* which gives detailed information on LPF's approach to ESG and our responsible investment activities. We also updated our Statement of Responsible Investment Principles and continued to support the Asset Owner Diversity Charter.

During the year we recruited 19 new colleagues across a variety of roles. This included Emmanuel Bocquet joining as Chief Investment Officer and Alan Sievewright as Chief Finance Officer, succeeding Bruce Miller and John Burns respectively. These hires will not only ensure that we remain adequately resourced to deliver what we need today, but will enable us to continue to improve our capabilities and the services we deliver to our members and employers.

In addition, 2023 saw several changes to the composition of the Boards of LPFE and LPFI, following the retirement of Hugh Dunn in September 2023. We were pleased to welcome two new non-executive directors, Dr Deborah Smart and Nareen Turnbull, to the Board of LPFE in early November, with Deborah being appointed as the Chair. In addition, Leslie Robb, was appointed as the Chair of the LPFI Board as an existing non-executive director.

As we seek to be a responsible investor and good steward of capital, we also seek to be a good employer and a great team. It was gratifying to see so many of our colleagues participate in charity events and fund raising during the year, and we continue to support Pride, World Mental Health week, Mental Health Awareness Day, International Women and Men's Day and Time to Talk. We also continue to work with Future Asset and GAIN to help encourage gender diversity in the asset management sector.

In 2024 we'll build on these achievements and look forward to the challenges and opportunities ahead.

Our planning process

Our planning process continues to build on the changes initiated in 2021, which led to a clear and comprehensive statement of strategy which was subsequently considered and approved by the Pensions Committee on behalf of our members and employers.

The proposed merger with Falkirk Council Pension Fund was paused in 2023. As a result, the strategy was reviewed before re-affirming the intention to pursue a broadly similar strategy and focus. The potential for extending collaboration with existing and new partners, where such collaboration benefits both LPF and partner funds remains an integral part of the strategy. The strategy was agreed by the Pensions Committee on 20 March 2024.

The planning process took the four broadly defined strategic goals and set out more detailed objectives and accompanying targets for each. These targets and measures allow us to monitor progress and identify where interventions may be required.

Those four strategic goals and more detailed objectives are set out in the following pages, along with individual functional plans, which detail how each function contributes to the overall strategy and goals of LPF. These are accompanied by financial metrics, headcount, and the other essential components of a comprehensive business plan.

STRATEGIC GOALS

Our four strategic goals are set by our Vision *"to deliver outstanding pension and investment services for the benefit of members and employers."* At LPF, we take pride in everything we do for our members, employers and stakeholders and strive for excellence. Our goals are as follows:

Develop and deliver a member and employer proposition for service excellence

We aspire to deliver service excellence to our members and employers. To achieve service excellence, we've benchmarked where we are, and agreed measures to achieve our goal.

We'll continue to target external validation including the Pensions Administration Standards Association (PASA) accreditation and the Customer Service Excellence (CSE) award. In addition, we'll use CEM Benchmarking to validate our goal of high quality/value for money positioning of participating UK pension funds.

We'll keep things simple by eliminating complexity and unnecessary friction in internal processes across the Fund and operating with clear information accessible across multiple channels.

Delivery of our digital strategy is key to this, as it will further improve our service proposition for both members and employers, making it easier to deal with us and reducing administration. It will also improve our operational resilience to protect our data and service continuity.

In addition to continuing the digital strategy, key priorities will include:

- Project delivery: complete McCloud and be ready for the launch of the Pensions Dashboard
- Recruit experienced administrators, improve capability and upskill teams
- Work with employers to improve performance and collaboration
- Continue service improvements: eliminating complexity and unnecessary friction in internal processes, explore automation, and operate with clear information accessible across multiple channels
- Maintaining PASA and CSE accreditation; utilise insights from CEM benchmarking.

Earn an appropriate risk adjusted investment return as responsible investors

We must exercise our fiduciary duty to provide benefits for members and their sponsoring employers with due awareness of the complex dynamics of investing in a changing world.

We'll do this by delivering sufficient investment returns over the long term to meet funding targets and seeking to have a positive impact on the economy and society by continuing to integrate Environmental, Social and Governance (ESG) considerations into our investment processes and demonstrating good stewardship of our assets.

Key priorities for 2024 include:

- Implement the revised strategic asset allocation and complete review and any rebalancing within policy groups
- Review team structure and resourcing
- Enhance our approach to Responsible Investment
- Maintain FRC Stewardship Accreditation.

Extend collaboration and services to existing partners and deepen where possible

Collaboration is key to our success.

We'll continue to collaborate through successful investment partnerships. In the short term, this is extending the investment management services to Falkirk and Fife pension funds, whilst continuing to provide advisory services to those funds and to the Scottish Borders LGPS and the Northern Ireland Government Officers' Superannuation Committee ("NILGOSC").

We seek to offer reliable and impartial advice to policy makers including the Scheme Advisory Board. We're currently supporting consideration and evolution of climate change reporting for Scottish LGPS funds.

Key priorities for 2024 include:

- Continue to support partner funds via LPFI and further alignment of portfolios
- Continue to work with Scottish LPGS in the SPLG / IGG forums
- Retain an advisory role with the SAB.

Foster great team and a great work environment

The key to our vision of delivering outstanding pension and investment services for the benefit of members and employers is our people. We're committed to growing a high-performing and inclusive workforce and creating an inspiring employer brand and culture.

We'll achieve this by: empowering a broad range of talents to meet our organisation priorities; cultivating leadership competencies and developing succession plans across the team; and by giving our people capacity and encouragement to contribute to our communities.

Having the right people with the right training and in the right roles is key to our success to achieve our vision. Our people processes from recruitment, people management, and training, all need to support the talent we have and the talent that joins us.

Key priorities for 2024 include:

- Re-locate to our new office which is better suited to the needs of our colleagues
- Recruitment and retention, training and development, talent management and succession planning
- Supporting organisational design to support evolving needs
- Continuing to support a fully inclusive culture and providing our colleagues with the tools, education and capacity to do so
- Supporting our communities, making sure each of our colleagues have two days annually to spend giving back to their communities in the manner they chose.

STRATEGIC PRIORITIES

Responsible Investment

At LPF, we're proud of our efforts to promote responsible investment and are recognised globally for our active participation in collaborative initiatives. Fundamentally, we seek to engage and influence rather than divest and exclude. Our Statement of Responsible Investment Principles describes our approach in more detail and how these principles complement and widen our ESG considerations.

Our investment strategy currently seeks alignment with the Paris goals and uses the Transition Pathways Initiative to guide us in this regard. We continue to explore a net zero commitment and would expect to introduce such a commitment and target date once we're confident about what it means for the fund and that we're capable of achieving it.

We continue to work with the Scottish Local Government Pension Scheme Advisory Board, who are considering enhanced climate change reporting and advising Scottish Ministers following the Department for Levelling Up, Housing and Communities public consultation on the same subject for the Local Government Pensions Schemes (LGPS) in England and Wales.

Office Accommodation

To accommodate our growing workforce and facilitate more face-to-face colleague collaboration, we're in the process of relocating our office to a larger premises in Haymarket Square. The move is expected to take place in May 2024.

McCloud and The Pensions Dashboard

The McCloud judgement introduced an additional benefit check to ensure that there's no age discrimination following the introduction of the career average benefit calculation. The McCloud Remedy came into force on 1 October 2023. This requires the collection of additional data on members past service, the introduction of additional benefit calculations, and remediation of any underpayments. This involves significant additional complexity and work.

The Pensions Dashboard Regulations 2022 were laid and approved by the UK government and came into force on 12 December 2022. Between 2023 and 2026, pension schemes will be compelled to join the ecosystem by their staging deadline, and all schemes in scope will need to connect by 31 October 2026. Pensions Dashboards will give increased transparency of expected pension benefits. The primary impact for LPF beyond supporting its introduction, is the likely increase in member queries from the increased visibility.

Good governance and embedding best practices

Upholding and maintaining sound corporate governance supports the long-term success of LPF, leading to better outcomes for our members, employers and partners. That's why we're committed to high standards of corporate governance, compliance and risk management. Our members, regulators, and City of Edinburgh Council (as Administering Authority and Shareholder of LPFI and LPFE) expect it of us, and so do we.

While a range of policies, procedures and frameworks are in place, we recognise there's room for improvement. We'll continue to make enhancements in the year to come.

During 2024/25 we would expect to:

- Continue to enhance and improve existing risk management arrangements by creating a fully integrated framework based on the following principles:
    - Focus on managing risk across the business in a proportionate and pragmatic way
    - Ensure arrangements are scalable with an emphasis on investing for the future and building resiliency
    - Reduce complexity by standardising processes wherever possible and appropriate
    - Continue to operate an integrated internal audit programme which includes the LPFE and LPFI entities
- Improve and evolve our governance operating model and framework, including our governance processes and practices, to continue to enhance and embed strong corporate governance.

OUR GROUP COMPANIES

LPFI

LPFI has developed its role and services since inception in 2016. It initially provided investment advice to our partner funds in Fife and Falkirk and now manages equity and bond mandates for them. The firm was set up for the benefit of the stakeholders of LPF, an asset owner. It aimed to do that by sharing costs with other LGPS funds in the spirit of public sector collaboration to benefit both parties to the arrangement. Consequently, LPFI doesn't treat clients in the same way as most investment management organisations by charging fees. Instead, it has sought to share costs rather than grow profits and it has only offered investment services that LPF undertakes for itself to ensure alignment of interests. There's an expectation, subject to appropriate advice and governance, that the range and value of funds under management for our Fife and Falkirk partners will continue to grow during 2024/5.

LPFI is regulated by the Financial Conduct Authority (FCA). During 2023, it was recategorised by the FCA as a non-small non-interconnected ("non-SNI") firm as a result of the increase in assets under management. The change in classification leads to an increased level of expectation from the FCA regarding the activities of the firm and how they're managed and governed. Recognising this and, more fully, the recent evolution in the services provided by LPFI, work took place to review and test many of the processes and controls to ensure they remain appropriate and continue to evolve to meet the requirements and expectations of the FCA. This work included the Investment Services Review (ISR) and Investment Governance Improvement Plan (IGIP) to ensure processes were in line with both the evolution in regulations and LPFI's business, and to ensure a robust operating model. We'll continue to build on this during 2024 through reviewing the investment headcount and structure as well as how other business areas support the investment team.

In-house investment management and collaboration with partner funds are two of the critical factors in the success of LPF. Some strategic options to be considered in the future to build on these include:

- The potential extension of investment advice and investment management to new LGPS Funds
- The use of collective investment vehicles to improve the efficiency of management for existing clients or support extension of services to new clients
- Bringing the investment activities of LPF within LPFI with inherent simplification of working arrangements and improved control through the regulated entity.

In each case, further investigation of the benefits, requirements and implications would be required. The Board is supportive to the logic of LPFI undertaking the investment activities on behalf of LPF, but further analysis would be required to fully understand the requirements and implications of this. It's recognised that the overriding strategic purpose of LPFI is to support LPF in achieving its purpose for members and employers of the Fund. The business case would be required to show this, and all appropriate approvals given prior to any such change.

The intention during 2024/25 is:

- To prepare a business case, including high level requirements and gap analysis for consideration by both the Pensions Committee and LPFI Board for the transition of investment management activities to LPFI under contract to LPF
- To consider an outline business case on the potential options and requirements of LPFI extending services beyond our existing partner funds
- To continue to monitor the development of Responsible Investment propositions and engage with our partner funds on their relevance, appropriateness, and interest.

LPFE

LPFE's primary purpose remains to recruit, develop and retain our colleagues who support the activities of LPF and LPFI. Growth in headcount in recent years to support the increasing requirements and services has been accompanied by increasing professionalism and capability, enabling LPF to remain at the forefront of the LGPS sector.

Like LPFI, LPFE has reviewed and improved key systems and processes to ensure they remain fit for purpose for the current and expected future needs of LPF and will continue to do so. The review of 2023 and the functional plan for 2024 highlight achievements and plans respectively.

For example, the LPFE Board supported the relocation to larger premises in 2024, recognising the impact of limited space on daily operation and colleague engagement. The move will complete in May this year.

2023/24 saw the introduction of stretch targets for the Senior Leadership Team. These have been carefully reviewed and enhanced to encourage over-achievement in key areas, with the focus on colleague engagement, risk management and strategic progress.

Finally, 2023 also saw the appointment of Dr Deborah Smart as Chair of the board following the retirement of Hugh Dunn in September 2023 and the subsequent appointment of Ms Nareen Turnbull to the Board.

FINANCIAL PROJECTIONS

Operating Budget

The table below shows the Group budget for the period 2024/25 with the prior year comparison and movement, as well as the indicative 2025/26 and 2026/27 budget and movement.

Total Group Operating Budget 2024/25 and Indicative 2025-27

	Budget 2023/24 £000	Movement £000	Budget 2024/25 £000	Indicative 2025/26 £000	Indicative 2026/27 £000
Employees	7,997	1,589	9,586	10,275	10,789
Plant and transport	306	475	781	820	861
Supplies and services	2,742	158	2,900	3,045	3,197
Third party payments	1,519	100	1,619	1,700	1,785
Investment managers fees – invoiced	3,850	(1,150)	2,700	2,835	2,977
Support costs	732	36	768	806	847
Capital funding	197	51	248	248	260
Gross expenditure	**17,343**	**1,259**	**18,602**	**19,730**	**20,716**
Income – collaboration	(1,966)	(736)	(2,702)	(2,909)	(3,054)
Income – other	(110)	-	(110)	(110)	(110)
Total income	**(2,076)**	**(736)**	**(2,812)**	**(3,019)**	**(3,164)**
Net expenditure	**15,267**	**523**	**15,790**	**16,711**	**17,552**
Percentage movement			**3.43%**	**5.83%**	**5.03%**
Strategic project costs	**1,193**	**(1,068)**	**125**	**-**	**-**
Total net planned expenditure	**16,460**	**(545)**	**15,915**	**16,711**	**17,552**

The largest component of the increased costs relates to employees. The budget is based on the headcount and Full Time Equivalent (FTE) information included in the Organisational Design section on page 23. Headcount is increasing to reflect the increased demands placed on the teams from managing more of the fund's assets internally, as well increased expectations of regulators, members, employers, and partner funds. Employees' costs have also increased to reflect salary changes from 1 April 2024, as well as the full year impact of recruitment activity in 2023.

Plant and Transport costs have increased to reflect the cost of the new office, the lease commencing in December 2023, with the move date in May 2024. The in-housing of c£350m of AUM from an external manager led to the reduction in Investment Managers fees.

Cash-flow forecast

Cash-flows from dealing with members is very dependent on the profile of fund 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 increasing payments of benefits to pensioners.

Employer contribution rates for the three years from 1 April 2024 were approved at the Pensions Committee in March 2024. Rates have been reduced to reflect the surplus of the fund and assumptions about future experience including investment returns. These will be reviewed again as part of the next valuation in 2026.

The figures in the below table consider the actual annual cash-flow of 2023/24 and the projected cashflows for the next three years.

