



Pensions Committee

2.00pm, Wednesday, 27 September 2023

Business Plan and Budget Update

Item number 6.8

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:
 - performance indicators
 - membership and cashflow monitoring; and.
 - Capital injection into LPFI

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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 KPI's are on target at 30th June, with the exception of a number of administration categories that are being actively managed (***discussed in 4.2***).
- 3.4.2 Annual benefit statements were delivered 1 month earlier than statutory deadline and prior year (***4.21-4.23***)
- 3.4.3 Progress continues on process enhancements and provision of data for Actuarial Valuation and accreditations.
- 3.4.4 The quarter to June continued the trend in increasing the asset allocation to Real Assets from Cash (***4.24-4.31***)
- 3.4.5 The Risk Management Framework continues to evolve and the LPFI ICARA was approved by the board on 4th September (***4.34-4.39***)

- 3.4.6 The lease for the new office has been signed with an expected move date in Spring 2024 **(4.43)**
- 3.4.7 Forecasted financial outturn to 31 March 2024 **(section 5)** shows a projected £2,125k saving against original budget. The two main contributors are savings from in-housing the investment management form Harris and the reduction in costs from the pausing of Project Forth.
- 3.4.8 Capital injection into LPFI made by the Fund to ensure on-going compliance with FCA capital requirements **(5.9)**

4. Main Report

- 4.1 Progress of particular note made against LPF's Strategic and Functional plans year to date are detailed below.

Operations

Pension Administration performance indicators

- 4.2 Overall, Pension Administration are marginally below target year to date. A number of factors have contributed to this including -
- Workforce includes a large number of trainees. Trainees require daily support, time out to study towards exams and also require work to be checked by a senior administrator which can result in delays to workflows. Changes have been made to address these issues including the appointment of 2 new coaching roles (from existing headcount) to assist trainees with day to day queries, increasing capacity for checking and creating a dedicated training resource to upskill less experienced staff.
 - Due to secondments and permanent leavers the Fund has lost some experienced colleagues from the operations teams. Active recruitment processes are underway to backfill these gaps. To adapt to these challenges improved workflows have been introduced with a case ownership model introduced, resulting in 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 issues and to ensure work priorities are being met.

Accreditation

- 4.3 The Fund has held the Customer Service Excellence (CSE) standard for a number of 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.
- 4.4 LPF's on-site assessment 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.

- 4.5 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. This year's assessment begins with the provision of supporting evidence in October followed by a site visit in November to validate this evidence. A final review with recommendations is expected by the end of the calendar year.

Customer Experience Team

- 4.6 Through a combination of group events and Customer Journey Mapping the Fund has been reviewing some of its key procedures, with particular focus on death and retirement processes.
- 4.7 As a result of reviewing the experience of bereaved members, improvements and efficiencies have been found within the death procedure, including the option to upload documents securely on our website which links directly to the pension system and the associated member's record.

Digital Enhancements

- 4.8 After a successful trial with Crown Agents Bank (CAB), a new digital process for overseas pensioners to complete their annual existence check was rolled out between October 2022 and March 2023. The new process 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. **91%** of members completed the exercise with **88%** doing so using the digital process.
- 4.9 The Fund is now investigating the possibility of switching its overseas payment services to CAB. This could provide considerable benefit to our members including more favourable exchange rates on payments and greater self-service functionality through the CAB portal.

Actuarial Valuation

- 4.10 Work continues to progress on the triennial valuations for both Scottish Homes Pension Fund and Lothian Pension Fund, with positive feedback from the Actuary on the timeliness and quality of data received. Initial results have been received which indicate the overall funding position for both Funds has improved since the 2020 valuations.
- 4.11 The Fund will now review the results for individual employers and consider the impact of these on employer contribution rates for the next three years, the results of which will be shared with Committee in due course.

