



## **Pensions Committee**

2.00pm, Wednesday, 21 June 2023

### **Statement of Investment Principles**

**Item number 6.5**

#### **1. Recommendations**

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The Pensions Committee (Committee) is requested to:

- 1.1 adopt the revised Statement of Investment Principles.

**David Vallery**

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# Statement of Investment Principles

## 2. Executive Summary

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- 2.1 The report presents the Statement of Investment Principles (SIP) for Lothian Pension Fund and Scottish Homes Pension Fund (The Funds). It was last reviewed by Committee in June 2022.
- 2.2 The investment strategies approved by the Committee in June 2021 are detailed in Appendix A.
- 2.3 There is one material change to the SIP – the removal of the actual portfolio allocations, which were previously contained in Appendix B. These are reported to the Committee in the Annual Investment Update, which is item 6.6 on the agenda.
- 2.4 There are other minor changes to update dates and asset percentages where these have changed, but there are no changes to the principles themselves.
- 2.5 The Joint Investment Strategy Panel (JISP) reviewed and recommended approval of the revised SIP (which is presented with changes in Appendix 1) in June 2023.

## 3. Background

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- 3.1 The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 require administering authorities to prepare, maintain and publish a written Statement of Investment Principles.
- 3.2 The SIP is an important part of the Fund's governance arrangements and provides the framework within which the Committee delegates the implementation of the investment strategy, as defined by the policy (asset class) groups, to officers with advice from the Joint Investment Strategy Panel. Committee retains responsibility for investment strategy.

## 4. Main Report

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- 4.1 The Statement of Investment Principles (SIP) is formally reviewed by Committee annually whether there are changes or not. It takes advice from officers and advisers of the Joint Investment Strategy Panel (JISP). At its meeting in early June 2022, the JISP confirmed its belief that the SIP satisfies Committee's statutory duty and is an accurate reflection of current advice.
- 4.2 The SIP describes the Funds' investment strategies as allocations to various asset categories, or Policy Groups. These asset allocations and the investment

performance of the Funds are reviewed annually and are the subject of a separate paper on the agenda. The investment strategies, presented in Appendix A, have not changed since June 2021.

- 4.3 Appendix B of the SIP that Committee approved in June 2022 presented the changes to investment strategy implementation over the year ending 31 March 2022. It is proposed that Appendix B is removed from the document as it duplicates the table presented in section 4 of the Annual Investment Update, which is deemed a more appropriate place to report on the annual change of investment exposures.

## **5. Financial impact**

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- 5.1 There are no direct financial implications of this report. Investment strategy is covered elsewhere on the agenda.

## **6. Stakeholder/Regulatory Impact**

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- 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 governance, compliance, or regulatory implications as a result of this report.

## **7. Background reading/external references**

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- 7.1 None.

## **8. Appendices**

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Appendix 1 – Statement of Investment Principles including:

- Appendix A – Investment Strategies (21 June 2023)
- Appendix B – UK Stewardship Code 2020 - Principles
- Appendix C – Statement of Compliance with the CIPFA Principles for Investment Decision Making in the Local Governance Pension Scheme



STATEMENT OF  
**INVESTMENT PRINCIPLES**  
JUNE 2023

## INTRODUCTION

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This Statement of Investment Principles (SIP) describes the objectives, policies and principles adopted by the Pensions Committee (Committee) of the City of Edinburgh Council (CEC) in undertaking the investment of fund monies. The SIP also discloses the extent to which the Funds comply with the six “Myners Principles” of investment practice.

The SIP was agreed by the Pensions Committee (Committee) of the City of Edinburgh Council (CEC) on 21 June 2023. CEC is the administering authority for the Lothian Pension Fund and Scottish Homes Pension Fund (the Funds).

The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010, require administering authorities to prepare, maintain and publish a SIP. The SIP must be reviewed from time to time and revised within six months of any material changes in the Policy.

In preparing this statement, the Committee has taken professional advice from the Joint Investment Strategy Panel (JISP), which includes external advisers and members of the internal investment team who are FCA authorised individuals.

## GOVERNANCE

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CEC has delegated responsibility for the supervision of the Funds to the Committee, which comprises five elected members from CEC and two co-opted members representing employer and beneficiary interests. The Committee is supported by a statutory Pensions Board consisting of five Trade Union and five employer representatives, which is responsible for ensuring that the Funds operate in accordance with the applicable laws and regulations. The Committee and Board are supported by an independent professional observer.



