Pensions Committee

2.00pm, Wednesday, 25 September 2019

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

Item number	**5.3**
Executive/routine	
Wards	**All**
Council Commitments	

1. Recommendations

The Pensions Committee is requested to:

1.1 invite the Pension Board to raise any relevant matters or concerns which the Committee should consider;

1.2 note the report by Scott-Moncrieff "Lothian Pension Funds 2018/19 Annual Audit Report to Members and the Controller of Audit" (at Appendix 1);

1.3 note the audited Annual Report for the year ended 31 March 2019 for the Lothian Pension Fund and the Scottish Homes Pension Fund (at Appendix 2); and

1.4 note that the audited financial statements, for the year ended 31 March 2019, of both the wholly-owned companies, LPFE Limited and LPFI Limited, were approved by the respective Board of Directors in May 2019. These statements are shown in full at Appendices 3 and 4.

Stephen S. Moir

Executive Director of Resources

Contact: John Burns, Chief Finance Officer, Lothian Pension Fund

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

EDINBVRGH
THE CITY OF EDINBURGH COUNCIL

Report

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

2. Executive Summary

2.1 The unaudited Annual Report for the year ended 31 March 2019 for the Lothian Pension Fund and Scottish Homes Pension Fund has now been considered by the external auditor, Scott-Moncrieff.

2.2 International Standard on Auditing (ISA) 260 requires the external auditor to communicate its findings to those charged with governance of the Funds. Accordingly, the Scott-Moncrieff "Lothian Pension Funds 2018/19 Annual Audit Report to Members and the Controller of Audit" is included at Appendix 1.

2.3 Scott-Moncrieff has provided "an unqualified opinion on the financial statements and other prescribed matters for Lothian Pension Fund and Scottish Homes Pension Fund within our independent auditor's report" and has also stated "that there were no matters which we were required to report by exception".

3. Background

ISA 260 annual report by External Auditor

3.1 Under statutory accounting guidance issued by the Scottish Government, Administering Authorities are required to issue a separate Annual Report covering the Local Government Pension Scheme (LGPS) funds that they are responsible for. These Annual Reports are subject to a separate external audit.

3.2 International Standard on Auditing (UK and Ireland) 260 (ISA 260) requires the External Auditor to communicate its findings to those charged with governance of the Funds. This summarises any matters arising from the audit of the financial statements prior to the formal signing of the independent auditor's report.

3.3 As part of the standard, the External Auditor is required to provide its view of the following:

3.3.1 Any significant qualitative aspects within the Funds' accounting practice;

3.3.2 Any significant difficulties encountered during the audit;

3.3.3 Any material weakness in the design, implementation or operating effectiveness of the system of internal control;

3.3.4 Any significant matters arising from the audit discussed with management;
3.3.5 Any representations that have been requested from management; and
3.3.6 Any other matter that is significant.

3.4 City of Edinburgh Council noted the Unaudited Annual Report 2019 for the Lothian Pension Fund and Scottish Homes Pension Fund at its meeting on 28 June 2019.

4. Main report

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

4.1 The report by the external auditor on the financial statements is included at Appendix 1 – "Scott-Moncrieff - Lothian Pension Funds 2018/19 Annual Audit Report to Members and the Controller of Audit. This will be presented to Committee by Nick Bennett, Partner, Scott-Moncrieff.

4.2 Scott-Moncrieff has stated that its "work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK and Ireland) and Ethical Standards".

4.3 Scott-Moncrieff has provided "an unqualified opinion on the financial statements and other prescribed matters for Lothian Pension Fund and Scottish Homes Pension Fund (collectively referred to as "the Funds") within our independent auditor's report" and has also stated "that there were no matters which we were required to report by exception".

4.4 The external auditor has commented that "We are pleased to report that our audit identified no material adjustments. In addition, we can confirm that there were no unadjusted errors relating to the 2018/19 financial statements. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual report and financial statements. The most significant disclosure change related to the present value of promised retirement benefits."