	2023/24 £000	2024/25 £000	2025/26 £000	2026/27 £000
Contributions Received	290,000	252,000	264,600	277,830
Benefits Paid	(308,000)	(329,000)	(352,030)	(376,672)
Net Additions/(Deductions) From Dealings with Members	**(18,000)**	**(77,000)**	**(87,430)**	**(98,842)**

Fund cash flow management will be subject to greater scrutiny by Finance and Investment teams going forward as LPF expects to have a negative cash flow from dealing with members. Forecasted investment returns will more than offset this with no asset sales being required to fund on going pensioner payments.

FUNCTIONAL PLANS

Each team within LPF has prepared detailed functional plans setting out their key deliverables, priorities, and risks. The following section provides a summary of these.

Investments

The Investment team supports the Pensions Committee setting and implementing the investment strategy. It manages a significant majority of assets internally and oversees external managers who also invest on our behalf.

In addition, operating through LPFI, the team manages over £1.7bn of assets for the Falkirk and Fife LGPS funds, provides both funds with strategic advisory services and collaborates with two other LGPS funds (NILGOSC and Scottish Borders) by arranging private market investments, which it does for all five funds. The funds continue to explore areas in which they can improve efficiencies and returns through synergies and expect to expand their collaborative activity.

LPF has been a long-term advocate of Responsible Investment (RI) and promotes integration of environmental, social and governance (ESG) considerations into investment decision-making. This is an integral part of the investment process and the investment team, directly and indirectly through collaborative initiatives, engages with corporates and policymakers on a range of issues to influence strategy, reduce risk and enhance sustainability. It also leads on RI and climate change reporting activities and obligations.

Strategic priorities for 2024/25 include:

- Implementing the Pension Committee's investment strategy
- Supporting portfolio alignment activities with our partner funds
- Continuing to integrate climate-related considerations into investment decision-making, including carbon risks and decarbonisation opportunities, as well as expanding climate-related reporting to meet new regulatory requirements
- Reviewing and enhancing investment operational activities, including internal and external service provider management
- Reviewing team structure and undertaking recruitment to ensure resilience.

Operations

The Operational Services teams deliver the core services to our members and employers.

These services include supporting new joiners to the fund, payment of pensions and benefits, issuing annual benefit statements and supporting all other administration services and queries. In addition, the team manage the relationship with the scheme's actuarial advisors and work closely with them on the scheme valuation, cessation and transfer valuations, and the application of our funding strategy.

The Data & Quality team looks after data accuracy, quality of information and service. The Customer Experience Team is responsible for simplifying and streamlining our processes, identifying digital opportunities, responding to customer feedback, and making improvements to our operational processes and enhancing our customer experience.

The service standards they work to are set out in Appendix 2 and remain the same as 2023/24. Maintaining PASA accreditation and the CSE award, meeting the required regulatory standards and a high level of customer satisfaction are the expectations from these teams.

The high-level focus for the Operations team in 2024/25 includes:

- Continuing the Digital Transformation project. Further detail of which is included in the Project and Change section of this plan
- Customer journey mapping
- Implementation of the requirements of the McCloud judgement and the Pensions Dashboard
- Conclusion of the 2023 Triennial Actuarial Valuation as at 31 March
- Funding Strategy review
- Gaining PASA reaccreditation
- Working in partnership to improve employer performance.

IT & Change

2024 will see the IT & Change team continue to manage and build on the LPF IT service delivered by third-party vendor Cased Dimensions, leveraging the existing service, and deploying or developing new solutions and technologies to enhance the value gain.

The team will deliver significant support to the development of digital opportunities for member services, office re-location and other new services and procurement. IT & Change will also provide governance through ITOCG and the PMO, its process and methodologies. They'll also continue to support projects / new services and procurements with a focus on the new finance system.

The key priorities for 2024/25 are:

- Embed our newly developed Information Security Management System (ISMS)
- Support the procurement of a new Risk and Compliance system
- Support the office move ensuring a seamless transition of our IT requirements
- Ensure our controls are robust in terms of protecting our data and preventing loss or breaches
- Redesign of our Sharepoint sites
- Cyber Essentials + Support data analytics, management, and classification
- Review our IT architecture, prepare and document our future IT Strategy.

Governance, Legal, Risk & Compliance

We care about and respect our members and employers and are committed to being a responsible business. We have comprehensive policies and procedures in place, and, collectively, these functions ensure that LPF and its group companies meet all corporate governance, legal, and regulatory obligations and expectations that impact our work. They support the delivery of our long-term objectives and success, by helping to ensure that we're trusted, respected and appropriately managed.

Key priorities 20243/254 include:

- Continue to develop and embed enhanced risk management arrangements, supported by improved risk management processes and methodology
- Select a risk system that will effectively help facilitate the risk management framework across business areas
- Design, develop and implement a dedicated investment compliance oversight programme and uplift of complimentary policy standards
- Improve and evolve our governance operating model and framework, including our governance processes and practices, to continue to enhance, embed and maintain strong corporate governance and aspire to the highest standards
- Continue to monitor the horizon to identify the implications of an evolving regulatory landscape on our business, identifying gaps, risks and opportunities to our existing practices. The new General Code of Practice by the Pensions Regulator is an example and a key focus for the year ahead
- Continue to work with Finance, to further improve the Internal Capital and Risk Assessment process and resulting ICARA report for LPFI
- Continue to progress development, implementation and identification of further improvements regarding LPF's approach to managing and protecting data

Finance

The Finance function is responsible for all aspects of planning, budgeting, and reporting of LPF's finances. This includes preparation of the Annual Report and managing the external audit process. Tax, maintaining the unitised valuations for the Fund, procurement and working with the custodian Northern Trust complete the main areas of responsibility.

2023/24 saw an investment in core systems and 2024/25 will offer the opportunity to realise the benefits identified in the scoping phase of each implementation.

In 2024/25, key priorities for the Finance team include:

- Co-ordinate the Strategy and Business Plan reporting
- Complete the implementation of the new Finance system and accounting ledger
- Integrate the supplier management database with the payment/invoicing process for the new Finance system

- Review of Finance processes for efficiency gains or process automation via existing or new software, and consider impact on ways of working
- Roll out of an enhanced financial forecasting process including budget monitoring process with increased oversight for budget holders and associated KPIs/KRIs
- Support the review of the operating structure in the Investment Team
- Retender of Custody services currently provided by Northern Trust
- Investment Management cost transparency and value analysis using CTI and CEM benchmarking data
- Ongoing management of LPF group cashflow and regular review of fund cashflows from dealing with members which is expected to be in an outflow position going forward
- Monitoring the capital and liquidity position of LPFI, and working in collaboration with the Investments, and Risk and Compliance teams on the ICARA process and reporting, and all FCA reporting requirements.

People & Communications

Core deliverables of the Communications team include production and distribution of key documents including the Annual Report, the Statement of Responsible Investment Principles, *ENGAGE* ezine and the Stewardship Report. In addition, the team manages internal communications, events, external media and the look and feel of member and employer communications.

The HR team is responsible for supporting the business in resourcing and colleague management including reward, organisational design, career pathways, learning and development and the full suite of HR policies. They're responsible for assessing and monitoring colleague engagement and run twice annual colleague surveys to gain feedback from colleagues and find out what is going well/ where we can make improvements, as well as facilitating the colleague recognition awards. Office management, business continuity and health and safety also fall under their remit.

In addition to these core deliverables, in 2024/25 the teams will be heavily involved in the New Office project, which will include

- Clear and comprehensive communication to all colleagues, and other stakeholders on timelines and address changes
- The production and upskilling of all colleagues on new ways of working and systems in the new office
- The transfer of old office furniture to the new premises to support sustainability
- The Health and Safety requirements of the new office in conjunction with the CEC H&S team

Additional areas of focus for these teams will be:

- The Organisational design requirements across all functions
- Recruitment of all vacant and new roles
- Updating and reviewing our HR policies
- Business continuity upskilling and management across the teams
- Remuneration and Benefits review.

CEC Shared Services

City of Edinburgh Council (CEC) have three relationships with LPF. Firstly, as Administering Authority and Scheme Manager CEC are responsible in legislation for the management of the LGPS in Edinburgh and the Lothians. It delegates the running of the Fund to the Pensions Committee and two arm's length operating companies (LPFE and LPFI) in this regard. Secondly, CEC is one of 65 contributing employers connected to the Fund, being the employer with the largest number of active, deferred and pensioner members.

Lastly, CEC provide services to the Fund, including:

- Internal Audit services
- Company secretarial services to support the Pensions Committee.

In addition, CEC have oversight responsibility. This, with associated advisory input, is provided by:

- The Information Governance Unit and Data Protection Officer
- Information Security.

In 2024/25 the expectations for these shared services are as follows:

- Internal Audit will continue to provide internal audit services, which includes the delivery of some audits by CEC's co-source audit partner
- Following the transition to the new LPF finance system and ledger, CEC's Finance and Procurement team will continue to provide certain services including support on procurement and treasury facilities.

PROJECTS & CHANGE

Our Programme Management Office and Change Approvals Committee ensure that all projects and change activities are managed appropriately and monitored regularly using best practice methodology. This ensures that there's differentiation between projects, small change, and non-project change activities, and recognises that different degrees of governance and practices are appropriate for each.

The table below sets out the current list of formal projects.

Project Name	Objective	Project Sponsor	Delivery Timescale
Finance Systems	Having reviewed the current finance system and documented procedures, procure a fit for purpose, tailored and flexible solution to best meet pension funds' needs, with revised procedures as required.	CFO (Alan Sievewright)	Q2 2025
Digital Transformation	To ensure the digital service offering for both members and employers is class leading for the pensions industry.	COO (Karlynn Sokoluk)	20234/25
McCloud	Ensure rectification of historic LGPS age discrimination in accordance with (future) regulations and timetable, together with requisite member communications.	COO (Karlynn Sokoluk)	2024
Climate Disclosure and Strategy Project	To satisfy annual reporting requirements and SRIP revisions, which involves reviewing existing and prospective regulations, data requirements, data suppliers, budget implications, including time resource, and deciding on what commitments can and should be made.	CIO (Emmanuel Bocquet)	2023/24
Pensions Dashboard	Support the introduction of the UK Government's Pension Dashboard, working with our pensions administration software supplier to facilitate data submission and address member servicing requirements in readiness for go live.	COO (Karlynn Sokoluk)	2024/5
Multi-fund Employers	Develop business cases and processes to support employers who are considering or might benefit from consolidation from participating in multiple LGPS funds.	COO (Karlynn Sokoluk) and CFO (Alan Sievewright)	2024/25

ORGANISATIONAL DESIGN

As noted in the review of 2023, we recruited new Chief Investment and Chief Financial Officers. Both are taking the opportunity to review both functions to create more focussed teams.

The table below shows the expected evolution of full-time equivalent roles (FTE) to 31 March 2025. It assumes the current functional structure is maintained over this period.

Function, Team/Full Time Equivalent (FTE)	Mar-24	Mar-25
CEO	1	1
Governance	3.6	3
Legal	2	3
COO	1	1
IT and Change	4	4
Operations	43.7	48.7
CFO	1	1
Finance	9.5	11.5
CIO	1	1
Investments	19.1	25.1
CRO	1	1
Risk & Compliance	3	4
CPO	1	1
People and Communications	6	7
Total	**96.9**	**112.3**

FTE is expected to increase during 2024 across all teams through a combination of new roles, parental leave cover and filling existing vacancies. The increases within Risk and Compliance and Finance are to enhance Data, Business Continuity and Supplier Management frameworks, Investments, and Operations to return the team to the optimal level of resource to meet the requirements of members and employers.

RISKS

During 2023 a comprehensive review of the LPF group risk register was undertaken, which has resulted in an improved articulation and evaluation of current risks which the group is exposed to and how these are being managed. The register is reviewed and updated as required on an ongoing basis, and reports on this to the Pensions Committee and its Audit Sub-Committee and to each of the LPFE and LPFI Boards.

The risk register and reports issued to the Boards and Committee have been reviewed to reflect this business plan and the risks inherent in it.

No additional risks have been added to the risk register based on the plans set out, however some of those risks noted may potentially increase if they're not effectively managed, as set out below.

Business Plan Risks

People risk is acknowledged as one of LPF's key risks, and we face challenges around recruitment, retention and resourcing as the business experiences difficulties filling positions, managing training and knowledge gaps, and managing and prioritising workload. Whilst this is true across most parts of the organisation, it's particularly challenging in our Pensions Administration area where several open vacancies and a limited number of experienced colleagues contribute to increased strain on resources.

However, LPF is no different from other LGPS, who are also struggling to identify resources with the required knowledge and experience in defined benefit schemes. Where LPF is at a potential advantage from other LGPS in attracting and retaining desired resource, is through the unique employment proposition provided through LPFE, although competition for resources from the private sector will always be a challenge. Management are actively considering a number of tactical and longer term strategies to manage resource strain and the LPFE Board continue to monitor this risk.

Following the retirement of the previous CIO, the change in leadership in the Investment team will bring some structure and resourcing changes in that area. Furthermore, the completion of the Investment Governance Improvement Plan project identified options regarding how LPF's middle office activities could be organised and arrangements improved which will be taken forward at the same time. The impact of these changes across several teams is likely to elevate people risk for a period, however the changes will allow LPF to introduce efficiencies and improve effectiveness, as well as making us more operationally resilient.

Although staff engagement continues to be very positive, culture and engagement remain firmly on the radar as we work through the organisational changes noted above and manage the relocation to LPF's new premises in Q2 24. The office move is seen as a significant improvement to current arrangements, delivering a notable uplift to our colleagues' working environment. Whilst the hybrid working model which promotes part time homeworking is considered beneficial and effective, there have been challenges in bringing people together at the same time. While ongoing communication with team calls, all colleague briefings and away days have helped to bring colleagues together remotely and in person and created opportunities to meet peers and network more widely, the uplift to office arrangements will help facilitate more opportunities for face-to-face interactions and cross-team engagements on a more routine and spontaneous basis.

Regulatory risk will always feature at least moderately for an organisation such as LPF, especially with its range of regulatory bodies. The regulatory landscape is under constant review, as it adapts to geopolitical, economic, social and technological influences. It's key that LPF continues to stay abreast of planned and actual regulatory changes and developments and there are several stakeholders across the organisation that work collaboratively in identifying, analysing and planning for changes, and subsequently implementing required operational or governance changes within the business. This is reflected in the work we've undertaken to deliver on McCloud and the Pensions Dashboard, as well as the review and preparation for changes being introduced by The Pensions Regulator's new General Code of Practice which goes live during the first half of 2024. Keeping up with Financial Conduct Authority themes also continues to be a focus, particularly as LPFI's assets under management grow in line with increased collaboration with our partner funds.

Project Risks

Each of the projects set out in this plan and any that are added to the change programme will have project specific risk registers and a statement of project risk appetite. Improved project risk reporting will continue to evolve through the creation of the Project Office.