The Committee determines investment strategy based on proper advice from CEC’s Executive Director of Resources. The Executive Director of Resources delegates this role to the Head of Finance taking advice from the JISP.

Responsibility for implementing the strategy is also delegated to the Executive Director of Resources who delegates this role to the Head of Finance, taking advice from the JISP. Day to day management of the Fund’s assets is undertaken by internal investment managers, and external investment managers whose activities are governed by Investment Management Agreements and the limits set out in Scheme regulations.

The SIP forms part of a governance framework that includes Statutory Regulations, the Pensions Committee, the Pension Board, the Joint Investment Strategy Panel, the Funds' Advisers and the Funds' Funding Strategy Statement.

## HIGH LEVEL INVESTMENT PRINCIPLES

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The following principles agreed by the Committee are designed to guide the Funds' governance, strategies and alignment with their agents and to support consistency in decision-making over the long term.

### Governance

**Principle 1: Committee believes that their decisions, and those of officers, must give precedence to the fiduciary duty owed to members and employers.**

Fiduciary duty is paramount. The Pensions Committee recognises the potential conflicts of interests inherent in a local authority administering a multi-employer pension fund. The objectives of the administering authority, its officials and officers and those of the pension fund are not necessarily the same. The primary objective is to ensure sufficient funding in the long term so that retirement benefits that employers promise to members under scheme rules can be paid when they fall due. (The legal view on fiduciary duty issued by the Scottish Local Government Pension Scheme Advisory Board is available at <https://lgpsab.scot/fiduciary-duty-guidance/>.)



**Principle 2: Committee believes that the Funds should mitigate risk by ensuring alignment of interests wherever possible.**

Agency costs are high in the financial services industry – agents are often motivated to act in their own best interests rather than those of the principal (the Funds). Alignment of interests and partnering with similarly aligned organisations will help to reduce risk and address the principal-agency problem to the benefit of the Funds and partners. External resources should, therefore, be used where internal resources cannot be justified or obtained, or where an external perspective provides additional skills or insight into investment matters, and where suitable alignment can be established.

**Principle 3: Committee believes that it should work with like-minded partners to benefit from increased scale and greater resilience.**

There are significant economies of scale in the business of managing investments, so working with like-minded partners with similar long-term objectives and liabilities can achieve lower costs and reduce operational risks with increased resilience.

**Principle 4: Committee believes that cost transparency aids decision-making.**

The asymmetric structure of incentives in financial markets (upside participation in success without downside participation in failure) encourages strategies that may benefit agents (external managers and other financial intermediaries) and be detrimental to investor (Fund) returns. Agents often present fees and other charges in a way that obscures rather than illuminates. Full cost transparency should aid decision-making and so benefit Fund returns.

**Principle 5: Committee believes it should focus on policy setting, including high-level strategic asset allocation which defines risk and return objectives, with appropriate governance structure and oversight.**

Implementation of more granular investment decisions (such as the selection/deselection of individual managers and investments) and regular monitoring should be delegated to suitably qualified and experienced individuals with sufficient time and other resources at their disposal. Appropriate delegation, constraints and reporting requirements should be in place. Reporting to Committee should focus on the long-term objectives of the Fund and how delegated decisions have contributed to these.

## Funding

**Principle 6: Given future uncertainties, the funding strategy should be prudent and should reduce risk to employers of another employer defaulting on its pension obligations.**

The Funding Strategy Statement expresses the funding objective, which informs the investment strategy options. The ultimate objective is to ensure long-term solvency so that retirement benefits that employers promise to members under scheme rules can be paid when they fall due, so full funding should be achieved in a prudent manner to ensure that liquid assets are available at the required time. This is important for members, employers and taxpayers as the scheme is ultimately state-backed.



**Principle 7: Committee believes that the Lothian Pension Fund should consider requests for different investment strategies from employers with different objectives.**

Employers have conflicting desires: on the one hand, they'd like to minimise the fluctuations in contributions and on the other hand, they'd like to minimise the overall amount of contributions. Committee believes in allocating employers to different investment strategies reflecting their timescale for participation in the Fund and their covenant. Employers may have different objectives, so they should be given the opportunity to request a bespoke investment strategy. The Fund should consider such requests, taking account of issues such as employer covenant and implementation costs.