4.5 After the Supreme Court denied the Government leave to appeal the McCloud and other associated cases on 27 June 2019, a written ministerial statement confirmed that as 'transitional protection' had been offered to members of all the main public service pension schemes, the difference in treatment would need to be remedied across all those schemes, including the Local Government Pension Scheme (LGPS). As the remedy will involve 'levelling up' member benefits, any future agreed outcome will serve to increase the cost of LGPS pensions.

4.6 Prior to the Supreme Court's determination, a contingent liability had been disclosed by Lothian Pension Fund in its unaudited financial statements 2018/19 (note 32).

4.7 The actuary has now carried out an assessment of the impact of the McCloud judgement on the Lothian Pension Fund. The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting

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

4.8 A revised IAS19 statement for LPFE Limited to incorporate the potential implications of the McCloud judgement was also sought. The actuary has estimated an increase of £255k to LPFE's defined benefit obligation. Whilst this has been declared by supplementary note, the group financial accounts have not been adjusted so as to remain consistent with LPFE Limited's audited financial statements.

4.9 For the Scottish Homes Pension Fund, the actuary has stated that the McCloud judgement has no impact because this Fund has no active employees.

4.10 Appendix 1 ("Appendix 1: Management action plan", Pages 40 to 46 of that report) "details the control weaknesses and opportunities for improvement that we (Scott-Moncrieff) have identified during our audit". Planned management actions by Lothian Pension Fund staff in relation to the points raised by the external auditor are also stated.

4.11 In addition to members of the Pensions Committee and Pensions Audit Sub-Committee, Scott-Moncrieff has also sent the report to the Controller of Audit and has advised that it will be published on the Audit Scotland web-site in due course.

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

4.12 With the completion of the work by Scott-Moncrieff, the Audited Annual Report 2019 for the Lothian Pension Fund and Scottish Homes Pension Fund has been finalised and is included at Appendix 2.

4.13 As part of the completion of the audit, the auditor seeks written assurances from the Chief Finance Officer, Lothian Pension Fund, on aspects of the financial statements and judgements and estimates made. A draft letter of representation under ISA580 is attached at Appendix 5.

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

4.14 The consolidated financial statements (within the Annual Report 2019) combine those of the Fund (the parent entity) and its controlled entities (the investment staffing company, LPFE Limited, and the investment services company, LPFI Limited), as defined in International Accounting Standard (IAS) 27. As reported to Pensions Committee in June 2019, the financial statements of both companies have been audited by Scott-Moncrieff and were approved by the respective Boards of Directors in May 2019. In the interests of governance transparency, these statements are shown in full at Appendices 3 and 4.

4.15 LPFE Limited is the employment vehicle for the Fund's staff. It provides staffing services to the City of Edinburgh Council, LPFI Limited and to Falkirk Council. The company's financial objective is "to make a modest trading surplus before adjustments required under International Financial Reporting Standards (IFRS)". Such adjustments primarily relate to pension costs, as required by International Accounting Standard (IAS) 19, and the related deferred tax. For the year ended 31

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

4.16 LPFI Limited provides Financial Conduct Authority (FCA) regulated investment services, both to Lothian Pension Fund and other pension funds, but does not employ any staff directly. Its financial objective is "to make a modest trading surplus". For the year ended 31 March 2019, the underlying trading profit of the company was £59,396 (2018: £34,619).

4.17 A separate report on the two companies on this agenda provides a more detailed progress update.

5. Next Steps

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

6. Financial impact

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

7. Stakeholder/Community Impact

7.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the pension funds and they are invited to comment on the relevant matters at Committee meetings.

7.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report. The forward planning of the Committees' agendas should facilitate improved risk management and governance for the pension funds.

7.3 There are no adverse sustainability impacts arising from this report.

8. Background reading/external references

8.1 None.

9. Appendices

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

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

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

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

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

Scott-Moncrieff
business advisers and accountants

Appendix 1

Lothian Pension Fund and Scottish Homes Pension Fund

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

August 2019

Table of contents

1. Key messages

Annual accounts audit

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

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

Wider scope audit

Financial sustainability

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

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

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

Financial management

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

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

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

Governance and transparency

Governance arrangements at the Funds are deemed to be appropriate.