APPENDIX 1: KEY PERFORMANCE METRICS

DEVELOP AND DELIVER A MEMBER AND EMPLOYER PROPOSITION FOR SERVICE EXCELLENCE
Customer Satisfaction, as measured by employers and members through survey results > 90%
>92% of pensions administration work completed within standards
Data Quality, as defined by the Pensions Regulator achieve “common” and “conditional” data scores in excess of 95% and 95% respectively. The data is assessed as at 31 August 2024 (members’ Annual Benefit Statements)
The Fund operates within the approved budget
The audit of the Annual Report is unqualified with no significant or substantial risks identified in audit observations
EARN AN APPROPRIATE RISK ADJUSTED INVESTMENT RETURN AS RESPONSIBLE INVESTORS
Rolling 10-year fund return is >+5% pa unless the benchmark is <+5%pa, in which case, the relative return is positive
Publish *ENGAGE* and the Revised SIP and SRIP
RISK, GOVERNANCE, LEGAL AND COMPLIANCE FRAMEWORKS
Mandatory LMS training completion rate >95%
ACHIEVE GREATNESS IN OUR PEOPLE, TEAMS, AND CULTURE
The Employee Engagement index KPI of 70% or above
Less than 10% unplanned employee turnover

APPENDIX 2: SERVICE PERFORMANCE INDICATORS

Measure	Target
Monthly pensioner payroll paid on time	100%
Acknowledge the death of a member to next of kin within 5 working days	96%
Employer contribution paid within 19 days of month end	99%
Estimate requested by employer of retirement benefits within 10 working days	91%
Notification of dependant benefits within 5 working days of receiving all necessary paperwork	96%
Notify early leavers entitled to deferred benefits of their rights and options within 10 days of being informed of end of pensionable service	91%
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	85%
Pay a refund of contributions within 7 working days of receiving the completed declaration and bank detail form	91%
Pay any lump sum death grant within 7 working days of receipt of the appropriate documentation	96%
Pay lump sum retirement grant within 7 working days of receiving all the information we need from the member	96%
Payment of CETV within 20 working days of receiving all completed transfer out forms	96%
Proportion of pensions administration work completed within standards – individual performance within this indicator is shown below	92%
Proportion of members receiving a benefit statement by August	100%
Provide a maximum of one guaranteed Cash Equivalent Transfer Value (CETV) within 10 working days of receiving a request	91%
Provide new members with scheme information within 20 working days of getting details from employer	100%
Provide transfer-in quote within 10 working days of receiving the Cash Equivalent Transfer Value (CETV) from member's previous pension provider	96%
Respond in writing within 20 working days to formal complaints that have escalated from frontline resolution, or recorded directly as an investigation	96%
Level of Sickness Absence	<4%
A minimum of two days training for all staff for the year	100%

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Lothian Pension Fund – Proposed Internal Audit plan for 2024/25

Item number 6.9

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 review the proposed Lothian Pension Fund 2024/25 Internal Audit plan and recommend to the Pensions Committee for approval.

1.2 note the approach to developing a forward-looking approach to assurance by considering indicative audits over a three-year period, which will be reviewed and approved annually.

Laura Calder
Head of Internal Audit

Legal and Assurance, Corporate Services Directorate

E-mail: laura.calder@edinburgh.gov.uk | Tel: 0131 469 3077

Lothian Pension Fund – Proposed Internal Audit plan for 2024/25

2. Executive Summary

2.1 The purpose of this paper is to present the Lothian Pension Fund (LPF) proposed Internal Audit (IA) plan for the period 1 April 2024 to 31 March 2025 to the Committee for review and approval.

2.2 The audit universe covers the LPF group structure and will provide assurance for the LPFI and LPFE boards where appropriate.

2.3 The plan will also include ongoing IA follow up on implementation of management actions arising from previous internal audit reports.

2.4 In discussion with management, a forward-looking approach to assurance which provides an indicative internal audit plan over a three-year period has been considered.

3. Background

3.1 The LPF IA plan is driven by requirements of section 2010 of the Public Sector Internal Audit Standards (PSIAS) which requires IA to establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organisation's goals.

3.2 IA has reviewed LPF's organisational objectives and priorities, and completed an assessment of the risks that could prevent LPF from meeting those objectives and providing pension services to employers and members.

3.3 The PSIAS specifies that the risk-based plan must consider the requirement to produce an annual IA opinion. IA work performed must be appropriately scoped to cover LPF's most significant risks, with an appropriate depth of testing performed to provide sufficient assurance on the control environment, governance, and risk management frameworks to support provision of the annual opinion.

3.4 PSIAS also specifies that internal audit activity must evaluate the effectiveness of risk management processes and contribute to their improvement.

3.5 In 2023/24, the audit universe was expanded to include the LPF group structure and to provide a single integrated audit programme and provide assurance for the LPFE and LPFI Boards where appropriate.

3.6 It should be noted that Internal Audit is not the sole source of assurance provision for LPF, as several additional external second line assurance providers are engaged (in addition to the annual external audit review of LPF's financial statements) to provide additional assurance coverage.

Co-source internal audit provision

3.7 Following a request from LPF in 2019/20, all LPF internal audit services are currently provided by the City of Edinburgh Council's co-source professional services provider PwC with oversight from the Council's Head of Internal Audit.

3.8 In addition, the Boards of LPFI and LPFE may seek additional assurance where necessary to fulfil required obligations, where either the Council Internal Audit service or the co-source provider does not have capacity or expertise.

Internal Audit Charter

3.9 PSIAS also specify that the purpose, authority, and responsibility of IA must be formally defined in an Internal Audit Charter (the Charter) that is periodically reviewed and presented to senior management and the board for approval. The Council's IA charter, approved by the Council's Governance, Risk and Best Value Committee in March 2024 fulfils this requirement for LPF.

New Global Internal Audit Standards

3.10 In January 2024, the Institute of Internal Auditors launched new Global Internal Audit Standards (GIAS), which will come into effect in January 2025. The new standards will require several changes to Internal Audit practice including the introduction of 'topical requirements' for all internal audits.

3.11 Guidance on the full requirements of the new GIAS will be released by the Institute of Internal Auditors as it develops. It is proposed that relevant updates are provided as part of the quarterly update paper and supported by necessary training sessions for both LPF colleagues and committee members delivered by IA.

4. Main Report

Scope of Internal Audit Assurance

4.1 The scope of IA assurance provided to LPF in relation to regulatory compliance is specifically limited to confirming LPF's ongoing compliance with Local Government Pension Scheme (Scotland) requirements.

4.2 The audit universe was expanded across the LPF group in 2023/24 with the inclusion of the operation of the Fund's two wholly owned subsidiary companies LPFE and LPFI Ltd that are responsible for providing employee resources to administer the pension funds, and provision of Financial Conduct Authority regulated services to both LPF and other Local Government Pension Scheme Funds.

Preparation and content of the proposed plan

4.3 The areas proposed for inclusion in the plan were identified by considering the key risks included in the LPF risk register as at January 2024, and discussions with the LPF management team, Pensions Audit Sub Committee members and External Audit.

4.4 The LPF risk register as at January 2024 included a total of 26 risks, of which there were nil very high, 3 high, 15 moderate, 7 low and one insignificant rated risk.

4.5 The 3 high and 15 moderate risks were considered together with the outcome of previously completed audits, other assurance sources and key regulatory requirements.

Proposed 2024/25 Internal Audit Plan

4.6 The proposed IA plan for 2024/25 includes the following five audits:

- Pensions Committee Governance & Operational Effectiveness: Governance - discharge of responsibilities and accountabilities and best practice governance are high and moderate rated increasing LPF risks. This audit will be completed in Quarter 1 and will consider governance and operational effectiveness in line with the delegated functions set out in the Pensions Committee Terms of Reference and relevant regulations as well as consideration of fiduciary duties. It will also consider member skills, knowledge, and training.

- Member Payments: Process and Execution – operation errors is a moderate rated risk. This audit will be completed in Quarter 2 and will review key controls for ensuring member payments are accurate and on time, including payment administration of regular payments, pro-rata payments, one-off lump sum payments, change of bank details, and management of under/overpayments.

- Infrastructure Asset Selection, Management & Oversight: Investment Management – investment performance; investment services delivery and investment strategy are moderate rated risks. This audit will be completed in Quarter 3 and will consider how infrastructure assets are selected and managed including the investment strategy, costs, investment risk management, investment performance and consideration of climate change.

- Investment Governance Improvement Plan (IGIP) Implementation**:** This audit will be completed in Quarter 4 and will provide assurance on a range of moderate rated risks aligned to implementation of the improvement actions set out in the IGIP, developed to address the gaps and weaknesses identified in the themed review of Investment Services.

- Annual Validation Review: This review will be completed in Quarter 4 and will include a review of a sample of previously implemented and closed audit actions to confirm that they have been effectively sustained.

4.7 Reports detailing outcomes of each review will be presented to the Pensions Sub Committee. All reviews completed for LPFI/LPFE will also be presented to the relevant Board.

4.8 The proposed Internal audit reviews planned for the year 1 April 2024 to 31 March 2025 should provide assurance on 1 high and 9 moderate rated risks included in the

LPF risk register. Extending this to include follow-up of work performed in 2023/24 provides assurance for a total of 16 of the 18 high and moderate risks.

4.9 As part of preparation of the 2024/25 IA plan, a forward-looking assurance approach which provides indicative audit coverage across the LPF group risks on a three-year basis was considered through discussion with IA and LPF colleagues. Proposed indicative audit titles for 25/26 and 26/27 are included at Appendix 2. These areas will be reviewed as part of annual planning processes to ensure they remain appropriately aligned to LPF's top scoring risks.

4.10 It is important that the Committee confirms that appropriate assurance coverage will be provided across LPFs remaining population of moderate risks and (in particular) the risks associated with 'business as usual' operational activities by the additional assurance providers engaged by the Fund.

4.11 Table 2 of the 2024/25 IA plan provides an initial assurance mapping across the high and moderate LPF risks. It is proposed this will be developed further during 2024/25 with LPF colleagues to provide members details of where sources of assurance across the risks is provided. It is envisaged that the updated assurance map will be presented to the September 2024 meeting.

Delivery of the 2024/25 IA plan

4.12 The co-source provider contract is now due for re-tender, and an exercise to select a co-source provider for 2024 to 2026 (with an option to extend) will commence in March 2024. LPF colleagues have been invited to participate in the selection process.

4.13 During 2024/25 some audits may be conducted by the Council's in-house IA team, as agreed with LPF management.

Risk Management

4.14 PSIAS requires that an appropriate depth of testing is performed to provide sufficient assurance on the control environment, governance, and risk management frameworks to support provision of the annual IA opinion.

4.15 Whilst sufficient information is generally collated across multiple audits to provide an understanding of the effectiveness of risk management processes to support the annual opinion, IA typically also performs targeted risk management audits to assess and provide assurance on the adequacy and effectiveness of the risk management framework across the entire organisation. The most recent audit of risk management was completed in August 2022.

4.16 LPF undertook a comprehensive review of its Risk Management Framework during 2023 which resulted in a simplified methodology and a revised risk register. During 2024/25, where appropriate, IA will consider how well the new framework is being embedded and LPF's risk culture as a core element of the audits completed.

Follow-up activity

4.17 Follow-up work will also be performed in line with a risk-based approach to confirm whether agreed management actions implemented to support closure of findings raised in previous LPF audits have been effectively implemented.

New Global IA Standards

4.18 During 2025, IA will prepare for the introduction of the new Global IA standards including update of key documents, audit team training and colleague/committee member training and awareness.

5. Financial impact

5.1 The estimated costs associated with delivery of the LPF 2024/25 IA plan are estimated to be circa £86,000 which reflects:

- current direct recharging of costs based on agreed rates as specified in the Council's IA co-source contract
- direct recharging of costs for audits completed by the Council's IA team which will be charged on an actual costs' basis through completion of IA timesheets
- costs associated with plan delivery and administration including preparation of the annual plan, annual opinion, review and oversight of all IA reviews, preparation of Committee reports, attendance at Committee meetings, as well as ongoing review and validation of previously raised audit actions. This will be charged on an actual costs' basis through completion of IA timesheets.

6. Stakeholder/Regulatory Impact

6.1 The LPF management team, members of the Pensions Audit Sub Committee and External Audit were consulted when developing the 2024/25 IA plan.

7. Background reading/external references

7.1 Public Sector Internal Audit Standards

7.2 Internal Audit Charter

8. Appendices

Appendix 1 – Lothian Pension Fund 2024/25 Internal Audit Plan
Appendix 2 – Indicative proposed audit areas for 2025/26 and 2026/27

Internal Audit

2024/25 Annual Plan

Contents

Introduction and approach **3**
Risk Assessment **4**
2024/25 Internal Audit Plan **6**

Introduction and approach

Introduction

In line with the Internal Audit Charter, Internal Audit provides independent and objective assurance on the overall effectiveness of the Lothian Pension Fund's (LPF) governance, risk, and control frameworks.

This document sets out the scope of the Internal Audit 2024/25 annual plan with the objective of delivering independent assurance on the key controls established across the LPF group to mitigate high and moderate risks.

Approach

The approach to preparing the annual plan is set out at Figure 1. The plan is driven by LPF's objectives and priorities, and an assessment of the risks that could prevent LPF from meeting its objectives.

The audit universe includes the LPF group structure and provide assurance for the LPFI and LPFE Boards where appropriate.

LPF's Business Plan centres around the following four broadly defined strategic goals:

- ***develop and deliver a member and employer proposition for service excellence***
- ***earn an appropriate risk adjustment investment return as responsible officers***
- ***extend collaboration and services to existing partners and deepen where possible***
- ***achieve greatness in our people, teams, and culture.***

Other sources of assurance

Internal Audit is only one of several sources of assurance over the LPF groups risks. In developing our risk assessment and plan we have considered other sources of assurance and have considered the extent to which reliance can be placed upon these other sources (for example, external audit, BDO, Mercer and LPF's Risk and Compliance function).

IA does not intend to place formal reliance upon these other sources of assurance but would not seek to duplicate the work they do. Key stakeholders including senior management, committee members and external audit (Azets) have been invited to provide input into the IA annual plan to help ensure that the relevant areas are targeted for review.

***Figure 1**: Approach to developing the 2024/25 IA Annual Plan*

Step 1 *Understand LPF's corporate objectives*	Review the LPF business plan to understand strategic objectives and priorities.
Step 2 *Review LPF's risk profile*	Review the LPF's risk profile, risk appetite and consider any other external and internal risks that could impact LPF.
Step 3 *Consider the audit universe*	Identify all auditable areas across LPF.
Step 4 *Consider other sources of assurance provided*	Consider other sources of assurance across the audit universe and the extent to which reliance may be provided on such work.
Step 5 *Consult with key stakeholders*	Consult with key stakeholders to ensure areas which may be of risk to operations are considered for inclusion within the IA work programme.
Step 6 Determine the audit plan	Based on the outcomes of steps 3, 4 and 5, determine the timing and scope of audit work required.
Step 7 *Other considerations*	Consider any requirements in addition to those identified from the risk assessment process.

Risk Assessment

To ensure a risk-based approach to the LPF Group IA annual plan which is proportionate and aligned to business-critical risks and emerging issues, consideration was given to the LPF group's priorities as detailed in the 2023-24 Business Plan.

LPF undertook a comprehensive review of its Risk Management Framework during 2023 which resulted in a simplified methodology and revised risk registers. The IA risk assessment considered the LPF group risk profile as at January 2024 (Table 1). All high and moderate risks (a total of 15 risks) were reviewed, together with the outcome of previously completed audits, other assurance sources and key regulatory requirements (Table 2).