## Investments

**Principle 8: Committee believes that the ability of the Funds to pay pension benefits when they fall due is more important than mark-to-market funding levels.**

Committee recognises that there are various ways to measure the value of promised benefits in a defined benefit scheme. Committee believes that where employer circumstances allow, investment strategy should focus on delivering strong (real) returns that grow to cover cashflows over the longer term rather than focusing on protecting the funding level in the short term.

**Principle 9: Committee believes ‘return-seeking’ assets are likely to outperform ‘risk-free’ assets as the investment horizon lengthens, but this is not guaranteed.**

Time horizons matter a great deal. The appropriate horizon for investment risk-taking depends on the duration of the liabilities, the profile of projected cash flows and the deficit recovery and contingency plans for the scheme (the sponsor covenant).

**Principle 10: Committee believes in owning a diversified portfolio of assets so that it is not overly exposed to any particular contingency.**

Asset diversification can reduce risk where assets are not perfectly correlated. Committee recognises that the future is unpredictable and that real returns from investments are uncertain. Fund returns will be determined primarily by the high-level investment strategy allocation to different asset classes and the timing of material changes. Asset allocation balances diversified risks with the expected additional returns for these risks.



**Principle 11: Committee believes that responsible investment should reduce risk and may improve returns, but that mechanistic divestment is inconsistent with the Funds’ fiduciary duty to members and employers.**

The Local Government Pension Scheme (LGPS) was designed with an important social purpose in mind – the provision of retirement income for individuals. The Funds’ fiduciary duty means that the pursuit of financial return is its paramount concern, although it may also take purely non-financial considerations into account provided that doing so would not involve significant risk of financial detriment. Committee believes that the decisions to invest in, or divest from, a particular company should be made by an investment manager based on a holistic analysis of financially material issues, including environmental, climate change, social and governance issues.

**Principle 12: Committee believes it should exercise its ownership rights in a responsible way, constructively engaging with companies to reduce risk.**

The Funds’ interests are better protected from adverse impacts by collaborating with like-minded investors to have greater influence in engaging with companies, government and regulators.



Engagement aims to encourage responsible behaviour by companies in relation to environmental, climate change, social and governance issues.

**Principle 13: Committee believes that monitoring and assessment of investment success should be viewed on a long-term basis.**

No asset mix provides a stream of cash flows that perfectly matches the liability payments of the Funds as they fall due, so monitoring activity is complex. The Funds are long term in nature and the success of a given investment strategy is likely to ebb and flow with changing investment environments in an unpredictable way. Investment monitoring is challenging and should be viewed through a long-term lens.

**Principle 14: Committee believes that peer group comparative analysis needs to be treated with care.**

No two pension funds are identical, so peer group analysis should be undertaken with care as different funds can hold different investment beliefs, objectives and return and risk appetites.

## RESPONSIBLE INVESTMENT

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With liabilities extending decades into the future, it's in the Funds' interests to take their responsibilities as institutional asset owners seriously. To this end, the Funds' approach to responsible investment centres on effective stewardship of all their assets, with a particular focus on good corporate governance to deliver sustainable investor value.

To demonstrate and embrace an open and transparent approach, the Funds became a signatory of the Principles for Responsible Investment (PRI) in 2008. Signatories commit to six principles and, since 2014, to an annual assessment of their responsible investing practices, which is published on the Funds' website. The Funds demonstrate their open and transparent approach to Responsible Investing by publishing a Statement of Responsible Investment Principles (**SRIP**). This document explains how the Funds practise responsible investment asset class by asset class, and how it's committed to limiting the impact of climate change. The SRIP is published as a standalone document. It represents the Funds' position on Responsible Investment, and it forms part of the Pensions Committee's regular review of Stewardship and Engagement activities.



The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting high quality corporate governance and reporting, and Appendix C lists the principles of the FRC's voluntary Stewardship Code 2020. To become a signatory to the Code, organisations must submit a Stewardship Report to the FRC demonstrating how they have applied the Code's principles. The Funds

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

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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.
- **Non-Gilt Debt** instruments are issued by a range of 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).