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

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

Value for money

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

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

Conclusion

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

Scott-Moncrieff
August 2019

2. Introduction

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

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

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

Introduction

1. This report summarises the findings from our 2018/19 audit of Lothian Pension Funds (the Funds).

2. We outlined the scope of our audit in our External Audit Plan, which we presented to the Pensions Committee at the outset of our audit. The core elements of our work include:

- an audit of the 2018/19 annual report and accounts and related matters;
- a review of the Funds' arrangements for governance and transparency, financial management, financial sustainability and value for money; and
- any other work requested by Audit Scotland.

Exhibit 1: Audit dimensions within the Code of Audit Practice

3. The Funds are responsible for preparing an annual report and accounts which show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the annual report and accounts or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

4. The report contains an action plan with specific recommendations, responsible officers and dates for implementation. Senior management should assess these recommendations and consider their wider implications before deciding on appropriate actions. We give each recommendation a grading to help the Funds assess their significance and prioritise the actions required.

5. We discussed and agreed the content of this report with the Chief Finance Officer. We would like to thank all management and staff for their co-operation and assistance during our audit.

Confirmation of independence

6. International Standards on Auditing in the UK (ISAs (UK)) require us to communicate on a timely basis all facts and matters that may have a bearing on our independence.

7. We confirm that we have complied with the Financial Reporting Council's (FRC) Revised Ethical Standard (June 2016). In our professional judgement, the audit process is independent and our objectivity has not been compromised in any way.

8. We set out in Appendix 1 our assessment and confirmation of independence.

Adding value through the audit

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

Feedback

10. Any comments you may have on the service we provide, the quality of our work and our reports would be greatly appreciated at any time. Comments can be reported directly to the audit team or through our online survey: www.surveymonkey.co.uk/r/S2SPZBX

11. While this report is addressed to the Funds and the Controller of Audit, it will be published on Audit Scotland's website www.audit-scotland.gov.uk

3. Annual report and accounts

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

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

Annual report and accounts

An unqualified audit opinion on the annual report and accounts

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

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

Overall conclusion

An unqualified audit opinion on the annual report and accounts

12. The annual report and accounts for the year ended 31 March 2019 are due to be considered by the Pensions Committee on 25 September 2019. We intend to report within our independent auditor's report:
    - an unqualified opinion on the financial statements; and
    - an unqualified opinion on other prescribed matters.

13. We are also satisfied that there are no matters which we are required to report by exception.

Good administrative processes were in place

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

Our assessment of risks of material misstatement

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

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

1. Management override

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

Excerpt from the 2018/19 External Audit Plan

16. We have not identified any indication of management override in the year. We have reviewed the Funds' accounting records and obtained evidence to ensure that transactions outside normal processes were valid and accounted for correctly. We have also reviewed management estimates and the journal entries processed in the period and around the year end. We did not identify any areas of bias in key judgements made by management and judgements were consistent with prior years.

17. While we have not identified any instances of management override from our testing we noted in 2017/18 that City of Edinburgh Council staff, with access to Oracle, have the ability to post journals to the Funds' financial ledger. This is an ongoing issue in 2018/19, however, we did not identify any instances where journals were posted by inappropriate users.

2. Revenue recognition

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

Excerpt from the 2018/19 External Audit Plan

18. While we did not suspect incidences of material fraud and error, we evaluated each type of revenue transaction and documented our conclusions. We have reviewed the controls in place over revenue accounting and found them to be sufficient.

19. We have evaluated key revenue transactions and streams to gain assurance over the completeness and occurrence of income. We are satisfied income in fairly stated in the financial statements. We also carried out testing to confirm that the Funds' revenue recognition policies are appropriate and have been applied consistently throughout the year.

3. Risk of fraud in the recognition of expenditure

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

Excerpt from the 2018/19 External Audit Plan

20. At the planning stage of our audit cycle, we reported that we did not believe the risk of fraud in expenditure recognition was material to the financial statements and we therefore rebutted this risk. This position has been reviewed throughout this audit and this conclusion has remained appropriate.