Review of Funding Strategy Statement and Employer Performance

- 4.12 Pensions Committee approved a revised Funding Strategy Statement (FSS) in June 2023. As required under the scheme regulations, a consultation exercise was carried out with Fund employers. No responses were received.
- 4.13 The revised FSS amended the salary strain recharging mechanism to provide that a review of each employer's funding position would be carried out in tandem with the annual salary strain exercise. The results of this review will then determine the level of salary strain recharged to the employer.
- 4.14 As this change has retrospective effect (from December 2022), fund officers have engaged the actuary to carry out a review at that date. When the results have been received, officers will review charges levied to employers for the 2022 exercise.
- 4.15 The Fund's employer services team continues to support employers by providing training and guidance on their roles and responsibilities under the regulations. Training has been delivered to five employers, with further training planned and positive feedback has been gained from employers on efforts introduced to simplify processes.
- 4.16 An example of this is the introduction of a simplified process for submitting information for members leaving the fund before retirement, previously advised to Committee in June 2023. This process reduces work for employers and as a result employer performance for submitting early leaver information has improved significantly.

McCloud

- 4.17 McCloud rectification comes into effect from 1 October 2024. We believe we are well placed to implement the requirements.
- 4.18 Employer data collection and cleansing continues to take place using the Altair Insights dashboard tool. Through data testing, records in the pensions system have been identified for corrections before revised McCloud calculations take place. The outputs of these quotations will allow the Fund to check records to ensure the underpin calculation is correct and get a better idea of the level of assistance required to correct errors and check underpins.

Pensions Dashboard

- 4.19 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.

- 4.20 The timeline for this has now been delayed and the government announced this date has been extended until 31 October 2026, a further year later than initially indicated. The parliamentary under-secretary of state for pensions stated “more time is needed to deliver this complex build and for the pensions industry to help facilitate the successful connection of a wide range of different IT systems to the dashboards digital architecture. We await further guidance and detail and continue to improve the quality of the data we hold for all our members.

Annual Benefit Statements

- 4.21 The Fund notified and published 100% of benefit statements to its active and deferred members by 31 July 2023. This was achieved a month earlier than the statutory deadline of 31 August and represents a significant time saving on last year’s completion (24 August 2022).
- 4.22 Significant changes were made to how this exercise was distributed to members, making greater use of the pension systems functionality to send bulk emails instead of using an external product. This also had the added benefit of extra security as emails were generated within the system and not extracted and transferred.
- 4.23 Ahead of benefit statement production, an exercise took place to contact members who up until now had requested a paper copy of their statement and gauge interest in moving to e-communications. This exercise was extremely successful with the number of paper statements dropping from 1,354 in 2022 to 502 in 2023. Newsletter printing was also kept in house using Royal Mail’s Print and Post functionality creating a saving on print costs of over £2.5k.

Investments

Asset Allocation

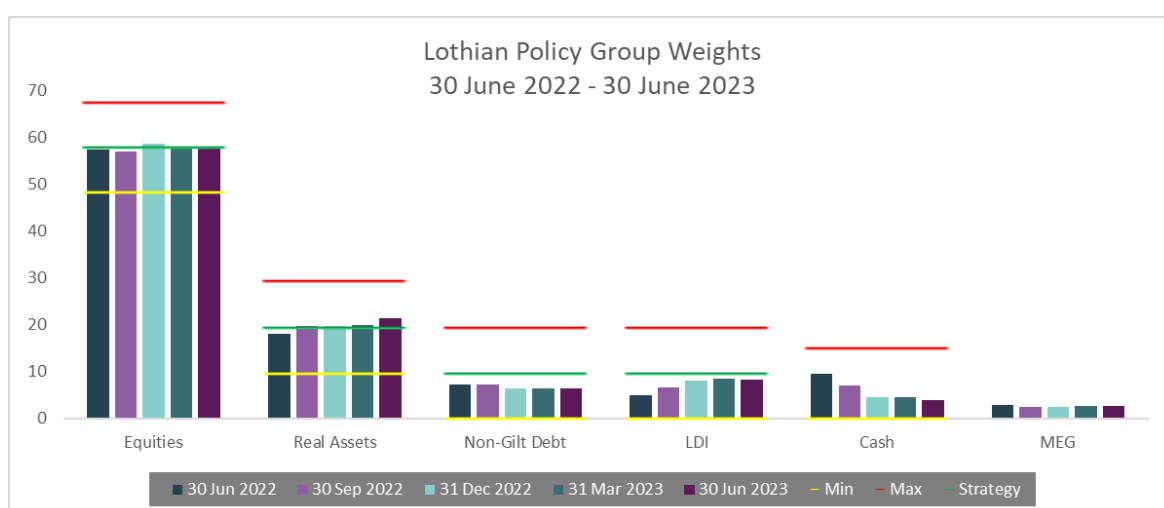
- 4.24 The assets under management by the Fund at 30 June 2023 are as follows –