- **LDI** are gilts, which are debt instruments issued by the UK Government. Typically, these provide interest payments on a regular basis over the life of the loan until capital is repaid at maturity. Some gilts provide interest payments and capital repayment value that is directly linked to price inflation (the Retail Price Index (RPI)). 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 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

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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 strategy protects them from short-term changes in funding level and employer contribution rates. Less than 1% of employers' assets are invested in the MEG Strategy.

- **50/50 Strategy** invests in a portfolio comprising 50% of the Main Strategy and 50% of the MEG Strategy for employers with a ‘medium’ tolerance for investment risk. Less than 1% of employers’ assets are invested in the 50/50 Strategy.
- **Buses Strategy** is a diversified portfolio of assets tailored to suit the risk appetite of the Lothian Buses company. The Lothian Buses Pension Fund merged with Lothian Pension Fund in Q1 2019. It represents 5.5% of Fund assets.

There may also be demand from individual employers for other investment strategies. The Fund will consider such requests, subject to practical implementation of such strategies and, if appropriate, a review of employer contribution rates. It’s not practical for the Fund to offer individual employers full flexibility on asset allocation.

**Scottish Homes Pension Scheme** was fully funded at the most recent actuarial valuation in March 2020. Its investment strategy protects this closed and mature scheme from short-term changes in funding level and increases in contribution rates by investing in UK gilts and cash.

The Funds’ investment strategies are measured against strategy-specific benchmarks by an independent performance measurement specialist, and these are reported to Committee annually with reference to asset market returns as well as liability valuations. The Executive Director of Resources is responsible for monitoring investments and investment activity and he delegates this function to the Head of Finance taking advice from the JISP, which meets at least quarterly.

## STRATEGY IMPLEMENTATION

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The Committee delegates implementation of strategy to the Executive Director of Resources, who delegates the role to the Head of Finance, taking advice from the JISP. The Head of Finance operates within the parameters agreed by the Committee, investing the Funds’ assets in the policy groups within the permitted ranges.

The Head of Finance, advised by the JISP, identifies the combination of investment managers and mandates within the policy groups to deliver the objectives of the Funds. The investment managers and mandates are listed in Appendix A. The Lothian Pension Fund employs both external and internal managers, recognising that there are cost and alignment advantages of an in-house investment team.



To reduce the risk that a Fund doesn't deliver its objective, controls are set around policy group allocations and each manager/mandate. For external managers, these are detailed in formal Investment Management Agreements; and similarly, formal investment objectives and constraints are set for internal mandates. The investment managers are responsible for the selection of individual holdings.

The Funds' investment managers and mandates are measured against mandate-specific benchmarks of risk and return by an independent performance measurement specialist. Performance and mandate implementation is monitored by the JISP on a quarterly basis.

The Funds collaborate with other investors to benefit from increased scale and cost sharing arrangements. The Funds obtained regulatory approval from the Financial Conduct Authority (FCA) to facilitate this element of strategy implementation.

## OTHER INVESTMENT CONSIDERATIONS

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### Realisation of investments

Most of the Funds' investments are in liquid markets and can be expected to be sold relatively quickly if required. A proportion of the Funds' investments (such as property, private equity, private debt and infrastructure) have less or limited liquidity and would therefore take longer to be sold. The overall liquidity of each Fund's assets is considered in the light of potential demands for cash.

### Stock Lending

The Funds lend a proportion of their investments to generate income from share ownership. Stock lending is conducted within parameters prescribed in the regulations. Stock lending doesn't prevent any investments from being sold. Safeguards are in place to reduce risk of financial loss in the event of default. These safeguards include receiving liquid collateral in excess of the value of the loan, an indemnity agreement with the lending agent and regular reviews of the credit-worthiness of potential borrowers.

### Underwriting

Managers are permitted to underwrite and sub-underwrite stock issues subject to the security being deemed attractive on a medium-term view and subject to the application being limited to an amount the manager would wish to hold over the medium term.

### Derivatives

The Committee has approved the use of derivatives, subject to prevailing legislation and control levels outlined in investment manager agreements. A derivative is a security or contract that derives its value from its relationship with another asset. The Funds may make use of contracts for differences and other derivatives either directly or in pooled funds investing in these products for efficient portfolio management or to hedge specific risks. For example, forward currency contracts allow the Funds to reduce risk from currency fluctuations and equity futures allow the Funds to reduce risk during major portfolio rebalances/transitions.