21. We conducted our testing based on our approach to low inherent risk areas and we evaluated each type of expenditure transaction and documented our conclusions. We gained reasonable assurance over the completeness and occurrence of expenditure and are satisfied that expenditure is fairly stated in the annual accounts. To inform our conclusion we carried out testing to confirm that the Funds' policy for recognising expenditure is appropriate and has been applied consistently throughout the year.

4. Valuation of investments

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

Excerpt from the 2018/19 External Audit Plan

22. In 2018/19, the value of level 2 and 3 investments rose by 13% to £2.639 billion (2017/18: £2.321 billion) increasing as a proportion of overall investments to 36% (34.7% in 2017/18). Fair values of investments of this nature are provided by fund managers and custodian using various bases selected by the investment manager or custodian. The base of investment values can include reference to similar companies or bid prices.

23. We have considered the valuation basis for a sample of investments and concluded that an appropriate base has been applied in each case. The custodian and investment managers are deemed to be management experts. In line with ISA (UK) 500 we have considered the competence, capability and objectivity of the experts used to inform the valuation. In addition we have reviewed auditor reports on the internal controls at the custodian and at each key investment manager. Our testing did not raise any issues regarding the qualifications of or work provided by the management experts employed by the Funds.

24. For a sample of hard to value investments we reviewed the assumptions and bases of the fair value. We challenged the Funds on the rationale for selecting the bases and assumptions and ensured we were satisfied they were appropriate.

25. The disclosures within the annual report and financial statements are consistent with the information provided by the custodian.

5. Lothian Buses Pension Fund Merger

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

Excerpt from the 2018/19 External Audit Plan

26. Lothian Buses Pension Fund was set up by way of a minute of agreement between Lothian Regional Council and Lothian Region Transport PLC dated 31 March 1987 (the Admission agreement). This agreement outlines that the Authority (Council) wishes to establish a 'further fund' in terms of regulation 3 of the Local Government Superannuation (Funds) (Scotland) Regulations 1986 in addition to the existing fund (i.e. Lothian Pension Fund).

27. Historically, Lothian Pension Fund has elected to present Lothian Pension Fund and Lothian Buses Pension Fund separately in the annual accounts. Following the decision to manage the Lothian Buses Pension Fund as part of the main Lothian Pension Fund in year, it was considered that the accounting policy of reporting the Funds separately in the accounts was no longer appropriate.

28. The accounting policy of reporting Lothian Buses Pension Fund as a separate fund was therefore changed in 2018/19. From 2018/19 Lothian Buses Pension Fund was included in the Lothian Pension Fund accounts. As this is a change in accounting policy, there is a requirement to retrospectively restate the 2017/18 figures in line with accounting standards. Consequently Lothian Pension Fund adjusted the prior year figures for comparative purposes.

29. We have considered the basis for the change in accounting policy and concluded that the judgements made by the Funds' management were appropriate. In addition we have reviewed the restated figures and confirmed that they are appropriate and accurately reflect the transactions which took place in 2017/18.

6. Governance statement

In 2017/18 Internal Audit provided a red[1] rated audit opinion meaning significant enhancements were required to the Funds' control environment.

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

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

Excerpt from the 2018/19 External Audit Plan

30. The internal audit opinion was presented to the June Pensions Committee and provided an amber rating[2]. This opinion was based on the findings from three reports in year and the follow up of prior year recommendations.

31. All internal audit reports issued within 2018/19 gave adequate assurance over the control environment. The amber rating related to overdue 'high risk' items from 2017/18 audit work.

32. The issues in 2017/18 related to IT Business Resilience and disaster recovery, pensions tax and third party suppliers. Internal audit confirmed that three of four high risk items had been appropriately addressed by June 2019. The outstanding item relates to the methodology used by Aquila Heywood in the calculation of pension tax. The Funds are currently engaged with Aquila Heywood to update the methodology.