31 March 2023 £'000	Lothian Pension Fund – Policy Groups	30 June 2023 £'000
5,595,028	Equities	5,476,284
1,922,199	Real Assets	2,037,823
605,179	Non Gilt Debt	599,634
807,288	LDI (Gilts)	793,926
262,748	MEG (Mature Employer Gilts)	243,236
448,097	Cash	364,898
9,640,539	Total	9,515,801

- 4.25 The LPF total fund return was -1.4% in Q2, broadly in line with the Fund benchmark of -1.5%. The slightly negative return was characterised by a largely flat return from both Equities and Real Assets, brought down by a double-digit

negative return from Liability-driven investments (LDI) and a smaller negative return from Non-Gilt Debt assets. During the quarter, the Fund invested more into Real Assets (infrastructure) and LDI, sourced from reductions in Equities and Cash. Relative to the strategic asset allocation, the Fund (as at 30.6.23) was underweight Equities, Non-Gilt Debt and LDI, and overweight Real Assets and Cash.

- 4.26 The green lines in the bar chart below represents the strategic target for 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 weightings to the five policy groups and MEG over the last few quarters to end June 2023. **All policy groups remain comfortably within the agreed ranges.** (The allocation to MEG is held to fund more mature employer liabilities.) In the event that the policy group weights move outwith those ranges, officers are required to report this to the Pensions Committee and agree what action to take.