### Safekeeping of Assets

The services of a global custodian are employed to ensure the safekeeping of investments.



## COMPLIANCE

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### Regulations and Investment Limits

The Funds are compliant with the statutory restrictions set out in the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 and the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Amendment Regulations 2016.

The Regulations contain limits on the percentage of a pension fund that may be invested in certain asset types. In accordance with the Regulations, the Committee have agreed the limits applicable to the Funds' investments in partnerships to accommodate the allocation to unlisted investments, including infrastructure, timber, property, equity and debt. The limits agreed by Committee are:



- All contributions to any single partnerships: 5% (statutory maximum of 5%)
- Contributions to all partnerships: 20% (statutory maximum of 30%)

The Committee took proper advice in respect of these limits from the Joint Investment Strategy Panel and from officers. The limits will apply for the period during which the Funds' strategic allocations include investments in partnerships, unless investment considerations require an earlier review. This decision is compliant with the Regulations.

### CIPFA Principles for Investment Decision Making

Regulations require administering authorities to publish the extent to which they comply with guidance issued by Scottish Ministers, which in turn refer to guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Funds' compliance statement is provided in Appendix C.

### Review of SIP

The Committee will review this statement annually or more frequently if appropriate. The Committee will consult with such persons as it considers appropriate and take proper advice when revising the statement.

## APPENDIX A – INVESTMENT STRATEGIES (21 JUNE 2023)

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### Lothian Pension Fund: Main Strategy

Investment Objectives: to generate returns sufficient to pay pensions as they fall due.

#### Investment Strategy:

Policy group	Target weight 2021-2024	Permitted range
Equities	60%	50-70%
Real Assets	20%	10-30%
Non-Gilt Debts	10%	0-20%
LDI (Formerly Gilts)	10%	0-20%
Cash	0%	0-15%
<b>Total</b>	<b>100%</b>	

### 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 2021-2024	Permitted range
Equities	30%	25-35%
Real Assets	10%	5-15%
Non-Gilt Debts	5%	0-10%
LDI (Formerly Gilts)	55%	45-65%
Cash	0%	0-10%
<b>Total</b>	<b>100%</b>	



## Lothian Pension Fund: Buses Strategy

Investment Objective: to generate sufficient returns to pay pensions as they fall due.

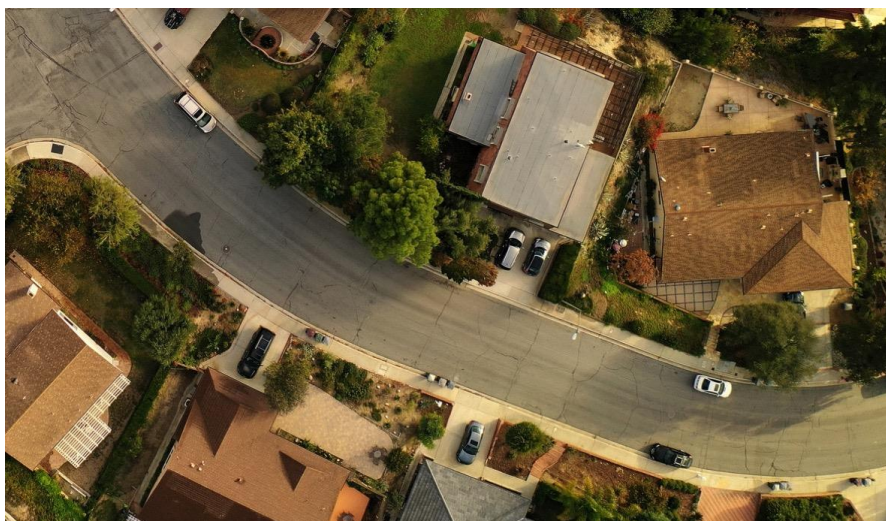
Investment Strategy: to achieve its objective, the Buses Strategy invests in a proportion of the MEG Strategy and the Main Strategy that reflects the maturity of liabilities. This is currently 45:55. Based on the Main Strategy above, the Buses Strategy will have the following exposures.