33. The City of Edinburgh Council has considered the internal audit findings and its Chief Executive and Head of Finance are satisfied that reasonable assurance can be placed upon the adequacy and effectiveness of Funds' systems of internal control.

34. We noted that in the draft accounts the Governance Statement still refers to a red rating which is out of line with the findings of internal audit. We have requested this be updated in the revised accounts.

Our application of materiality

35. The assessment of what is material is a matter of professional judgement and involves considering both the amount and the nature of the misstatement. This means that different materiality levels will be applied to different elements of the financial statements.

36. Our initial assessment of materiality for the financial statements is set out in the table below. On receipt of the 2018/19 draft financial statements, we reassessed materiality as outlined in the table below. We consider that our updated assessment has remained appropriate throughout our audit.

[1] Significant enhancements to the control environment required
[2] Generally acceptable but with enhancements required

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

37. Our assessment of materiality is set with reference to the Funds' net investment assets. We consider this to be one of the principal considerations for the users of the financial statements when assessing the financial performance.

38. As outlined in our External Audit Plan we considered transactions when dealing with members (i.e. contributions and expenditure incurred providing payments to pensioners) to also be of key interest to the users. This is reported in the first section of the Fund Account and contains information about the day to day operation of the Funds.

39. ISA 320 states that in certain circumstances it is appropriate to set a materiality amount for particular classes of transactions for which lesser amounts than the overall materiality could influence the decision of the users of the accounts. We have therefore set a separate materiality for transactions relating to dealings with members, based on the expenditure incurred for providing payments to pensioners.

Performance materiality

40. Performance materiality is the amount set by the auditor for each financial statement area, to reduce to an appropriately low level the probability that collectively any uncorrected and undetected misstatements are less than materiality for the financial statements as a whole.

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

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

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

Group accounts

43. The Funds' annual report includes accounts for Lothian Pension Fund and Scottish Homes Pension Fund.

44. Lothian Pension Fund accounts are prepared on a group basis following the creation of two special purpose vehicles, LPFE Ltd and LPFI Ltd in October 2014. The companies are wholly owned and controlled by the City of Edinburgh Council.

45. We reviewed the consolidation process in 2018/19 and concluded the subsidiary companies had been

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

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

correctly included in the group accounts of Lothian Pension Fund.

Audit differences

46. We are pleased to report that our audit identified no material adjustments. In addition, we can confirm there were no unadjusted errors relating to the 2018/19 financial statements.

47. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual report and financial statements.

48. The most significant disclosure change related to the present value of promised retirement benefits.

49. In 2018/19 there were 2 significant legal cases in relation to pension scheme's which we considered to have a potential financial impact on the Funds' present value of promised retirement benefits:

- **McCloud Judgement:** This case related to an employment tribunal ruling that transitional provisions impacting on a public sector final salary scheme were unlawfully age discriminatory. This was upheld in the Courts in December 2018 although the Government at that stage sought leave to appeal this judgement. The ruling has implications for all public service schemes including the LGPS funds. In June 2019, the Supreme Court has rejected the Government's request for a further appeal.
- **Guaranteed minimum pension (GMP)** was accrued by members of the Local Government Pension Scheme (LGPS) between 6 April 1978 and 5 April 1997. The value of GMP is inherently unequal between males and females for a number or reasons, including a higher retirement age for men and GMP accruing at a faster rate for women. However overall equality of benefits was achieved for public service schemes through the interaction between scheme pensions and the Second State Pension. The introduction of the new Single State Pension in April 2016 disrupted this arrangement and brought uncertainty over the ongoing indexation of GMPs, which could lead to inequalities between men's and women's benefits. As an interim solution to avoid this problem, GMP rules were changed so that the responsibility for ensuring GMPs kept pace with inflation passed in full to pension schemes themselves for members reaching state pension age between 6 April 2016 and 5 April 2021. This new responsibility leads to increased costs for schemes (including the LGPS) and hence scheme employers.