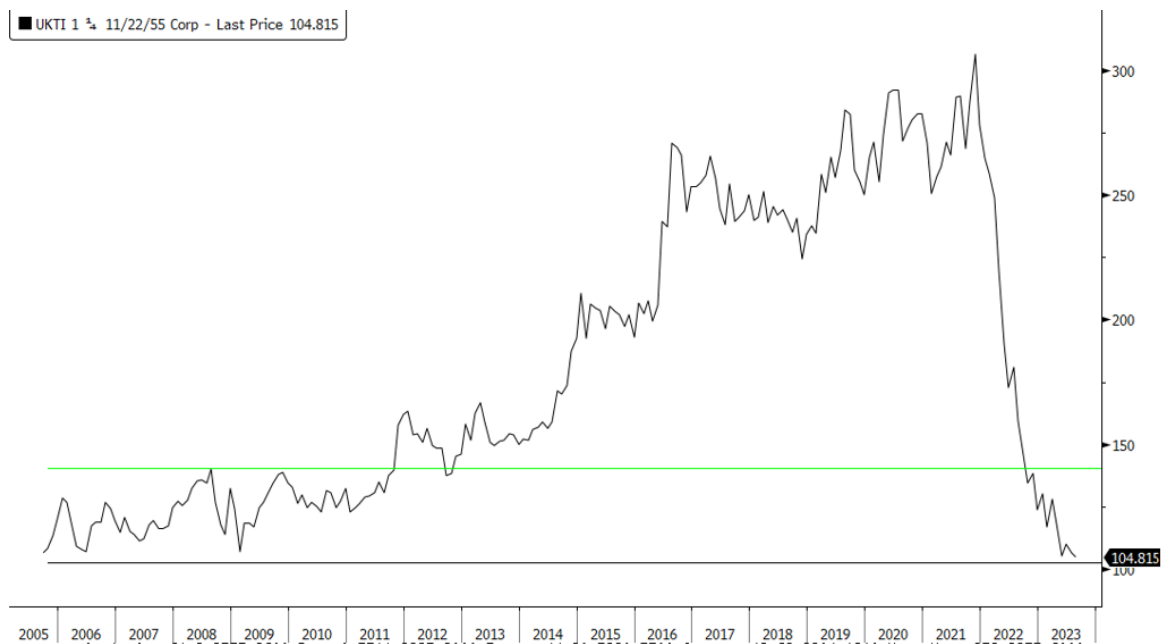
Activity

- 4.27 The main changes to asset allocation over the last several quarters have been the increase in the weight to Real Assets and LDI (index-linked gilts) and the reduction in Cash. Further commitments to Real Assets, all of which have been infrastructure investments, and LDI have been made post the end of the quarter.
- 4.28 Index-linked gilt prices have weakened, and real yields once again approached or breached the levels of autumn last year. Bond price weakness has not been a purely UK phenomenon as the chart below highlights. It displays the US 30-year bond yield (black line) rising from 1.2% to 4.2% over the last 3 years as the US inflation rate (yellow line) spiked to levels not experienced since the early 1980s.



Source: Bloomberg

4.29 The inverse of yields rising is prices falling and the following chart shows the price of the 2055 index-linked gilt. It was issued in 2005 and traded in a band of 102 to 140 for the next 5 years. As quantitative easing (QE) became established and yields fell, the price peaked at over 300. It now trades near 100, and the Fund has increased its weight and reduced its long-standing underweight position.



Source: Bloomberg

4.30 The consequence of rising interest rates is pressure on financial asset valuations in general as future cash flows are discounted at a higher rate. With central banks still in monetary tightening mode to tame inflation, there is a headwind to asset prices.

- 4.31 This has created opportunities in infrastructure, and the Fund has added investments during 2023, mainly in the social, renewables and transport sectors. The source of funds for these investments has been a reduction in the weight in Cash and in Equities. The exuberance around artificial intelligence (AI) seems to ignore the impact that rising interest rates should have on high growth equity valuations.

Investment Strategy Review

- 4.32 Investment strategy is inextricably entwined with the actuarial assessment of the Fund, so in this actuarial valuation year, the officers and advisers have started work to review the existing strategy.
- 4.33 The Fund's investment consultant will share the results of its initial investment modelling exercise with the Pensions Committee in September. This provides a framework for setting investment strategy and will incorporate the experience of the last 3 years, and future expectations for asset and liability values, including consideration of major risks, such as climate change risks. The Committee should be in a position to reaffirm or alter the existing strategy and benchmarks (which were discussed earlier in the year) in late 2023 / early 2024.

Governance, Legal, Risk & Compliance

Risk Management Framework

- 4.34 The plan to improve and embed the risk management framework is progressing well with some key components developed to help operationalise the framework across the business. This includes the development of standard risk language, simplification of risk evaluation methodology, a comprehensive review and refresh of the risk register, introduction of operational functional risk profiles, and improved reporting.

LPFI Internal Capital and Risk Assessment (ICARA)

- 4.35 The ICARA process is being enhanced with increased collaboration between the Risk & Compliance and Finance teams and improved integration with the risk management framework. In addition, business stakeholders have been more actively engaged in the process to ensure more thorough evaluation of plausible scenarios and informed variables has been reflected in the internal assessment of capital. As colleagues continue to evolve the process, further enhancements are expected.

Data Protection, Information Governance and Procurement

- 4.36 The Information Governance framework is being improved with the development and embedding of refreshed policies and procedures. The Risk Management Group's terms of reference have been refreshed, and now include a standing item

on Information Governance metrics. This will allow effective oversight of compliance with key obligations such as: data breaches, subject access requests, data protection assessments, and freedom of information requests.

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- 4.38 The roll out of a new board portal for Pensions Committee, Pensions Board and LPFE/I board meetings has been completed. This will enable meeting papers to be efficiently and securely distributed and meeting attendees to easily access and annotate them before and during meetings.
- 4.39 Incident reporting processes have been improved, with LPF-wide training sessions carried out, to ensure that all colleagues remain aware of the importance of protecting our members data, where data risks may arise, and can identify and manage potential issues.