Table 1: LPF Risk Summary as at January 2024

Total risks	Very High	High	Moderate	Low	Insignificant
26	0	3	15	7	1

Table 2: High and Moderate risks assessment and assurance map

Risk Ref	Level 1 Risk	Level 2 Risk	Risk Name	Entity	Rating	Previous IA Assurance			Proposed 24/25 coverage	Other sources of assurance
						21/22	22/23	23/24		
7	Governance, Legal & Compliance	Governance	Discharge of Accountabilities & Responsibilities	LPF	H	Risk Management	Project Forth Programme Health Check	Follow-up	**Pensions Committee Governance & Operational Effectiveness**	
16	People & Culture	People & Culture	Recruitment & Retention	All	H	-	-	People Processes	Follow-up of 2023/24 People Processes Audit	Azets People review 2022
17	People & Culture	People & Culture	Resources	All	H	-	-	People Processes Business Continuity	Follow-up of 2023/24 People Processes Audit and 2023/24 Business Continuity Audit	Azets People review 2022
25	Governance, Legal & Compliance	Governance	Best Practice Governance	All	M	Risk Management	Project Forth Programme Health Check	Follow-up	**Pensions Committee - Governance & Operational Effectiveness**	BDO Compliance Assurance Monitoring Programme (LPFI)
2	Information Security IT & Data	Data	Data Management	All	M	Bulk Transfers	Information Governance	Information Security	Follow-up of 2022/23 Information Governance Audit and 2023/24 Information Security Audit	
13	Business Operations	Third Party	Supplier Performance and Oversight	All	M	Capital Calls Employer Contributions	Third-Party Supplier Management Information Governance	Follow-up	Follow-up of 2022/23 Third-Party Supplier Management Audit	
19	Investment Management	Investment Management	Investment Strategy	LPFI LPF	M	-	-	-	**IGIP Implementation Infrastructure Asset Selection, Management & Oversight**	Themed Services Investment Reviews

Risk Ref	Level 1 Risk	Level 2 Risk	Risk Name	Entity	Rating	Previous IA Assurance			Proposed 24/25 coverage	Other sources of assurance
						21/22	22/23	23/24		
11	Information Security IT & Data	Information Security & Cyber	Cyber Security	All	M	-	-	Information Security	Follow up of 2023/24Information Security Audit	Independent cyber security maturity assessment completed Dec 2021
4	Governance, Legal & Compliance	Regulatory Compliance	Regulatory Breach	All	M	-	-	Senior Manager Certification Regime	**IGIP Implementation** Follow-up of 2023/24 Senior Manager Certification Regime Audit	Themed Services Investment Reviews
21	Strategy	Strategy	Strategic Goals	All	M	-	Risk Management	-	No internal audit work in 2024/25 proposed. Audit of Responsible Investment / ESG proposed for 2025/26 and further review of Risk Management to be considered in 2026/27	
18	Strategy	Climate	Climate Change and Responsible Investing	All	M	-	-	-	Responsible Investment/ ESG review proposed for 25/26	
9	Business Operations	Business Continuity	Business Interruption	All	M	-	-	Business Continuity	Follow-up of 2023/24 Business Continuity Audit	
1	Investment Management	Investment Management	Investment Performance	All	M	Capital Calls	-	-	**Infrastructure Asset Selection, Management & Oversight**	Mercer Systems and Controls Review (LPFI)
6	Business Operations	Processing and Execution	Investment Operations Errors	All	M	Capital Calls	-	-	**IGIP Implementation**	
27	Business Operations	Processing and Execution	Operational Errors	LPF	M	Bulk Transfers	-	-	**Member Payments**	
8	Business Operations	Processing and Execution	Investment Services Delivery	LPF	M	Cessations	-	-	**Infrastructure Asset Selection, Management & Oversight**	
5	Scheme	Employer Contributions	Employer Failure	LPF	M	Employer Contributions	-	-	No internal audit work in 2024/25 proposed.	
10	Information Security IT & Data	Technology	IT systems	All	M	Technology Model Development		Information Security	Follow up of 2023/24 Information Security Audit	

2024/25 Internal Audit Plan

The following table sets out the LPF internal audit work programme for the period 1 April 2024 to 31 March 2025. Reports detailing outcomes of each review will be presented to the Pensions Sub-Committee. Reviews completed for LPFI/LPFE will also be presented to the relevant Board.

While the audit plan includes a short summary of the area proposed for review, IA will meet with key officers prior to commencing each audit to further understand the key risks and to develop and refine the scope of each review. It should be noted, that if areas are identified during testing that are outwith scope but impact the risk and control framework, findings and recommendations will still be raised and reported on, where appropriate.

Audit	Entity	Risks	Quarter
Pensions Committee Governance & Operational Effectiveness – review of the governance arrangements for the Pensions Committee to provide assurance on operational effectiveness in line with the delegated functions set out in the Terms of Reference and relevant regulations as well as consideration of fiduciary duties. Will also consider member skills, knowledge, and training.	LPF	7 and 25	Q1
Member Payments – review of design adequacy and operating effectiveness of key controls and processes established to ensure member payments are accurate and on time, including payment administration of regular payments, pro-rata payments, one-off lump sum payments, change of bank details, and management of under/overpayments.	LPF	27	Q2
Infrastructure Asset Selection, Management & Oversight – review of will consider how infrastructure assets are selected and managed including the investment strategy, costs, investment risk management investment performance and consideration of climate change.	LPFI	1, 8, 19	Q3
Investment Governance Improvement Plan (IGIP) Implementation – review of progress with implementation of the improvement actions set out in the IGIP, to address the gaps and weaknesses identified in the themed review of Investment Services	LPFI	4, 6, 8 13, 19	Q4
Annual Validation review - review of a sample of previously implemented and closed audit actions to confirm that they have been effectively sustained.	All	Dependent on sample	Q4
Other IA activities including annual planning and reporting, committee reporting and attendance, and officer/member support including training on the New Global IA Standards.			Ongoing

Appendix 2 – Indicative proposed audit areas for 2025/26 and 2026/27

During the 2024/25 annual audit planning process consideration was given to developing a forward-looking approach to assurance planning through identifying potential areas for future internal audit reviews over a three-year period.

Details of the indicative areas for 2025/26 and 2026/27 are provided below for information. These areas would be reviewed as part of the annual planning process to ensure alignment with LPF top scoring risks and emerging issues.

2025/26	2026/27
Invoicing	Settlement & Custody Arrangements
Payroll	Supplier Management
Death Process Management	Risk Management
Corporate Board Governance & Operational Effectiveness	
McLeod Implementation	
Responsible Investment / ESG	

This page is intentionally left blank

Pensions Committee

2.00pm, Wednesday, 20 March 2024

External Audit Annual Plan 2023/24 by Azets

Item number 6.10

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 note the planned programme of work to support the statutory audit 2023/24. This is shown at Appendix 1 - "Lothian Pension Fund External Audit Annual Plan 2023/24" by Azets;

1.2 note that progress against the Lothian Pension Fund External Audit Annual Plan 2023-24 will be reported to future meetings of the Pensions Audit Sub-Committee and the Committee.

Alan Sievewright

Chief Finance Officer, Lothian Pension Fund

Contact: Alan Sievewright, Chief Finance Officer, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

External Audit Annual Plan 2023/24 by Azets

2. Executive Summary

2.1 Azets, the external auditor to Lothian Pension Fund and Scottish Homes Pension Fund, has detailed its planned programme of work to support the statutory audit 2023/24. This is shown in full at Appendix 1.

2.2 Azets representative(s) will present the External Annual Audit Plan 2023/24 to Committee.

2.3 To meet independence requirements the audit signatory for the Funds has changed from Nick Bennett to Chris Brown.

3. Background

3.1 Azets has been appointed by Audit Scotland as the external auditor to Lothian Pension Fund and Scottish Homes Pension Fund ("the Funds") for the period 2022/23 to 2026/27.

4. Main Report

4.1 Azets, the external auditor to Lothian Pension Fund and Scottish Homes Pension Fund, has detailed its planned programme of work to support the statutory audit 2023/24. This is provided in full at Appendix 1.

4.2 Additionally, the Code of Audit Practice requires Azets to perform a wider scope audit over the following areas:

4.2.1 Financial sustainability
4.2.2 Financial management
4.2.3 Vision, leadership and governance
4.2.4 Use of resources to improve outcomes.

4.3 Progress against the plan will be reported to future meetings of the Pensions Audit Sub-Committee and thereafter the Committee.

5. Financial impact

5.1 The proposed audit fee for 2023/24 is £54,680 (a 6% increased on the 2022/23 fee of £51,590).

5.2 The audit fee is addressed in detail by Azets in Appendix 1, pages 20 to 21.

6. Stakeholder/Regulatory Impact

6.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the funds and it is invited to comment on the relevant matters at Committee meetings.

6.2 There are no adverse health and safety, governance, compliance or regulatory implications arising from this report. External audit is a critical part of the LPF Group's governance and assurance.

7. Background reading/external references

7.1 The responsibilities of Azets, as independent auditor, are established by the Local Government (Scotland) Act 1973 and the Code of Audit Practice, as approved by the Auditor General for Scotland and the Accounts Commission.

8. Appendices

Appendix 1 – "Lothian Pension Fund External Audit Annual Plan 2023/24" by Azets.

This page is intentionally left blank

Appendix 1

Lothian Pension Fund

External Audit Annual Plan

Year ended 31 March 2024

March 2024

Table of Contents

Introduction	3
Audit scope and general approach	4
Financial statements - significant audit risks	11
The wider scope of public audit	17
Audit team and timetable	19
Audit Fee	20
Audit independence and objectivity	22
Appendices	23

Introduction

Purpose

This audit plan highlights the key elements of our proposed audit strategy and provides an overview of the planned scope and timing of the statutory external audit of Lothian Pension Fund and Scottish Homes Pension Fund ("the Funds") for the year ended 31 March 2024 for those charged with governance.

Our audit work will cover:

- the financial statements within the 2023/24 annual report and accounts;
- the wider scope of public audit;
- any other work requested by Audit Scotland.

Adding value through the audit

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 standards of governance, better management and decision making and more effective use of resources.

Feedback

If there are any elements of this audit plan to which you do not agree or you would like to discuss, please let us know as soon as possible.

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 any member of your audit team.

This plan has been prepared for the sole use of those charged with governance and management and should not be relied upon by third parties. No responsibility is assumed by Azets Audit Services to third parties.

Openness and transparency

This report will be published on Audit Scotland's website http://www.audit-scotland.gov.uk/

Audit scope and general approach

Responsibilities of the auditor and the Funds

The Code of Audit Practice outlines the responsibilities of external auditors appointed by the Accounts Commission for Scotland and it is a condition of our appointment that we follow it.

Auditor responsibilities are derived from statute, International Standards on Auditing (UK) and the Ethical Standard for auditors, other professional requirements and best practice, the Code of Audit Practice and guidance from Audit Scotland.

The Funds have primary responsibility for ensuring the proper financial stewardship of public funds. This includes preparing an annual report and accounts that are in accordance with proper accounting practices. The Funds are also responsible for complying with legislation and putting arrangements in place for governance and propriety that enable it to successfully deliver its objectives.

Appendix 3 provides further details of our respective responsibilities.

Risk-based audit approach

We follow a risk-based approach to the audit 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. Our audit planning is based on:

Discussions with senior officers	**Our understanding of the public pension funds sector, its key priorities and risks**	**Attending & observing the Pensions Committee**
Guidance from Audit Scotland	**Discussions with Audit Scotland and public sector auditors**	**Discussions with internal audit and review of plans and reports**
Review of the Funds' corporate strategies and plans	**Review of the Funds' corporate risk registers**	**Consideration of the work of other inspection bodies**

Planning is a continuous process and our audit plans are updated during the course of our audit to take account of developments as they arise.

Communication with those charged with governance

Auditing standards require us to make certain communications throughout the audit to those charged with governance. These communications will be through the Pensions Committee.

Partnership working

We coordinate our work with Audit Scotland, internal audit, other external auditors and relevant scrutiny bodies, recognising the increasing integration of service delivery and partnership working within the public sector.

Audit Scotland

Although we are independent of Audit Scotland and are responsible for forming our own views and opinions, we do work closely with Audit Scotland throughout the audit. This helps identify common priorities and risks, treat issues consistently across the sector, and improve audit quality and efficiency. We share information about identified risks, good practices and barriers to improvement so that lessons to be learnt and knowledge of what works can be disseminated to all relevant bodies.

Audit Scotland undertakes national performance audits on issues affecting the public sector. We may review the Funds' arrangements for taking action on any issues reported in the national performance reports which have a local impact. We also consider the extent to which the Funds use the national performance reports as a means to help improve performance at the local level.

During the year we may also be required to provide information to Audit Scotland to support the national performance audits.

Delivering the audit

Hybrid audit approach

We adopt a hybrid approach to our audit which combines on-site visits with remote working; learning from the better practices developed during the pandemic.

All of our people have the equipment, technology and systems to allow them to work remotely or on-site, including secure access to all necessary data and information.

All of our staff are fully contactable by email, phone call and video-conferencing.

Meetings can be held over Microsoft Teams or by telephone.

We employ greater use of technology to examine evidence, but only where we have assessed both the sufficiency and appropriateness of the audit evidence produced.

Secure sharing of information

We use a cloud-based file sharing service that enables users to easily and securely exchange documents and provides a single repository for audit evidence.

Regular contact

During the 'fieldwork' phases of our audit, we will arrange regular catch-ups with key personnel to discuss the progress of the audit. The frequency of these meetings will be discussed and agreed with management.

Signing annual accounts

Audit Scotland recommends the electronic signing of annual accounts and uses a system called DocuSign.

Electronic signatures simplify the process of signing the accounts, which can be signed using any device from any location. There is no longer a need for duplicate copies to be signed, thus reducing the risk of missing a signature and all signatories have immediate access to a high-quality PDF version of the accounts.

Approach to audit of the financial statements

Our objective when performing an audit is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement and to issue an independent auditor's report that includes our auditor's opinion.

As part of our risk-based audit approach, we will:

- perform risk assessment procedures including updating our understanding of the Funds, including their environment, the financial reporting framework and their system of internal control;
- review the design and implementation of key internal controls;
- identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement level and the assertion level for classes of transaction, account balances and disclosures;
- design and perform audit procedures responsive to those risks, to obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion; and
- exercise professional judgment and maintain professional scepticism throughout the audit recognising that circumstances may exist that cause the financial statements to be materially misstated.

Materiality

“Reasonable assurance” is a high level of assurance, but is not a guarantee that an audit 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 the financial statements. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. We include an explanation in the auditor’s report of the extent to which the audit was capable of detecting irregularities, including fraud, and respective responsibilities for prevention and detection of fraud.

We apply the concept of materiality in planning and performing the audit, and in evaluating the effect of misstatements within the financial statements identified during the audit.

Judgments about materiality are made in the light of surrounding circumstances and are affected by our perception of the financial information needs of users of the financial statements, and by the size or nature of a misstatement, or a combination of both. The basis for our assessment of materiality for the year is set out in Appendix 1.

Any identified errors greater than £7.35 million in relation to investments and £0.66 million in relation to dealings with members will be recorded and discussed with you and, if not adjusted, confirmed as immaterial as part of your letter of representation to us.