Policy group	Target weight 2021-2024	Permitted range
Equities	33.0%	28-38%
Real Assets	11.0%	6-16%
Non-Gilt Debt	5.5%	0-11%
LDI (formerly Gilts)	50.5%	40-60%
Cash	0.0%	0-10%
<b>Total</b>	<b>100%</b>	

## 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.

## APPENDIX B – UK STEWARDSHIP CODE 2020 - PRINCIPLES

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The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting transparency and integrity in business. It sets the UK's Corporate Governance and Stewardship Codes. The Stewardship Code 2020 requires signatories to report comprehensively on the following 12 Principles:

- *Principle 1: Signatories' purpose, investment beliefs, strategy, and culture enable stewardship that creates long term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.*
- *Principle 2: Signatories' governance, resources and incentives support stewardship.*
- *Principle 3: Signatories manage conflicts of interest to put the best interests of clients and beneficiaries first.*
- *Principle 4: Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.*
- *Principle 5: Signatories review their policies, assure their processes and assess the effectiveness of their activities.*
- *Principle 6: Signatories take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.*
- *Principle 7: Signatories systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.*
- *Principle 8: Signatories monitor and hold to account managers and/or service providers.*
- *Principle 9: Signatories engage with issuers to maintain or enhance the value of assets.*
- *Principle 10: Signatories, where necessary, participate in collaborative engagement to influence issuers.*
- *Principle 11: Signatories, where necessary, escalate stewardship activities to influence issuers.*
- *Principle 12: Signatories actively exercise their rights and responsibilities.*

## APPENDIX C – CIPFA PRINCIPLES FOR INVESTMENT DECISION MAKING AND DISCLOSURE

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The Chartered Institute of Public Finance and Accountancy (CIPFA) published six Principles for Investment Decision Making and Disclosure in the Local Governance Pension Scheme in the UK in 2012. Details of the principles and the Funds' compliance are described below.

### Principle 1 – Effective decision making

*Administering authorities should ensure that decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to take them effectively and monitor their implementation. Those persons or organisations should have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.*

- The Funds' [Trustee Training Policy](#) (comprising a compulsory training seminar for all new trustees and a requirement to undertake no less than three days (21 hours) of training in each financial year for all Pensions Committee and Pension Board members) provides the knowledge to enable them to evaluate and challenge the advice they receive. Standards relating to the administration of the Committee's business are strictly up-held.
- The Fund has appointed an Independent Professional Observer to strengthen governance. The role of the Observer is to provide the Committee with an impartial, additional source of experience and technical knowledge.
- The Pensions Committee focuses on setting the strategy for the Funds and monitoring performance. The Pension Board also attends Committee meetings and is responsible for assisting the Committee in securing compliance with relevant regulations and other legislation.
- The Committee delegates the day-to-day running of the Funds to the Executive Director of Resources, who in turn delegates to the Funds' officers. The Executive Director of Resources is responsible for the provision of the training plan for Committee to help them to make effective decisions to ensure that they are fully aware of their statutory and fiduciary responsibilities, and to regularly remind them of their stewardship role.
- The Joint Investment Strategy Panel advises the Executive Director of Resources on the implementation of the agreed strategies, reviewing structure, funding monitoring, performance and risk and asset allocation. The Joint Investment Strategy Panel meets at least quarterly and is made up of experienced investment professionals, including independent advisers.



- The in-house team undertakes day-to-day monitoring of the Funds. The team includes personnel with suitable professional qualifications and experience to provide the necessary skills, knowledge, advice and resources to support the Joint Investment Strategy Panel and the Pensions Committee.
- Conflicts of interest are managed actively. At each Committee meeting, elected members of the Pensions Committee and Pensions Board are asked to highlight conflicts of interest. A Code of Conduct applies to members of the Committee and the Pension Board. The Funds have a Compliance Policy, which ensures conflicts of interest are highlighted and managed appropriately.

## Principle 2 – Clear Objectives

*Overall investment objectives should be set out for the fund that take account of the scheme's liabilities, the potential impact on local council tax payers, the strength of the covenant of the participating employers, and the attitude to risk of both the administering authority and the scheme employers, and these should be clearly communicated to advisers and investment managers.*

- The Statement of Investment Principles and the Funding Strategy Statement define the Funds' primary funding objectives.
- Asset-liability modelling is undertaken with the help of external advisers to aid the understanding of risks and the setting of investment strategy. Each Fund has a scheme-specific investment strategy.
- Employers' attitude to risk is specifically considered in the setting of strategy, and employers can request a bespoke investment strategy.
- Reviews of investment strategy focus on the split between broad asset classes (equities, real assets, non-gilt debt, LDI and cash).
- Investment Management Agreements set clear benchmarks and risk parameters and include the requirement to comply with the Funds' Statement of Investment Principles.
- Appointments of advisers are reviewed regularly. Investment and actuarial advisers are appointed under separate contract. Procurement of advisers is conducted within European Union procurement regulations.
- The setting of the Funding Strategy includes specific consideration of the desire to maintain stability in employer contribution rates.