Finance

Finance General Ledger System

- 4.40 Good progress is being made in the financial systems project. The project will lead to a new single financial system and enable enhanced functionality and processes. Currently Oracle (provided by CEC) is used to record LPF's financial transaction and Xero is used for LPFE/I. As a result of a competitive tender process the Fund awarded a contract to Xledger (subject to an independent assurance review) to provide a finance system for LPF and its 2 companies LPFE and LPFI.
- 4.41 A 2-stage process for implementation was agreed, with the onboarding of LPFE/I took place in September and LPF to be onboarded at a later date, to be agreed with CEC (expected to be H1 2024). Substantial training and testing has already taken place on the system and the lower volumes of transaction in LPFE/I will allow staff to get used to the system, while LPF and CEC agree timescales and resources for the transition of LPF data.

Projects

Project Forth

- 4.42 An update on Project Forth is covered in a separate paper. For 2023/24 financial projection it has been assumed that Forth will remain on hold and associated costs/income have been removed.

Office Relocation

- 4.43 The lease has been signed for the new premises, landlord fit-out work is on-going as is expected to be completed in October, with an expected move date in Spring 2024. Final costings/timing associated with the move are being collated and will be communicated to the Committee in due course.

5. Financial impact

- 5.1 A summary of the projected and year-to-date financial outturn compared to the approved budget for 2023/24 is 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	8,170	(174)	2,086	1,751	(335)
Transport & Premises	577	577	-	144	97	(47)
Supplies & Services	2,768	2,478	(290)	692	567	(125)
Investment Managers Fees -Invoiced	3,850	2,800	(1,050)	962	819	(143)
Other Third-Party Payments	2,583	1,351	(1,232)	646	215	(431)
Central Support Costs	732	732	-	183	228	45
Depreciation	227	227	-	56	46	(10)
Gross Expenditure	19,081	16,335	(2,746)	4,769	3,723	(1,046)
Income	(2,621)	(2,210)	621	(655)	(537)	118
Total Cost to the Funds	16,460	14,335	(2,125)	4,114	3,186	(928)

- 5.2 The financial outturn includes year to date budget, actual expenditure and variance as at the end of June 2023. Year to date actual expenditure includes provision for services incurred but for which no invoice has yet been received.
- 5.3 The projection shows an underspend of approximately £2,125k. The key variances against budget are:
- Investment Managers Fees - Invoiced - £1,050k underspend. In July the Fund terminated the externally managed mandate of Harris bringing the resulting funds into inhouse management. The CIO will review the impact of this on internal resources/staffing headcount which will be quantified in forecasting when known.

- Other Third-Party Payments - £1,232k 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.
- Income – £621k 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.
- Supplies & Services – £290k underspend. Miscellaneous underspends expected for system, legal, and other costs.
- Employees – £174k underspend. Expected to be broadly in line with budget. At 30 June ongoing recruitment process underway for members in Operations team, as well as for a Senior Investment Risk and Compliance Officer (joined August 2023) and replacement Chief Investment Officer (expected start date November 2023).

5.4 Variance to date shows an underspend of £928k. A majority of this relates to Project Forth as per Other Third Party Payment commentary above. The year-to-date underspend on Employee costs is due to ongoing recruitment exercises and variable pay arrangements payable in March.

5.5 As noted in 4.43, the Fund is in the process of finalising the costings for the new premise. The current projections costs are in line with the budgeted assumptions. When finalised these, assumptions will be revised accordingly.

Membership and Cashflow monitoring

5.6 A high level summary of the cashflows from dealing with members as at the end of July 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	88,014	280,000
(282,713)	Benefits Paid	(101,099)	(312,000)
(17,591)	Net Additions/(Deductions) From Dealings with Members	(13,085)	(32,000)

5.7 2023/24 projected cashflow is broadly inline with expectations. With Lothian Pension Funds' 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.

- 5.8 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.