50. We requested the Funds' consider the likely implications for their financial statements and consult with their actuary on whether a revised estimate was required. The advice from the actuary was that the GMP impact was likely to be immaterial and that McCloud may have more significant consequences. This was in line with our understanding of the sector and therefore revised figures were only requested to show the impact of the McCloud judgement. The disclosures in note 23 in the accounts have been updated to show a present value of promised retirement benefits of £9,435 million, an increase of £102 million against the amount disclosed in the draft accounts.

51. Lothian Pension Fund group accounts disclose the actuarial valuation of the pension liability for LPFE Ltd. The actuary provided revised figures taking into consideration the McCloud judgement. The impact on the liability is £0.282 million. Management has considered the movement and elected not to adjust the accounts on the basis of materiality and to reflect that the figures used are from LPFE's audited accounts. Full details of the adjustment are included in appendix 3.

An overview of the scope of our audit

52. The scope of our audit was detailed in our External Audit Plan, which was presented to the Pensions Committee in March 2019. The plan explained that we follow a risk-based approach to audit planning that reflects our overall assessment of the relevant risks that apply to the Funds. This ensures that our audit focuses on the areas of highest risk. Planning is a continuous process and our audit plan is subject to review during the course of the audit to take account of developments that arise.

53. At the planning stage we identified the significant risks that had the greatest effect on our audit. Audit procedures were then designed to mitigate these risks.

54. Our standard audit approach is based on performing a review of the key financial systems in place, substantive tests and detailed analytical procedures. Tailored audit procedures, including those designed to address significant risks, were completed by the audit fieldwork team and the results were reviewed by the audit manager and audit partner. In performing our work we have applied the concept of materiality, which is explained earlier in this report.

Other matters identified during our audit

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

Other information in the annual report and accounts

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

Management Commentary

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

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

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

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

Annual governance statement

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

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

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

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

Governance compliance statement

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

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

Remuneration and staff report

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

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

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

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

Legality

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

The Local Authority Accounts (Scotland) Regulations

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

with respect to regulations 8 to 10[5] as they relate to the annual report and financial statements.

72. In 2018/19 we received an objection to the notice of the public right to inspect. Upon review there was found to be a delay in displaying the hard copy of the public inspection notice which is required to be published prior to 17 June as outlined by the 2014 Regulations. The notice was published in the local newspaper and on the City of Edinburgh Council website by 17 June 2019, however, was not available at Council offices until 26 June 2019.

73. We highlighted issues with regards to the public inspection in 2017/18 and we would recommend the Funds make arrangements to ensure full compliance in 2019/20. We have noted that prior period issues in this area are ongoing in appendix 2.

74. Other than the above issue we concluded that appropriate arrangements are in place to comply with these Regulations.

Banking arrangements

75. It was highlighted during the course of our audit that the Pension Fund had not been operating its bank account in line with the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010. There is a requirement for administering authorities to hold a separate bank account for funds and this should be used to hold pension fund money.

76. The Funds use the Council bank account to ensure that no unfunded payments are taken from a pension fund bank account.

77. In 2018/19 the Funds have requested that "unfunded discretionary payments" be transferred to the Scottish Public Pensions Agency which would mitigate the requirement for the Funds' to use the Council's bank account. However, this had not been agreed by the year end.

78. If the transfer of unfunded discretionary payments is not possible the resolution of this issue would dependent on the procurement of a new ledger system which did not progress in 2018/19.

Qualitative aspects of accounting practices and financial reporting

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

[5] Regulations 8 to 10 relates to the preparation and publication of unaudited accounts, notice of public right to inspect and object to the accounts and consideration and signing of the audited accounts.