### Principle 3 – Risk and liabilities

*In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of liabilities. These include the implications for council tax payers; the strength of the covenant of participating authorities; the risk of their default, and longevity risk.*

- The Funds take advice from the scheme’s actuary regarding the nature of its liabilities. Asset-liability modelling is undertaken periodically to aid the setting of investment strategy, and these exercises specifically take account of covenant strength and longevity risk.
- Lothian Pension Fund recognises that employers’ circumstances vary and an alternative investment strategy for their section(s) of the Fund may be deemed suitable. The Fund will consider requests for such alternatives, subject to practical implementation of such strategies and, if appropriate, a review of employer contribution rates. It’s not practical for the Fund to offer individual employers full flexibility on asset allocation.
- The Funding objectives for the Funds are expressed in relation to the solvency and employer contribution rates. The Funds regularly assess the covenants of participating employers.
- The Executive Director of Resources is responsible for ensuring the appropriate controls of the Funds. Controls are subject to internal audit, and results of audits are submitted to the Pensions Audit Sub Committee and/or the Pensions Committee.
- The Funds maintain a risk register, which is reviewed on a quarterly basis.



## Principle 4 – Performance assessment

*Arrangements should be in place for the formal measurement of the performance of the investments, investment managers and advisers. Administering authorities should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.*

- The Funds’ performance and risk analysis is produced by an independent external provider.
- The internal investment team monitors the external investment managers’ performance and risk on a regular basis and reports this to the Joint Investment Strategy Panel. The Joint Investment Strategy Panel assesses the performance and risk of both internal and external investment managers on a regular basis (typically quarterly).
- The Funds’ contracts with its advisers are regularly market tested.
- The Joint Investment Strategy Panel assesses its own performance on a regular basis and reports to Committee on its activities, typically annually.
- Training and attendance of members of the Pensions Committee and the Pensions Board are monitored and reported on a regular basis. The composition of the Committee and Pension Board is reviewed on a regular basis.

## Principle 5 – Responsible ownership

*Administering authorities should adopt, or ensure their investment managers adopt, the Institutional Shareholders’ Committee Statement of Principles on the responsibilities of shareholders and agents.*

*A statement of the authority’s policy on responsible ownership should be included in the Statement of Investment Principles.*

*Administering authorities should report periodically to members on the discharge of such responsibilities.*



- The Funds’ approach to responsible investment is described in the Statement of Investment Principles and the Statement of Responsible Investment, both of which can be found on the Funds’ website.
- The Funds’ policy on responsible ownership is included in the Stewardship Report, which has been assessed by the Financial Reporting Council, which can be found on the Funds’ website. See Appendix C for a list of the Stewardship Code 2020 principles.

- Details of the Funds' voting and engagements are available on the Funds' website. The Funds' annual report and accounts includes a summary of the Funds' approach to responsible investment. A summary of the report and accounts is sent to members. The full report is available on the website and is sent to members on request.

## Principle 6 – Transparency and reporting

*Administering authorities should act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives; and provide regular communication to members in the form they consider most appropriate.*

- Meetings of the Pensions Committee are open to the public. Members of the public are entitled to make a deputation at Committee meetings. Committee papers are available on the City of Edinburgh Council's website. The Pension Board joins the Committee at all meetings.
- The Committee's remit covers wider pension scheme issues, other than the management and investment of funds.
- The Funds' policy statements, including the Communications Strategy, Statement of Investment Principles, Statement of Responsible Investment Principles and Funding Strategy Statement are maintained regularly. Stakeholders are consulted on changes. Documents are available on the Funds' website.
- The Funds produce an Annual Report and Accounts. The full report is available on the website and is sent to members on request. The Funds also produce regular newsletters for members as well as an annual benefit statement. Regular briefings are provided to employers. The Funds' website is updated regularly.