LPFI capitalisation

- 5.9 The LPFI Internal Capital Adequacy and Risk Assessment (ICARA) concluded that, compared to previous years, LPFI needs to hold more capital as a result of the increased AuM and to allow for an appropriate buffer to ensure on-going compliance with the FCA prudential capital requirements. The LPFI board approved the allotment of 1m shares at the board meeting in September. LPF will be required to finance the additional £1m of share capital for LPFI taking the total share capital to £1,690k.

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

Appendix 1 – Business Plan Performance Indicators













Business Plan Performance Indicators

Pensions Committee

27 September 2023

Key Performance Metrics – Targets & Actual Performance 2023/24

	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% (Year to date 93.9%)			90%	
>92% of critical pensions administration work completed within standards	87.92% (Year to date 87.92%)			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	
The Fund operates within the approved budget	Within (Year to date Within)			Within	
The audit of the Annual Report is 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 (Year to date Pass)			Pass	
Publish ENGAGE, Revised SIP and SRIP	Pass (Year to date Pass)			Pass	
Mandatory LMS training completion rate >90%	100% (Year to date 100%)			90%	
The Employee Engagement index KPI of 70% or above	79% (Year to date 79%)			70%	
Less than 10% unplanned employee turnover	9.18% (Year to date 9.18%)			10%	

Service Performance Indicators – Targets & Actual Performance 2023/24

	Q1 April to June	Q2 July to Sept	Q3 Oct to Dec	Target	Status
Monthly Pension Payroll paid on time (Service1)	100% (Year to date 100%)			100%	✓
Acknowledge the death of a member to next of kin within 5 working days. (Service2)	98.01% (Year to date 97.1%)			96%	✓
Percentage of employer contributions paid within 19 days of month end (Service3)	99.9% (Year to date 99.9%)			99%	✓
Estimate requested by employer of retirement benefits within 10 working days. (Service4)	100% (Year to date 100%)			91%	✓
Notification of dependant benefits within 5 working days of receiving all necessary paperwork. (Service5)	95.6% (Year to date 96.6%)			96%	✓
Notify early leavers entitled to deferred benefits of their rights and options within 10 days of being informed of end of pensionable service. (Service6)	97.7% (Year to date 97.1%)			91%	✓
Notify members holding more than 3 months, but less than 2 year service, of their options at leaving. Target is within 10 days of the end of the one month and a day lying period or after the employer providing full leaving information if later.(Service7)	97.4% (Year to date 96.3%)			85%	✓
Pay a refund of contributions within 7 working days of receiving the completed declaration and bank detail form. (Service8)	97.0% (Year to date 98.3%)			91%	✓
Pay any lump sum death grant within 7 working days of receipt of the appropriate documentation. (Service9)	100% (Year to date 100%)			96%	✓
Pay lump sum retirement grant within 7 working days of receiving all the information we need from the member. (Service10)	98.2% (Year to date 98.4%)			96%	✓
Payment of CETV within 20 working days of receiving all completed transfer out forms. (Service11)	94.4% (Year to date 97.2%)			96%	✓
Pension Admin Workflow - Non Key Procedures Performance. (Service12)	75.4% (Year to date 77.0%)			75%	✓

	Q1 April to June	Q2 July to Sept	Q3 Oct to Dec	Target	Status
Proportion Of Members Receiving A Benefit Statement By 31st August (Service13)	100%			100%	✓
Provide a maximum of one guaranteed Cash Equivalent Transfer Value (CETV) within 10 working days of receiving a request. (Service14)	99.6% (Year to date 99.8%)			91%	✓
Provide new members with scheme information within 20 working days of getting details from employer (Service15)	99.7% (Year to date 97.6%)			96%	✓
Provide transfer-in quote within 10 working days of receiving the Cash Equivalent Transfer Value (CETV) from member's previous pension provider. (Service16)	100% (Year to date 97.4%)			96%	✓
Respond In Writing Within 20 Working Days To Formal Complaints That Have Escalated From Frontline Resolution, Or Recorded Directly As An Investigation (Service17)	100% (Year to date 100%)			100%	✓
Level of sickness absence (Service18)	2.1% (Year to date 2.6%)			4%	✓
A minimum of twenty hours training for all staff for the year (Service19)	80% (Year to date 72%)			100%	⚠