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

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

4. Financial sustainability

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

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

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

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

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

Significant audit risk

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

Financial sustainability: Market volatility

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

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

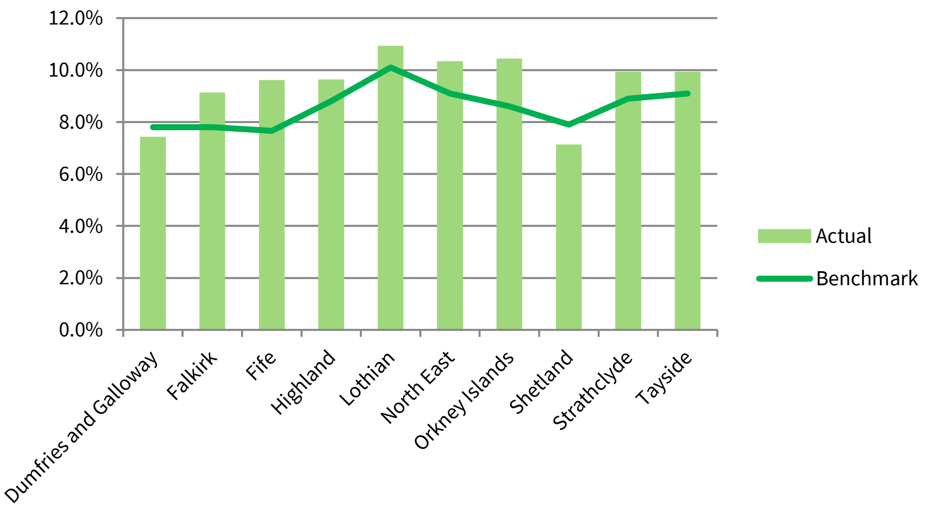
While it is noted that the Funds investment strategy is designed in such a way to withstand market volatility in the long term, we have noted that worldwide political events had a significant impact on the market in 2018 and volatility is expected to continue in 2019. There is a risk that the value of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

Excerpt from the 2018/19 External Audit Plan

80. Financial sustainability of the Funds relates to the performance over the longer term. The investment objective of the Funds is to achieve a return on the fund assets which is sufficient over the long term to meet the funding objectives outlined in the funding statement strategy.

81. When considering the risk over market volatility we have considered the performance over the longer term.

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



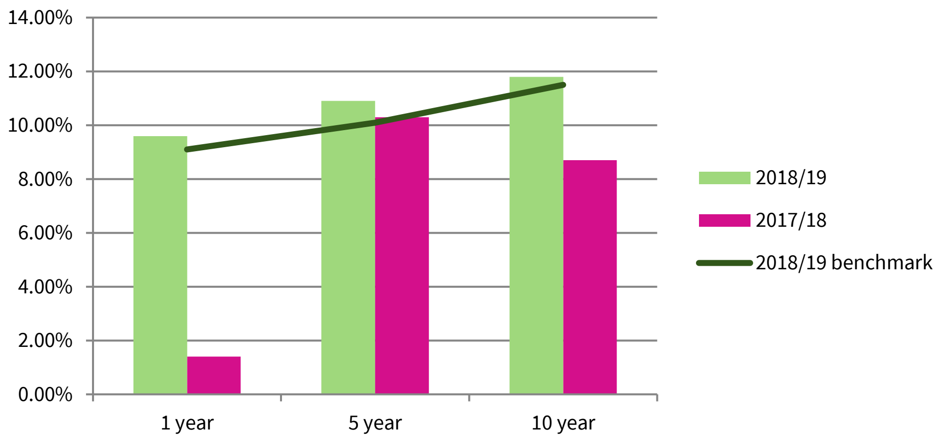
Source: Unaudited Pension Fund Annual Report and Accounts[6]

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

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

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

Exhibit 4: Performance against benchmark and compared to prior year



Source: Unaudited Lothian Pension Fund Annual Report and Accounts

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

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

Employers within the scheme

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

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

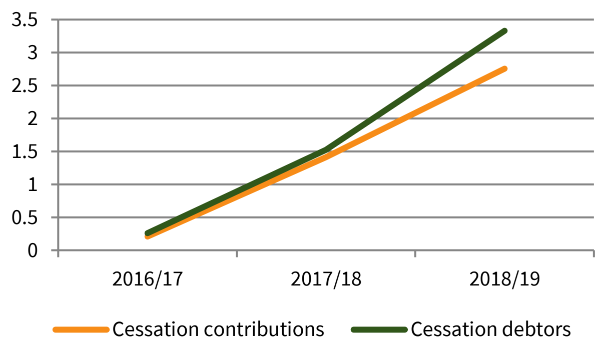
88. In recognition of this Lothian Pension Fund updated their Funding Strategy Statement with a requirement for employing bodies to confirm their commitment to meet the minimum contributions.