Accounting systems and internal controls

We will follow a substantive testing approach to gain audit assurance rather than relying on tests of controls. As part of our work, we consider certain internal controls relevant to the preparation of the annual accounts such that we are able to design appropriate audit procedures. However, this work will not cover all internal controls and is not designed for the purpose of expressing an opinion on the effectiveness of internal controls. If we identify significant deficiencies in controls, we will report these to you in writing.

Specialised skill or knowledge required to complete the audit

Our audit team will consult internally with our Technology Risk team in assessing the information technology general controls (ITGC).

Going Concern

In most public sector entities (including pension funds), the financial reporting framework envisages that the going concern basis for accounting will apply where the entity's services will continue to be delivered by the public sector. In such cases, a material uncertainty related to going concern is unlikely to exist.

For many public sector entities, the financial sustainability of the entity is more likely to be of significant public interest than the application of the going concern basis. Our wider scope audit work considers the financial sustainability of the Funds.

Prevention and detection of fraud or error

In order to discharge our responsibilities regarding fraud and irregularity we require any fraud or irregularity issues to be reported to us as they arise. In particular, we require to be notified of all frauds which:

- involve the misappropriation or theft of assets or cash which are facilitated by weaknesses in internal control and;
- are over £5,000.

We also require a historic record of instances of fraud or irregularity to be maintained and a summary to be made available to us after each year end.

Anti-money laundering

We require to be notified on a timely basis of any suspected instances of money laundering so that we can inform Audit Scotland who will determine the necessary course of action.

Best Value

Appointed auditors have a duty to be satisfied that local government bodies have made proper arrangements to secure best value.

Under the Code of Audit Practice, the audit of Best Value in Lothian Pension Fund is fully integrated within the annual audit work performed by appointed auditors. We are required to evaluate and report on the performance of Lothian Pension Fund in meeting the Best Value duties.

Reporting our findings

At the conclusion of the audit we will issue:

- an independent auditor's report setting out our formal audit opinions within the annual report and accounts, and
- an annual audit report describing our audit findings, conclusions on key audit risks, judgements on the pace and depth of improvement on the wider scope areas, and any recommendations.

Definitions

We will use the following gradings to provide an overall assessment of the arrangements in place as they relate to the wider scope areas. The text provides a guide to the key criteria we use in the assessment, although not all of the criteria may exist in every case.

There is a fundamental absence or failure of arrangements
There is no evidence to support necessary improvement
Substantial unmitigated risks affect achievement of corporate objectives.

Arrangements are inadequate or ineffective
Pace and depth of improvement is slow
Significant unmitigated risks affect the achievement of corporate objectives

No major weaknesses in arrangements but scope for improvement exists
Pace and depth of improvement are adequate
Risks exist to the achievement of operational objectives

Effective and appropriate arrangements are in place
Pace and depth of improvement are effective
Risks to the achievement of objectives are managed

Financial statements - significant audit risks

Significant risks are risks that require special audit consideration and include identified risks of material misstatement that:

- our risk assessment procedures have identified as being close to the upper range of the spectrum of inherent risk due to their nature and a combination of the likelihood and potential magnitude of misstatement; or
- are required to be treated as significant risks due to requirements of ISAs (UK), for example in relation to management override of internal controls.

Significant risks at the financial statement level

The table below summarises significant risks of material misstatement identified at the financial statement level. These risks are considered to have a pervasive impact on the financial statements as a whole and potentially affect many assertions for classes of transaction, account balances and disclosures.

Management override of controls	**Audit approach**
Auditing Standards require auditors to treat management override of controls as a significant risk on all audits. This is because management is in a unique position to perpetrate fraud by manipulating accounting records and overriding controls that otherwise appear to be operating effectively. Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and thus a significant risk. Specific areas of potential risk include manual journals, management estimates and judgements and one-off	Procedures performed to mitigate risks of material misstatement in this area will include: • Documenting our understanding of the journals posting process and evaluating the design effectiveness of management controls over journals. • Analysing the journals listing and determining the criteria for selecting high risk and/or unusual journals. • Testing high risk and/or unusual journals posted during the year and after the draft accounts stage back to supporting documentation for appropriateness, corroboration and to ensure approval has been

Management override of controls	Audit approach
transactions outside the ordinary course of the business. **Risk of material misstatement: Very High**	undertaken in line with the Funds' journals policy. • Gaining an understanding of the key accounting estimates and critical judgements made by management. We will challenge assumptions and consider for reasonableness and indicators of bias which could result in material misstatement due to fraud. • Evaluating the rationale for any changes in accounting policies, estimates or significant unusual transactions.

Significant risks at the assertion level for classes of transaction, account balances and disclosures

Fraud in revenue recognition	Audit approach
Material misstatement due to fraudulent financial reporting relating to revenue recognition is a presumed risk in ISA 240 (The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements). The presumption is that the Funds could adopt accounting policies or recognise income in such a way as to lead to a material misstatement in the reported financial position. Given the financial pressures facing the public sector as a whole, there is an inherent fraud risk associated with the recording of income around the year end. In respect of the contributions received from the Funds' funding partners, we do not consider the risk of revenue recognition to be significant due to a lack of incentive and opportunity to manipulate transactions of this nature. The risk of fraud in relation to revenue recognition is however present in all other income streams. **Inherent risk of material misstatement:** **Revenue (occurrence/completeness): High**	We will perform the procedures below based on their value within the financial statements: • Documenting our understanding of the Funds' systems for income to identify significant classes of transactions, account balances and disclosures with a risk of material misstatement in the financial statements. • Evaluating the design of the controls in the key accounting systems, where a risk of material misstatement was identified, by performing a walkthrough of the systems. • Obtaining evidence that income is recorded in line with appropriate accounting policies and the policies have been applied consistently across the year. • Substantively testing material income streams using analytical procedures and sample testing of transactions recognised for the year.

Investments valuations (key accounting estimate)	Audit approach
The Funds held investments of £9.64 billion as at 31 March 2023, of which 39% (£3.75 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 publicly 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. **Inherent risk of material misstatement:** • **Investments (valuation/existence): High**	Procedures performed to mitigate risks of material misstatement in this area will include: • Evaluating management processes and assumptions for the calculation of the estimates, the instructions issued to the investment managers and the scope of their work. • Evaluating the competence, capabilities and objectivity of the investment managers. • Considering the basis on which the valuation is carried out and the challenge in the key assumptions applied. • Testing the information used by the investment managers to ensure it is complete and consistent with our understanding. • Ensuring that the year end valuations have been reflected correctly in the ledger and that accounting treatment within the financial statements is correct.

Investment property valuations (key accounting estimate)	Audit approach
LPF hold a portfolio of investment properties which, as at the 31 March 2023, was valued at £366 million. The management of the properties is undertaken by JLL, along with the Fund accounting for the portfolio. Investment properties are valued annually at fair value, in line with the Code. There is a significant degree of subjectivity in the measurement and valuation of investment properties. This subjectivity and the material nature of the Funds' investment property portfolio represents an increased risk of misstatement in the annual accounts. **Inherent risk of material misstatement:** **Investment property (valuation/ existence): High**	Procedures performed to mitigate risks of material misstatement in this area will include: • Ensuring that investment properties are recorded in the annual accounts in accordance with the Code and the Funds' accounting policies, and have been accounted for appropriately. We will review investment property valuations. • Considering the competence, capability and objectiveness of the valuer in line with ISA (UK) 500 Audit Evidence. We will review the valuation report and consider the assumptions used by the valuer against external sources of evidence. • Considering the scope of the valuer's work and the information provided to the valuer for completeness.

Disclosure of present Value of retirement obligations (key accounting estimate)	Audit approach
An actuarial estimate of the pension fund asset/liability is calculated on an annual basis under IAS 26 and on a triennial funding basis by an independent firm of actuaries with specialist knowledge and experience. The estimates are based on the most up to date membership data held by the Funds and have regard to local factors such as mortality rates and expected pay rises with other assumptions around inflation when calculating the liabilities. There is a risk that the assumptions used are not appropriate, which may result in material misstatement of this disclosure note. **Inherent risk of material misstatement:** **Retirement obligations (valuation): High**	Procedures performed to mitigate risks of material misstatement in this area will include: • Reviewing the controls in place to ensure that the data provided to the actuary is complete and accurate. • Considering the reasonableness of the assumptions used in the calculation against other local government pension fund actuaries and other observable data. • Agreeing the disclosures in the financial statements to information provided by the actuary.

The wider scope of public audit

Introduction

The Code of Audit Practice frames a significant part of our responsibilities in terms of four wider scope audit areas:

- Financial sustainability
- Financial management
- Vision, leadership and governance
- Use of resources to improve outcomes.

Our audit approach to the wider scope audit areas

Appointed auditors are required to consider the wider scope areas when:

- identifying significant audit risks at the planning stage of the audit;
- reaching conclusions on those risks;
- making recommendations for improvement;
- where appropriate, setting out conclusions on the audited body's performance.

When reporting on such arrangements, the Code of Audit Practice requires us to structure our commentary under the four areas identified above. Appendix 3 provides further detail on the definition, scope and audit considerations under each wider scope area.

Our planned audit work against these four areas is risk based and proportionate. Our initial assessment builds upon our understanding of the Funds' key priorities and risks along with discussions with management and review of Funds and committee minutes and key strategy documents.

Wider scope significant risks

At this stage, we have not identified any significant risks in relation to the wider scope areas. Audit planning is a continuous process and we will report all identified significant risks, as they relate to the four wider scope areas, in our annual audit report.

In formulating our audit plan, we identified areas of possible significant risk in relation to vision, leadership and governance and use of resources to improve outcomes. Our audit approach will include reviewing and concluding on the following considerations to substantiate whether significant risks exist:

Financial management

- Whether the quality of the financial performance information presented to the Pensions Committee allows appropriate scrutiny of Lothian Pension Fund's performance and supports effective decision making.

Vision, leadership and governance

- Based on expected favourable funding levels resulting from the latest triennial valuation the Fund has reduced employer contribution rates to 17.6% which is below the contribution stability mechanism ("the CSM") low bracket of 18%. We will review the governance around the decision to suspend the CSM for that purpose.
- Whether the decisions on Project Forth have been clearly communicated to key stakeholders.

Use of resources to improve outcomes

- Whether the Funds can evidence the achievement of value for money in the use of resources.
- How the Funds demonstrate a focus for improvement in the context of continuing financial challenge.
- How the Funds provide a clear link between investment decisions and actual performance achieved.

Audit team and timetable

Audit Team

Our audit team will be as follows:

Role	Name	Email
Key Audit Partner	Chris Brown	Chris.Brown@azets.co.uk
Engagement Manager	Adrian Kolodziej	Adrian.Kolodziej@azets.co.uk
Auditor in Charge	Thomas McCormick	Thomas.McCormick@azets.co.uk

Timetable

Please find below confirmation of our proposed timetable for the audit as previously discussed with management:

Audit work/output	Target month/s
Audit planning meeting	30 January 2024
Pension Committee to consider audit plan	20 March 2024
Interim audit	February-March 2024
Pension Committee to consider accounts	June 2024
Receipt of draft accounts and commencement audit fieldwork	June - July 2024
Independent auditor’s report	September 2024
Annual Audit Report to the Pension Committee and the Controller of Audit	September 2024

Our Requirements

The audit process is underpinned by effective project management to co-ordinate and apply our resources efficiently to meet your deadlines. It is essential that the audit team and the Funds’ finance team work closely together to achieve the above timetable.

In order for us to be able to complete our work in line with the agreed fee and timetable, we require the following:

- draft financial statements of a good quality by the deadlines you have agreed with us. These should be complete including all notes, the performance report and the accountability report;
- good quality working papers at the same time as the draft financial statements. These will be discussed with you in advance to ensure clarity over our expectations;
- relevant staff to be available and on site (as agreed) during the period of the audit;
- prompt and adequate responses to audit queries.

Audit Fee

Audit Scotland sets an expected audit fee that assumes the body has sound governance arrangements in place, has been operating effectively throughout the year, prepares comprehensive and accurate unaudited accounts and meets the agreed timetable for audit.

The expected fee is reviewed by Audit Scotland each year, based on Audit Scotland's overall budget proposals. The budget proposal and fee levels (for the 2023/24 audits) have been developed in the context of a challenging economic environment, increased expectations on the audit profession and the ongoing process of recovery following the Covid-19 pandemic.

As auditors we negotiate a fee with the Funds during the planning process. The fee may be varied above the expected fee level to reflect the circumstances and local risks within the body.

The expected fee set by Audit Scotland for the 2023/24 audit of the Funds is £54,680. Which represents a 6% increase on the 2022/23 fee. This increase is applied on a sector basis and reflects the conditions of the public sector market.

The breakdown of the fee for 2023/24 is shown in the table below.

Fee element	2023/24	2022/23
Auditor remuneration	£88,450	£64,360
Pooled costs	£3,220	-
Contribution to PABV costs	-	-
Audit support costs	-	£2,440
Sectoral cap adjustment	-£36,990	-£15,210
Total fee	**54,680**	**£51,590**

We will take account of the risk exposure of the Funds and the management assurances in place. We assume receipt of the draft working papers at the outset of our on-site final audit visit. If the draft accounts and papers are late, or agreed management assurances are unavailable, we reserve the right to charge an additional fee for additional audit work. An additional fee will be required in relation to any other significant work not within our planned audit activity.

Audit independence and objectivity

Auditor Independence

We are required to communicate on a timely basis all facts and matters that may have a bearing on our independence.

In particular, FRC's Ethical Standard stipulates that where an auditor undertakes non audit work, appropriate safeguards must be applied to reduce or eliminate any threats to independence.

Azets provides accounts preparation, corporation tax services and ad hoc VAT advice to LPFE Ltd and LPFI Ltd which are subsidiaries of Lothian Pension Fund. In 2023/24 non-audit fees are estimated to be c.£6,500.

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 Azets. In addition to this, Azets also iXBRL tag the financial statements for submission to HMRC along with the corporation tax return. This tagging exercise is performed by an individual who is not involved in the audit of the financial statements.

We have considered our integrity, independence and objectivity in respect of non-audit services provided and we do not believe there are any significant threats or matters which should be brought to your attention.

Appendices

Appendix 1: Materiality	24
Appendix 2: Group audit scope and risk assessment	27
Appendix 3: Responsibilities of the Auditor and the Funds	28

Appendix 1: Materiality

An omission or misstatement is regarded as material if it would reasonably influence the users of the financial statements. The assessment of what is material is a matter of professional judgement and is affected by our assessment of the risk profile of the Funds and Group and the needs of the users.

Whilst our audit procedures are designed to identify misstatements which are material to our audit opinion, we also report to those charged with governance and management any uncorrected misstatements of lower value errors to the extent that our audit identifies these.

Under ISA (UK) 260 we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA (UK) 260 defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

When planning, we make judgements about the size of misstatements which we consider to be material, and which provide a basis for determining the nature and extent of our audit procedures. Materiality is revised as our audit progresses, should we become aware of any information that would have caused us to determine a different amount had we known about it during our planning.

Our assessment, at the planning stage, of materiality for the year ended 31 March 2024 was calculated as follows.

Group and Funds Materiality

	Group £million	Lothian Pension Fund £million	Scottish Homes Pension Fund £million
Overall materiality for the financial statements	149	147	1.9
Performance materiality (75% of materiality)	111.75	110.25	1.43
Trivial threshold	7.45	7.35	0.01

Materiality	Our initial assessment is based on approximately 1.5% of the group and Funds' estimated net assets as at 2023/24. We consider this to be the principal consideration for the users of the annual accounts when assessing financial performance of the Funds' and the group.

Performance materiality	Performance materiality is the working level of materiality used throughout the audit. We use performance materiality to determine the nature, timing and extent of audit procedures carried out. We perform audit procedures on all transactions, or groups of transactions, and balances that exceed our performance materiality. This means that we perform a greater level of testing on the areas deemed to be at significant risk of material misstatement. Performance materiality is set at a value less than overall materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of the uncorrected and undetected misstatements exceed overall materiality.
Trivial misstatements	Trivial misstatements are matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. In accordance with Azets methodology we have set a trivial threshold at 5% of the overall materiality level. We will consider appropriateness of this level during the audit. Individual errors above this threshold are communicated to those charged with governance.

Special materiality for dealings with members

	Group £million	**Lothian Pension Fund £million**	**Scottish Homes Pension Fund £million**
Dealings with members materiality	13.64	13.3	0.34
Performance materiality (75% of materiality)	10.23	9.95	0.25
Trivial threshold	0.68	0.66	0.02

Materiality	We apply lower materiality for dealings with members, based on the fact these transactions are significant to the Funds' activities and it would not be appropriate to use the assets-based materiality to audit them. Our initial assessment is based on approximately 5% of the group and Funds' 2022/23 gross expenditure as disclosed in the

	2022/23 audited annual accounts. We consider this to be the principal consideration for the users of the annual accounts when assessing financial performance of the Funds and its group. We have set our trivial threshold at 5% of overall materiality as explained above.

The Remuneration Report and Related Parties disclosures are material by nature.

In performing our audit, we will consider any errors which result in a movement between the relevant bandings on the disclosure table to be material.

For related party transactions, in line with the standards we will consider the significance of the transaction with regard to both Funds and their counter parties, the smaller of which will drive materiality considerations on a transaction by transaction basis.

Appendix 2: Group audit scope and risk assessment

As Group auditor, under ISA (UK) 600 we are required to obtain sufficient appropriate audit evidence regarding the financial information of the components and the consolidation process to express an opinion on whether the group financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Group audit scope

The Group consists of the following entities:

Component	Significant	Level of response required
LPFE Ltd	No	Analytical
LPFI Ltd	No	Analytical

Analytical - the component is not significant to the Group and audit risks can be addressed sufficiently by applying analytical procedures at the Group level.

Appendix 3: Responsibilities of the Auditor and the Funds

The Accounts Commission and Audit Scotland

The Accounts Commission is an independent public body. Its members are appointed by Scottish Ministers and are responsible for holding local government to account.

Under statute, the Accounts Commission appoints a Controller of Audit to consider the results of the audit of accounts, including the wider-scope responsibilities and Best Value auditing. The Controller of Audit makes reports to the Accounts Commission on matters arising from the accounts and on Best Value and acts independently of the Accounts Commission when reporting to it.

Audit Scotland is an independent statutory body that co-ordinates and supports the delivery of high-quality public sector audit in Scotland. Audit Scotland oversees the appointment and performance of auditors, provides technical support, delivers performance audit and Best Value work programmes and undertakes financial audits of public bodies.

Code of Audit Practice

The Code of Audit Practice (the 2021 Code) describes the high-level, principles-based purpose and scope of public audit in Scotland.

The Code of Audit Practice outlines the responsibilities of external auditors appointed by the Accounts Commission and it is a condition of our appointment that we follow it.

Our responsibilities

Auditor responsibilities are derived from the Code, statute, International Standards on Auditing (UK) and the Ethical Standard for auditors, other professional requirements and best practice, and guidance from Audit Scotland.

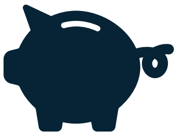
We are responsible for the audit of the accounts and the wider-scope responsibilities explained below. We act independently in carrying out our role and in exercising professional judgement. We report to the Pensions Committee and others, including Audit Scotland, on the results of our audit work.

Weaknesses or risks, including fraud and other irregularities, identified by auditors, are only those which come to our attention during our normal audit work in accordance with the Code and may not be all that exist.

Wider scope audit work

Reflecting the fact that public money is involved, public audit is planned and undertaken from a wider perspective than in the private sector.

The wider scope audit specified by the Code broadens the audit of the accounts to include additional aspects or risks in areas of financial management; financial sustainability; vision, leadership and governance; and use of resources to improve outcomes.

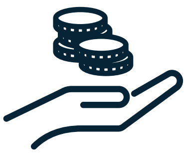


Financial management

Financial management means having sound budgetary processes. Audited bodies require to understand the financial environment and whether their internal controls are operating effectively.

Auditor considerations

Auditors consider whether the body has effective arrangements to secure sound financial management. This includes the strength of the financial management culture, accountability, and arrangements to prevent and detect fraud, error and other irregularities.



Financial sustainability

Financial sustainability means being able to meet the needs of the present without compromising the ability of future generations to meet their own needs.

Auditor considerations

Auditors consider the extent to which audited bodies show regard to financial sustainability. They look ahead to the medium term (two to five years) and longer term (over five years) to consider whether the body is planning effectively so it can continue to deliver services.

Vision, leadership and governance

Audited bodies must have a clear vision and strategy and set priorities for improvement within this vision and strategy. They work together with partners and communities to improve outcomes and foster a culture of innovation.

Auditor considerations

Auditors consider the clarity of plans to implement the vision, strategy and priorities adopted by the leaders of the audited body. Auditors also consider the effectiveness of governance arrangements for delivery, including openness and transparency of decision-making; robustness of scrutiny and shared working arrangements; and reporting of decisions and outcomes, and financial and performance information.

Use of resources to improve outcomes

Audited bodies need to make best use of their resources to meet stated outcomes and improvement objectives, through effective planning and working with strategic partners and communities. This includes demonstrating economy, efficiency and effectiveness through the use of financial and other resources, and reporting performance against outcomes.

Auditor considerations

Auditors consider the clarity of arrangements in place to ensure that resources are deployed to improve strategic outcomes, meet the needs of service users taking account of inequalities, and deliver continuous improvement in priority services.

Best value

Appointed auditors have a duty to be satisfied that local government bodies have made proper arrangements to secure best value.

Our work in respect of the Funds' best value arrangements is integrated into our audit approach, including our work on the wider scope areas as set out in this plan.

Audit quality

The Auditor General and the Accounts Commission require assurance on the quality of public audit in Scotland through comprehensive audit quality arrangements that apply to all audit work and providers. These arrangements recognise the importance of audit quality to the Auditor General and the Accounts Commission and provide regular reporting on audit quality and performance.

Audit Scotland maintains and delivers an Audit Quality Framework.

The most recent audit quality report can be found at Quality of public audit in Scotland: Annual report 2022/23 | Audit Scotland (audit-scotland.gov.uk)

Funds' responsibilities

The Funds have primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enables it to successfully deliver its objectives. The features of proper financial stewardship include the following:

Area	Funds responsibilities
Corporate governance	The Funds are responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Those charged with governance should be involved in monitoring these arrangements.
Financial statements and related reports	The Funds have responsibility for: • preparing financial statements which give a true and fair view of the financial position and its expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation; • maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support the balances and transactions in its financial statements and related disclosures; • ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority; and • preparing and publishing, along with the financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report in accordance with prescribed requirements. Management commentaries should be fair, balanced and understandable. Management is responsible, with the oversight of those charged with governance, for communicating relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework. The relevant information should be communicated clearly and concisely.

Area	Funds responsibilities
	The Funds are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of its objectives and safeguard and secure value for money from the public funds at its disposal. The Funds are also responsible for establishing effective and appropriate internal audit and risk-management functions.
Standards of conduct for prevention and detection of fraud and error	The Funds are responsible for establishing arrangements to prevent and detect fraud, error and irregularities, bribery and corruption and also to ensure that its affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.
Financial position	The Funds are responsible for putting in place proper arrangements to ensure the financial position is soundly based having regard to: • such financial monitoring and reporting arrangements as may be specified; • compliance with statutory financial requirements and achievement of financial targets; • balances and reserves, including strategies about levels and their future use; • plans to deal with uncertainty in the medium and long term; and • the impact of planned future policies and foreseeable developments on the financial position.
Best value	The Funds have a specific responsibility to make arrangements to secure Best Value. Best Value is defined as continuous improvement in the performance of the body's functions. In securing Best Value, the local government body is required to maintain an appropriate balance among: • The quality of its performance of its functions. • The cost to the body of that performance.

Area	Funds responsibilities
	• The cost to persons of any service provided by it for them on a wholly or partly rechargeable basis. In maintaining that balance, the Funds shall have regard to: • Efficiency • Effectiveness • Economy • The need to meet the equal opportunity requirements. The Funds should discharge its duties in a way which contributes to the achievement of sustainable development. In measuring the improvement of the performance of a local government body's functions for the purposes of this section, regard shall be had to the extent to which the outcomes of that performance have improved. The Scottish Government's Statutory Guidance on Best Value (2020) requires bodies to demonstrate that they are delivering Best Value in respect of seven themes: 1. Vision and leadership 2. Governance and accountability 3. Effective use of resources 4. Partnerships and collaborative working 5. Working with communities 6. Sustainability 7. Fairness and equality. Specified audited bodies are required to prepare and publish performance information in accordance with Directions issued by the Accounts Commission.

This page is intentionally left blank

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Cost Benchmarking

Item number 6.11

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 note the report; and

1.2 note that the CEM Investment Benchmarking Analysis (for the year to 31 March 2023) and the CEM Pension Administration benchmarking report 2023 have been provided on a confidential basis to the Conveners of the Committee and Audit Sub-Committee and the Independent Professional Observer.

David Vallery

Chief Executive Officer, Lothian Pension Fund

Contact: Emmanuel Bocquet, Chief Investment Officer, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Cost Benchmarking

2. Executive Summary

2.1 CEM Investment Benchmarking Analysis for the year to 31 March 2023 shows that Lothian Pension Fund (LPF)'s investment costs are significantly lower than its benchmark. LPF's costs are also significantly lower than the CEM-selected global peer group and the CEM LGPS universe.

2.2 Over the long term (CEM analysis over 9 years), Lothian has delivered investment returns above the LGPS peer group median with a lower level of risk and at lower cost.

2.3 CEM Pension Administration Analysis shows that Lothian delivers a high level of above-benchmark service at below-benchmark cost.

3. Background

3.1 The purpose of this report is to inform Committee about the annual results from benchmarking of:

- investment costs for the Lothian Pension Fund; and
- pension administration costs for Lothian Pension Fund and Scottish Homes Pension Fund (collectively known as **LPF**).

3.2 LPF's annual report for 2022/23 identifies £48.1m of total management expenses, of which investment costs (£41.4m) are by far the largest share, as expected.

3.3 Benchmarking is undertaken to help identify areas where improvements can be made to deliver better value for money and benefiting employers and members. The exercise should facilitate:

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

4. Main Report

Investment Cost Benchmarking

4.1 Analysis of investment costs was carried out by independent provider CEM Benchmarking Inc. ('CEM'). CEM's 2022/2023 database includes 34 LGPS funds with fund assets from £0.8bn to £27.8bn, and a wider global universe of 293 funds with £8.3tn of assets.

4.2 Lothian Pension Fund's actual investment cost of 0.26% of average assets was below the benchmark cost of 0.49% (adjusted for Lothian's asset mix). The majority of LPF's investment cost relates to external management of private markets assets (including infrastructure, private equity and private credit) and externally managed equity mandates. The 0.23% difference with the benchmark is equivalent to a saving of £21.8m per year. The main contributing factors to this difference are attributable to:

- LPF managing a high percentage of assets on an internal basis compared to the benchmark peer group; and
- LPF accessing externally managed private market investments at lower costs than the benchmark peer group.

4.3 CEM analysis shows that the Lothian Pension Fund investment cost of 0.26% is significantly below the median cost of 0.78% for the 39 funds in the global peer group (peer group costs are unadjusted for Lothian's asset mix).

4.4 Lothian's investment cost of 0.26% is also significantly below the median cost of 0.73% for the 34 funds in the LGPS peer group. This equates to a c.£45m saving in investments costs compared to the LGPS peer group median.

4.5 CEM also highlight that investment costs should be taken in the context of a fund's long-term net returns and risk. As part of the benchmarking, CEM provide the median annual return from their LGPS universe.

4.6 Lothian's 9-year[1] net return of +8.3% p.a. was above the LGPS median of +7.6% p.a., and in the 95th percentile of the CEM LGPS fund universe of 34 funds, where the 100th percentile is the highest return.

4.7 Lothian's 9-year higher net return was also delivered with less risk (8.4%) than the median LGPS level of risk (10.0%).

4.8 Appendix 1 provides further detail on the investment cost benchmarking process.

[1] 9 years is the longest period for which CEM provide LGPS data.

Pension Administration Benchmarking

4.9 In previous years, analysis of pension administration costs was undertaken by the Chartered Institute of Public Finance & Accountancy (**CIPFA**). Due to delays in receiving reports from CIPFA and a reduction in comparable peers, the decision was taken to end participation in CIPFA benchmarking.

4.10 To obtain further insight into pension administration cost and benchmarking on quality of service, LPF has also participated in the pension administration benchmarking survey carried out by CEM. Whilst CIPFA was exclusive to the LGPS, CEM also includes UK private sector schemes. Participating funds, both private and public, are of a significantly larger size than LPF. CEM's methodology includes an adjustment to business-as-usual costs to allow for fairer comparison to eliminate the effect of economies of scale. As a result, peer costs are increased by £8.25 per member.

4.11 Results from the 2023 CEM benchmarking survey again show LPF's pension administration service to be categorised as "low cost; high service standard", with a cost per member of £30.49. The adjusted peer average is £35.42 per member.

4.12 As with investment costs, cost in isolation is unhelpful, and as agreed in the 2022/23 strategy, the fund strives to provide a quality service which offers value for money rather than being cheap. Again, the CEM benchmarking survey provides positive confirmation of this as LPF's service score is 68 compared to the peer median of 63.

4.13 Further details of the pension administration cost benchmarking process are provided in Appendix 2.

5. Financial impact

5.1 There are no financial implications arising directly from this report. Out of LPF's total management costs of £48.1m for 2022/23, investment costs amounted to £41.4m, administrative costs to £2.7m and oversight and governance costs to £4.0m. The benchmarking exercise should aid future cost management efforts.

6. Stakeholder/Regulatory Impact

6.1 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.

6.2 There are no adverse health and safety, governance, compliance, or regulatory implications as a result of this report.

7. Background reading/external references

7.1 None.

8. Appendices

Appendix 1 – Investment Cost Benchmarking
Appendix 2 – Pension Administration Benchmarking

Appendix 1

Investment Cost Benchmarking

Background

LPF has contributed to CEM's database to better understand its investment expense base and how it compares with other pension funds.

The benchmarking analysis undertaken by CEM aims to provide comprehensive, like-for-like comparisons with similar funds, but they are unable to capture all investment costs from all funds. Consequently, the total actual costs reported by CEM differ from those reported in Lothian Pension Fund's annual report. CEM includes private asset performance fees, but investment transaction costs, including property operational costs, are excluded.

Care should be taken in deriving conclusions from the headline data. CEM itself states that "being high or low cost is neither good nor bad". What matters is whether a pension fund is receiving sufficient value for the costs incurred. This is reflected in the long term returns of pension funds, net of costs.

2023 Cost Benchmarking

The CEM 2022/2023 database includes 34 LGPS funds with fund assets from £0.8bn to £28 bn, and a wider global universe of 293 funds with £8.3tn of assets.

The peer group for calculating LPF's benchmark cost contains 39 funds, including 7 LGPS funds. The peer group funds have been selected on the basis of fund size and holding a broadly similar portfolio of assets to LPF.

The median fund size within the peer group is £9.7bn, which compares with Lothian Pension Fund's average assets of £9.6bn over the year to 31 March 2023. CEM calculates a benchmark cost for Lothian Pension Fund which reflects the fund's asset class mix, based on the asset class costs of the peer group funds.

LPF's actual cost figure to 31 March 2023 of c.0.26% of average assets was below the benchmark cost of 0.49%. CEM calculate that the 0.23% difference is equivalent to a saving of £21.8m for the year to 31 March 2023.

CEM analysis also shows that the Lothian Pension Fund cost of 0.26% is significantly lower than the median cost of 0.78% for the 39 funds in the global peer group (unadjusted for Lothian's asset mix) and also significantly lower than the median cost of 0.73% for the 34 funds in the LGPS peer group.

Previous CEM cost analyses are shown below (analyses prior to 31 March 2017 were calculated on a calendar year basis):

- 31 March 2022: 0.29% versus benchmark cost of 0.50%
- 31 March 2021: 0.35% versus benchmark cost of 0.46%
- 31 March 2020: 0.35% versus benchmark cost of 0.51%
- 31 March 2019: 0.39% versus benchmark cost of 0.48%
- 31 March 2018: 0.43% versus benchmark cost of 0.55%
- 31 March 2017: 0.31% versus benchmark cost of 0.48%
- 31 December 2015: 0.36% versus benchmark cost of 0.45%
- 31 December 2014: 0.39% versus benchmark cost of 0.50%

This page is intentionally left blank

Appendix 2

Pension Administration Benchmarking

Background

CEM has been benchmarking pensions administration for over 10 years, primarily in the US, Canada, and the Netherlands. In the UK, participants include some of the other public sector pension schemes and other large company pension Schemes. In 2019, Lothian Pension Fund was invited to join a group of other Local Government Pension Scheme (LGPS) funds taking part in the survey for the first time in 2019.

CEM Pensions Administration benchmarking

The Fund's benchmarking peer group within CEM is made up some UK private sector schemes, as well as other LGPS funds. In 2023, the peer group includes an increased number of LGPS funds, allowing a more meaningful comparison. The other funds in the peer group, both private and public, are generally of a significantly larger size than Lothian Pension Fund.

The CEM survey poses question about cost, covering the following areas:

- Business as usual costs;
- Project costs; and
- Governance costs.

Additional questions focus on delivery of service, particularly on the channels used to communicate with customers and how different customer groups are served. A scoring system is then used to derive a service score. CEM note: 'Many UK pension schemes focus too narrowly on performance against designated services standards (timescales for performing certain activities). SLAs {Service Level Agreements} are important but are a very limited measure of the members' service experience in their own right. Our scoring system reflects the rounded experience, seen from the members' perspective.'

CEM also carry out complete regular research on topics of interest which helps to refresh their model and reflect new practices.

Results from the 2023 survey show that cost per member of £30.49 is lower than the adjusted average of £35.42 (£26.30 and £39.94 respectively in 2022). Results are adjusted to take into account differences in the number of members within the peer group. As noted above, changes have been made to the peer group in 2023. LPF's third-party fees and other direct costs, which include accommodation, were lower than the peer group average.

CEM believes that looking at cost in isolation is unhelpful, and, to provide context and measure value for money, a service score is also calculated. Service is defined from a member's perspective and higher service means more channels, faster turnaround times, more availability, more choice, better content, and higher quality. This score is calculated by weighting the service scores for three customer groups (active members, deferred members, and pensioners) based on the membership mix. The results show a service score of 74 out of 100, which is higher than the peer median of 67. The 2022 score is above the score of 69 for 2021 (the peer median for 2021 was 64). Reasons for the higher score compared to the peer group include:

- paying retirement lump sums more quickly – for both active and deferred members;
- a higher percentage of both active and deferred members use our secure online portal, (59.6% and 58.4% respectively, compared to 49.3% (active) and 31.1% for the peer group average);
- our telephone service has returned to pre-pandemic experience for members; and
- carrying out targeted campaigns including encouragement to update beneficiary information.

The full CEM pensions administration benchmarking report is available on request.

Participation in the CEM benchmarking pensions administration survey also allows access to additional research and workshops to meet with the peer group and other pension funds to identify areas of best practice which could be adopted for future service delivery.

Fund officers recently attended CEM's UK Pension Administration Workshop. This event included presentations from one of CEM's Canadian clients, providing insight into their processes and a site visit to Brightwell, administrators of the BT Pension Scheme which included a demonstration of their online retirement process and a session on how their operating model has been developed to provide an improved customer journey. Officers also contributed to a discussion on developing the survey for 2024.

The benchmarking information provides a useful snapshot of costs compared with funds that are prepared to share their data, but care should be taken in interpreting the information as the output relies on the accuracy of the data supplied by participants.

Pensions Committee

2.00pm, Wednesday, 20 March 2024

Risk & Compliance Update

Item number 6.12

1. Recommendations

The Pensions Committee (Committee) is requested to:

1.1 note the LPF group's Risk Register and Quarterly Update

Kerry Thirkell
Chief Risk Officer, Lothian Pension Fund

Contact: Kerry Thirkell, Chief Risk Officer, Lothian Pension Fund

E-mail: lpfgovernancecomms@lpf.org.uk | Tel: 0333 996 1900

Risk & Compliance Update

2. Executive Summary

2.1 This paper provides an overview of monitoring and assurance undertaken in LPF since the last meeting, noting any material observations or exceptions.

2.2 This paper also provides a summary of the work to enhance current risk management arrangements.

3. Risk Management

3.1 The LPF Risk Management Group (RMG) met on 30 January 2024 and considered the LPF group risk register and the key and emerging risks to which the LPF group are exposed.

3.2 Governance risk has been elevated to high to reflect concerns regarding the effectiveness of pension committee operations. People risks have also increased to high due to recruitment and change factors affecting several business areas and dependencies on key roles and functions. Supplier performance and oversight risk is reduced to medium and continues trending down as improvements to the supplier management framework have been agreed and improved oversight of critical suppliers introduced and reported. Meanwhile improvements to governance and operations regarding the JISP (now Joint Investment Forum, JIF) and investment processes through the Investment Governance Improvement Plan project have also contributed to a reduction in the risk of regulatory breach. Several other risks, although medium rated, are trending up, and the leadership team have been considering any additional controls or mitigating actions that should be introduced at this time. More information is set out below.

3.3 A summary of LPF key risks is noted in appendix 1, whilst the updated risk register summary is available in appendix 2 to this report.

3.4 The first quarter of 2024 has seen activity developing the suite of LPF operational functional risk profiles to cover more business areas. This exercise is anticipated to complete in the coming months which will help drive a controls assurance programme to compliment other existing oversight and assurance work.

3.5 The Investment Governance Improvement Plan ('IGIP') project has now concluded. The project has run since April 2023 and focused on 4 workstreams: Joint Investment Strategy Panel ('JISP') and Governance; Investments; Strategy & Operations and Middle Office; and Risk Management & ICARA. All issues identified through the Investment Services Review that determined the contents of the project have been recorded and tracked as issues as part of the LPF issue management process throughout the life of the project and project deliverables have been aligned to corresponding issues. Whilst all issues and associated actions have now been closed, one deliverable in respect of consideration of options for 'middle office' arrangements (middle office covers the set of activities that sit in between the front office, the Investment function, and the back office, which at LPF is the Finance function) is now being taken forward by the leadership team.

4. Monitoring & Assurance Summary

Compliance Monitoring Programmes (CMPs)

Non-FCA Compliance Monitoring Programme – Findings & Recommendations

4.1 All testing scheduled for Q4 2023 has been completed with no matters requiring to be brought to the attention of the Committee.

4.2 The 2024 LPF CMP is currently undergoing a scheduled annual review, and any updates to the programme will be implemented from Q2. The CMP focuses on monitoring compliance with The Pensions Regulator (TPR) obligations and any changes arising from the new TPR Code of Practice will be integrated into the CMP.

BDO LPFI Compliance Monitoring Programme - Findings & Recommendations

4.3 All testing scheduled for Q4 2023 has been completed. Two new issues were recorded following completion of testing by BDO, neither of which are considered material. Both were acted on and closed during Q4.

Investment Compliance

4.4 During August 2023, the Risk and Compliance team recruited additional resource with a broad remit to review and improve the existing Investment and Front Office Compliance environment.

4.5 Throughout Q4, a range of enhancements have been delivered to the existing suite of compliance tests within the Investment Management System ("CRIMS"), improving accuracy, process efficiency and resiliency. These tests exist in order to ensure that funds remain in compliance with mandate restrictions, and other operational and regulatory restrictions.

4.6 Following the successful upgrade to CRIMS in November, a full review of the completeness and accuracy of these compliance tests is underway, and scheduled for completion during Q1 2024.

Internal Audit

4.7 At the time of writing, audit reports for Business Continuity and Information Security Arrangements have not yet been finalised.

4.8 The planning process for 2024/25 audit reviews is underway and the Internal Audit team have sought input from LPF regarding potential audit reviews. The Internal Audit team will seek approval for the plan for LPF (including LPFI and LPFE coverage) from the Pension Committee in March.

Policy Updates

4.9 The Personal Dealing policy has been reviewed and enhanced, with the new policy effective from 1 January 2024. Whilst the policy is broadly similar to the previous version in terms of the requirements it places on LPF employees, the new policy has been simplified to ensure understanding.

4.10 Accompanying the Personal Dealing policy was the introduction of a new Market Conduct policy which outlines the standards expected of LPF employees in that area.

4.11 In December 2023, the Conflicts of Interest (COI) policy underwent a significant rewrite, to provide greater clarity on LPF's approach to identifying, managing, and recording conflicts across the group. Improvements were also made to the COI register, to ensure more robust record keeping of conflicts and the steps taken to manage them.

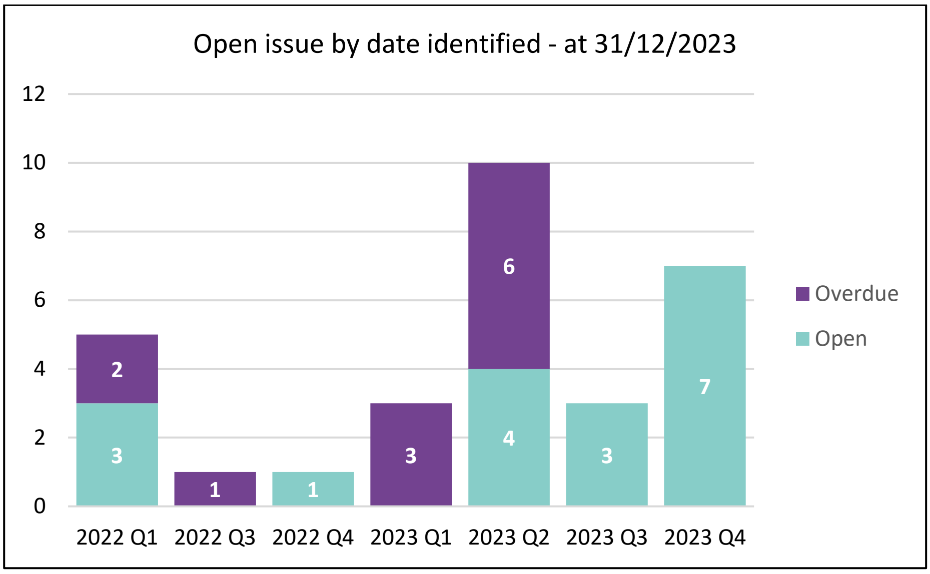
Training

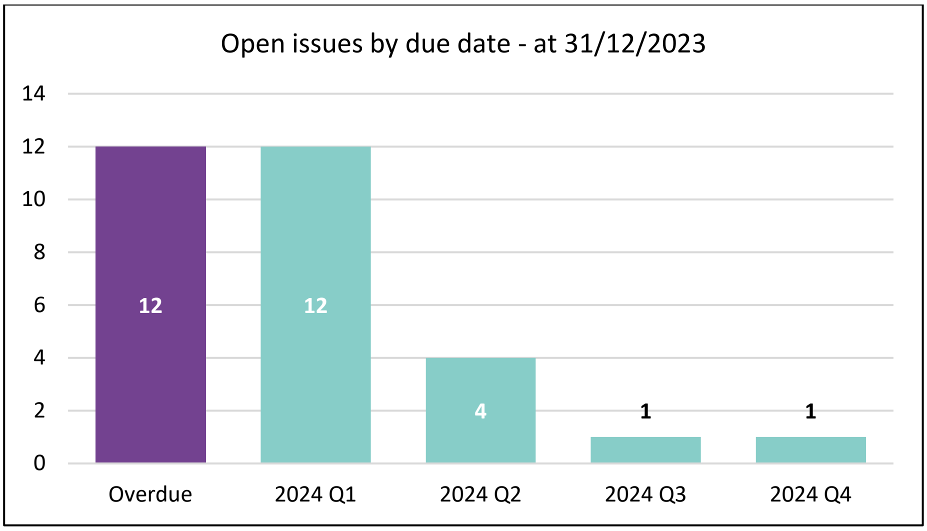
4.12 A series of training sessions, covering Market Conduct and Personal Dealing, were held in December, with a video version produced for non-attendees.

Issues & Incidents

4.13 Improvements continue to be made to the processes, governance and reporting regarding LPF Issues and incidents.

Issues





4.14 During Q4, 16 issues were closed and 9 new issues were raised.

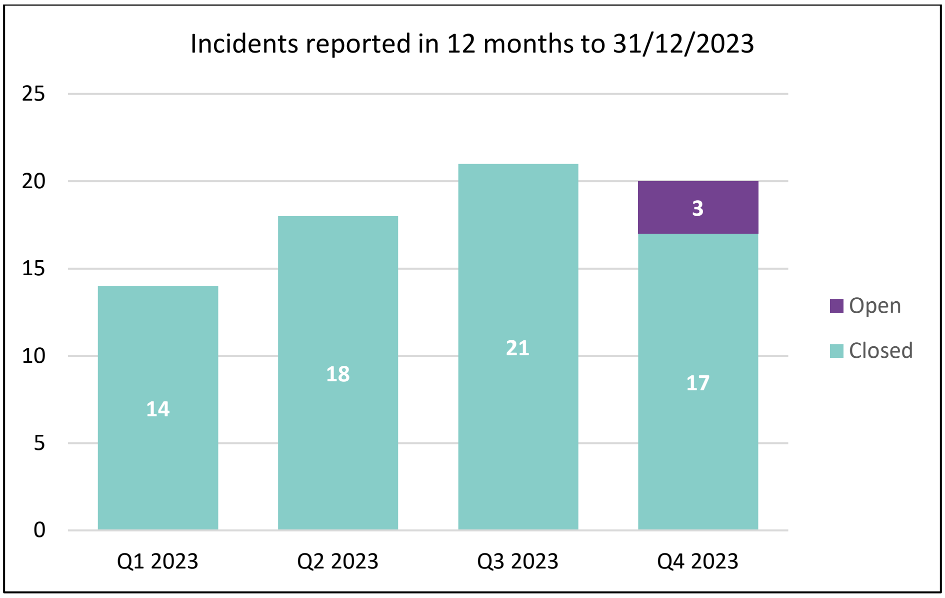
4.15 Since end Q4, no further issues have been added. At the time of writing, there are 24 open issues, 2 of which are overdue and a further 9 have a due date by the end of March.

4.16 The Risk & Compliance team continue to actively engage with issue stakeholders to discuss how agreed actions are being taken by the due date. Current open issues by rating and due date are as follow:

Issue Rating	Overdue	2024 Q1	2024 Q2	2024 Q3	2024 Q4	2025 Q2	Total
High		3	1			1	5
Medium	1	3	4			1	9
Low	1	3	3	1	1	1	10
Total	**2**	**9**	**8**	**1**	**1**	**3**	**24**

Incidents

4.17 Twenty incidents were raised during Q4 2023, three of which were classified as non-reportable data breaches, and one as a non-reportable FCA regulatory breach. Required actions to remediate seventeen of these incidents were completed during Q4, and the incidents subsequently closed.



4.18 During Q1, 2 member payment errors have been identified where member benefits have been paid out incorrectly. These errors were picked up through the McCloud rectification work being undertaken. Further review work is currently underway to identify any other similar cases and determine what/if any further action is required to be taken.

4.19 Further information on issues and incidents is available on request.

The Pension Regulator – Code of Practice

4.20 In January 2024, The Pensions Regulator (TPR) laid their new general code of practice before parliament (the 'General Code'). This consolidates and enhances 10 existing TPR codes into a single code of practice, aiming to provide one set of clear, consistent expectations on scheme governance and administration, with the new format designed to make it easier for schemes to identify TPR's expectations and consider whether they are meeting them.

4.21 In addition to consolidating existing codes, new expectations have been added on areas including Risk, Cyber Controls, and ESG. LPF will review the code and carry out a gap analysis against existing practices and processes and make any required changes to the LPF CMP. The final code is expected to come into effect at the end of March 2024.

5. Financial impact

5.1 There are no financial impacts to note at this time.

6. Stakeholder/Regulatory Impact

6.1 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.

6.2 Except as otherwise stated in the report itself, there are no adverse health and safety, governance, compliance or regulatory implications as a result of this report.

7. Background reading/external references

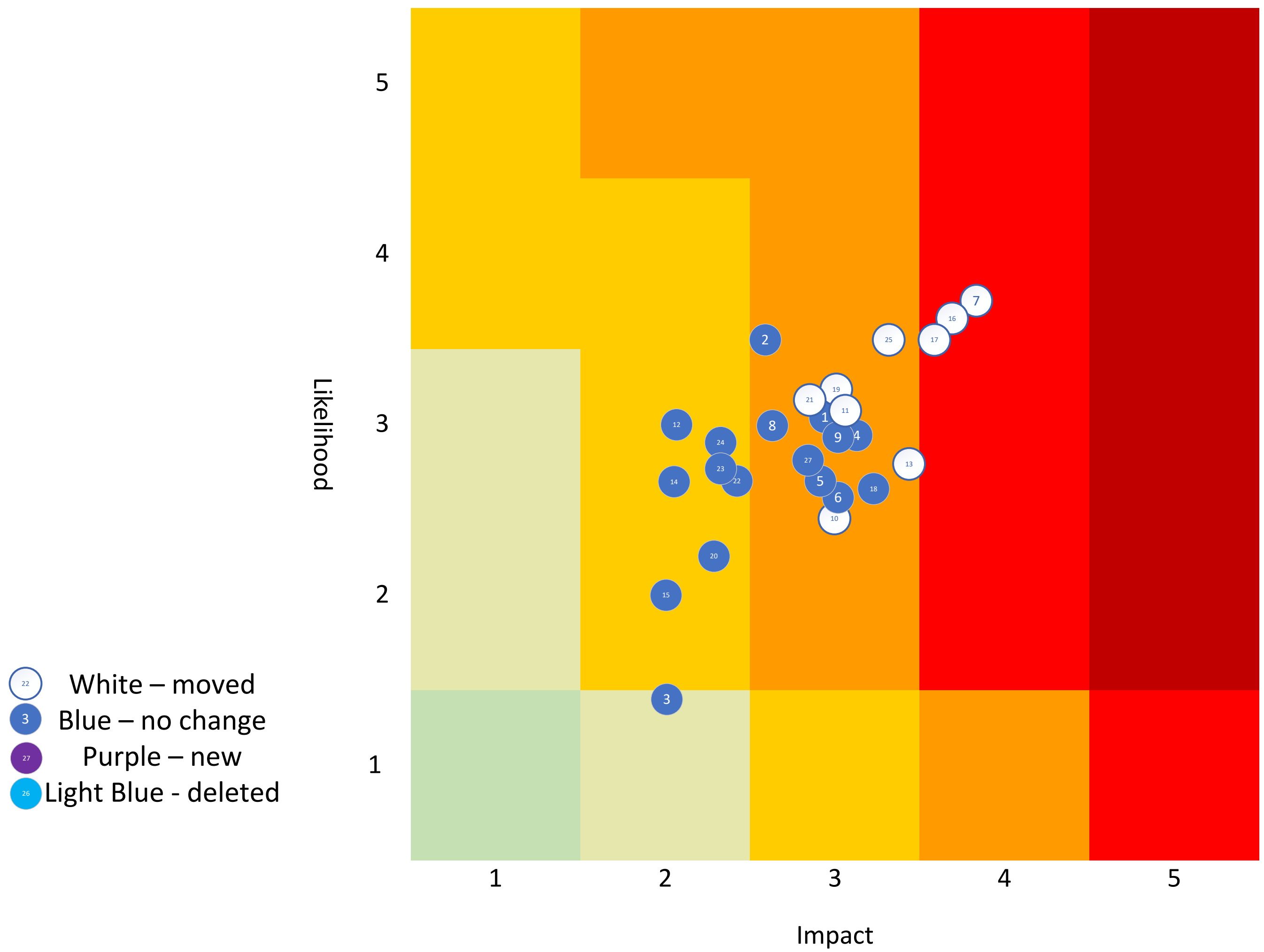
7.1 None.

8. Appendices

Appendix 1a and b – LPF Key Risks
Appendix 2 – Risk Register Summary

This page is intentionally left blank

Appendix 1a


Likelihood
5
4
3
2
1
Impact
1
2
3
4
5
White – moved
Blue – no change
Purple – new
Light Blue - deleted

This page is intentionally left blank

Appendix 1b - Risk Register Summary

Total Risks	New	Improving	Deteriorating	Unchanged	Deleted
26	0	1	8	17	0

Risk Rating	Count
Very High	-
High	3
Medium	15
Low	7
Insignificant	1

Ref	Type	Name	Rating
7	Governance Legal & Compliance	Discharge of responsibilities and accountabilities	⇧
16	People & Culture	Recruitment & retention	⇧
17	People & Culture	Resources	⇧
25	Governance Legal & Compliance	Best practice governance	⇧
2	Information Security IT & Data	Data Management	⇔
13	Business Operations	Supplier performance and oversight	⇩
19	Investment Management	Investment Strategy	⇧
11	Information Security IT & Data	Cybersecurity	⇧
4	Governance Legal & Compliance	Regulatory breach	⇔
21	Strategy	Strategic Goals	⇧
18	Strategy	Climate change & Responsible Investing	⇔
1	Investment Management	Investment Performance	⇔
9	Business Operations	Business Interruption	⇔
6	Business Operations	Investment operations errors	⇔
27	Business Operations	Operational errors	⇔
8	Business Operations	Investment services delivery	⇔
5	Scheme	Employer failure	⇔
10	Information Security IT & Data	IT systems	⇧
24	Information Security IT & Data	Data integrity and quality	⇔
23	Scheme	Unexpected drop in funding	⇔
22	Scheme	Meeting liabilities or capital requirements	⇔
20	Business Operations	Communications	⇔
12	Business Operations	Project and change activities	⇔
14	Business Operations	Fraud by LPF staff or relating to members	⇔
15	Business Operations	Member engagement, servicing and reporting	⇔
3	Conduct	Unauthorised activity or poor conduct	⇔

Appendix 2

LPF Risk Register

LPF group wide risks.
Last updated: Risk Management Group (RMG) meeting 31 Jan 2024

Risk Ref	Level 1 Risk	Level 2 Risk	Risk name	Risk Description	Entity	Current Risk	Previous Risk Rating
7	Governance Legal & Compliance	Governance	Discharge of responsibilities and accountabilities	Pension Committee or Board don't effectively discharge their responsibilities and accountabilities to the fund and decisions are taken against sound advice, beyond delegated authorities, on political grounds or due to lack of knowledge or attendance	LPF		
16	People & Culture	People & Culture	Recruitment & retention	Ability to attract, recruit, engage and retain talent leading to workforce capability gaps could affect LPF's ability to meet strategic objectives and legal and regulatory requirements and expectations	All		
17	People & Culture	People & Culture	Resources	Key person dependencies (particularly in significant roles or small teams) and resourcing could affect LPF's ability to meet strategic objectives and legal and regulatory requirements and expectations	All		
25	Governance Legal & Compliance	Governance	Best practice governance	Failure to operate within corporate governance best practice and principles could impact strategic decision making and may lead to project failure, increased costs, poor morale and/or regulatory censure	All		
2	Information Security IT & Data	Data	Data Management	Mis-management or poor maintenance and protection of data could lead to operational errors, regulatory breaches/fines or reputational damage	All		
13	Business Operations	Third Party	Supplier performance and oversight	Sub-optimal service performance/delivery, management and oversight of third party suppliers could lead to lack of resiliency and/or material errors and breaches	All		
19	Investment Management	Investment Management	Investment Strategy	Investment strategy does not deliver investment objectives due to incorrect implementation, investments falling outside agreed risk parameters or inadequate JISP governance. This could lead to a fall in funding levels and inability to meet liabilities.	LPF and LPFI		
11	Information Security IT & Data	Information Security & Cyber	Cybersecurity	Inadequate cyber and data security arrangements to protect LPF from information security threats and cyber-attacks could prevent key operational processes from being undertaken and lead to financial losses and reputational damage	All		
4	Governance Legal & Compliance	Regulatory Compliance	Regulatory breach	LPF do not meet regulatory obligations leading to enforcement action or fines and reputational damage	All		

Risk Ref	Level 1 Risk	Level 2 Risk	Risk name	Risk Description	Entity	Current Risk	Previous Risk Rating
21	Strategy	Strategic	Strategic Goals	Strategic goals are unclearly defined and/or inconsistently implemented	All	↑	
18	Strategy	Climate	Climate change & Responsible Investing	LPF don't adequately address Environmental, Social and Corporate Governance factors within the company, with service providers, and through underlying investments, due to lack of climate or sustainability strategy. This could lead to missed opportunities, regulatory scrutiny, financial loss and reputational or stakeholder damage	All	↔	
9	Business Operations	Business Continuity	Business Interruption	Significant and/or extended business interruption (including third party suppliers) leading to a failure or inability to complete key LPF processes	All	↔	
1	Investment Management	Investment Management	Investment Performance	Investment returns are less than expected due to fall in fair price of securities including equities, bonds, real assets could impact value of the fund and consequently funding levels and liabilities	All	↔	
6	Business Operations	Processing & Execution	Investment operations errors	Material or systemic investment operational errors, in relation to LPFI clients (such as trading errors) could result in operational losses, regulatory breaches or reputational damage	All	↔	
27	Business Operations	Processing & Execution	Operational errors	Material or systemic operational errors, in relation to members, employees or clients (such as pension payment errors) could result in operational losses, regulatory breaches or reputational damage	LPF	↔	
8	Business Operations	Processing & Execution	Investment services delivery	Delivery of LPFI's investment services do not meet client expectations or requirements or regulatory obligations		↔	
5	Scheme	Employer Contributions	Employer failure	Failure of an employer with a deficit, or failure to pay required contributions, or failure to fulfil a funding agreement on cessation may lead to the balance to be met by higher contributions from remaining employers	LPF	↔	
10	Information Security IT & Data	Technology	IT systems	LPF's IT does not meet operational requirements due to inadequate IT hardware or software leading to material or extended service delivery issues	All	↑	
24	Information Security IT & Data	Data	Data integrity and quality	Data used to fulfil member, employer, client, regulatory or reporting requirements, and trigger actions or inform decision making, comes from multiple sources and systems and may contain errors	All	↔	
23	Scheme	Funding	Unexpected drop in funding	Unexpected drop in funding levels may require higher employer contributions which may be unaffordable to employers	LPF	↔	
22	Scheme	Funding	Meeting liabilities or capital requirements	Insufficient funds and liquid assets to meet liabilities or capital requirements which may arise through contribution payment failure by employers, unexpected employers exits, shortfall in expected investment income, unexpected investment calls and failure or delays of creditors and receivables	All	↔	

Risk Ref	Level 1 Risk	Level 2 Risk	Risk name	Risk Description	Entity	Current Risk	Previous Risk Rating
20	Business Operations	Communication & Digitalisation	Communications	Unclear, misleading or out of date member or client communications compromises the quality of their decision-making, leading to member or client complaints and reputational damage as well as regulatory censure	All	↔	
12	Business Operations	Business Change	Project and change activities	Ability to deliver internal or regulatory change in line with strategic or legal/regulatory expectations could overwhelm business areas through pressure on BAU processes, causing delivery delays or failures, and/or change fatigue and impacting organisational culture	All	↔	
14	Business Operations	Internal Fraud	Fraud by LPF staff or relating to members	Challenges due to general cost of living increases could drive both employees and members to attempt to acquire assets or monies not belonging or due to them	All	↔	
15	Business Operations	Communication & Digitalisation	Member engagement, servicing and reporting	Member engagement, servicing and reporting does not meet LPF's expected standards and corporate values contributing to operating inefficiencies, member dissatisfaction or complaints and reputational damage	LPF	↔	
3	Conduct	Conduct	Unauthorised activity or poor conduct	Unauthorised activity or poor conduct behaviours by employees representing themselves or the firm could fall short of legal and regulatory standards and requirements	All	↔	

This page is intentionally left blank

Document is Restricted

This page is intentionally left blank

by virtue of paragraph(s) 3, 6, 8 of Part 1 of Schedule 7A
of the Local Government(Scotland) Act 1973.

Document is Restricted

This page is intentionally left blank

LOTHIAN PENSION FUND

Wednesday 20 March 2024

DEPUTATION REQUESTS

Subject	**Deputation**
4.1 In relation to: Item 6.7 2024/25 Business Plan and Budget Update	Time To Divest

This page is intentionally left blank