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

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

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

Exhibit 5: Cessation contributions and debtors (£m)



Source: Lothian Pension Fund annual accounts

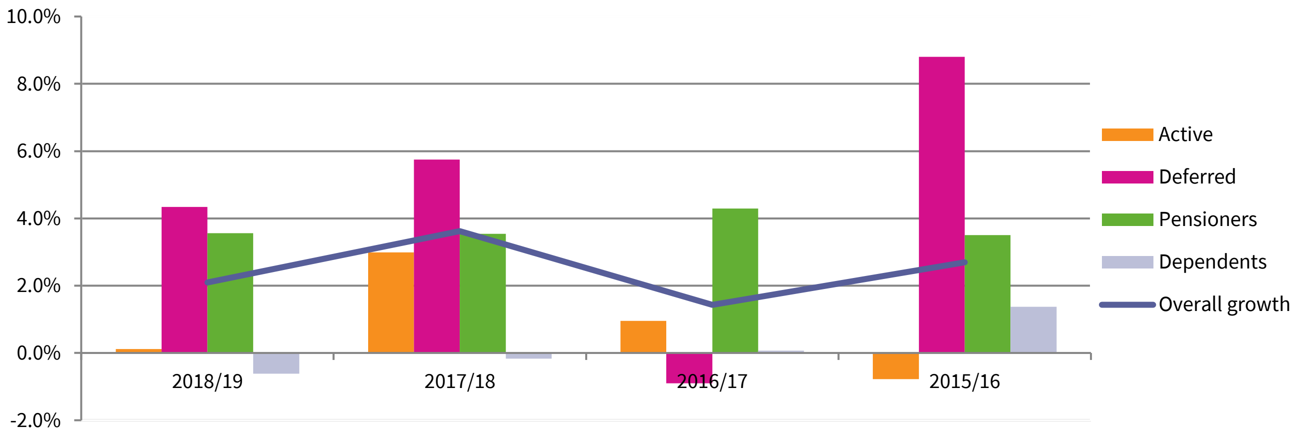
92. There is therefore an ongoing risk that an employer fails to pay contributions leading to increased contributions and pressure on other scheduled and admitted bodies.

Membership

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

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

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



Source: Lothian Pension Funds Annual Report and Accounts

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

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

LGPS Consultation

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

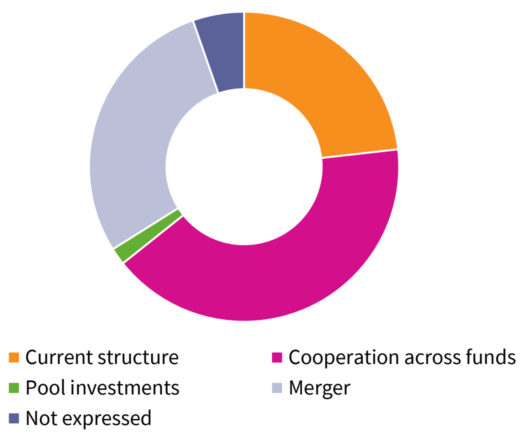
98. In February 2017, SAB produced a review report which highlighted 4 options for the future structure of the local government pension scheme in Scotland:

- Retain the current structure with 11 funds;
- Promote cooperation in investing and administration between the 11 funds;
- Pool investments between the 11 funds; and
- Merge the 11 funds into one or more new funds.

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

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

Exhibit 7: Responses to LGPS Scotland consultation



Source: Scheme Advisory Board

101. Lothian Pension Fund responded in favour of reform, specifically the creation of conditions in which like-minded schemes could seek to merge.

102. The draft report went to the Scheme Advisory Board on 24 April 2019 and further work on how to proceed is scheduled. We will continue to monitor the position in 2019/20.

5. Financial management

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

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

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

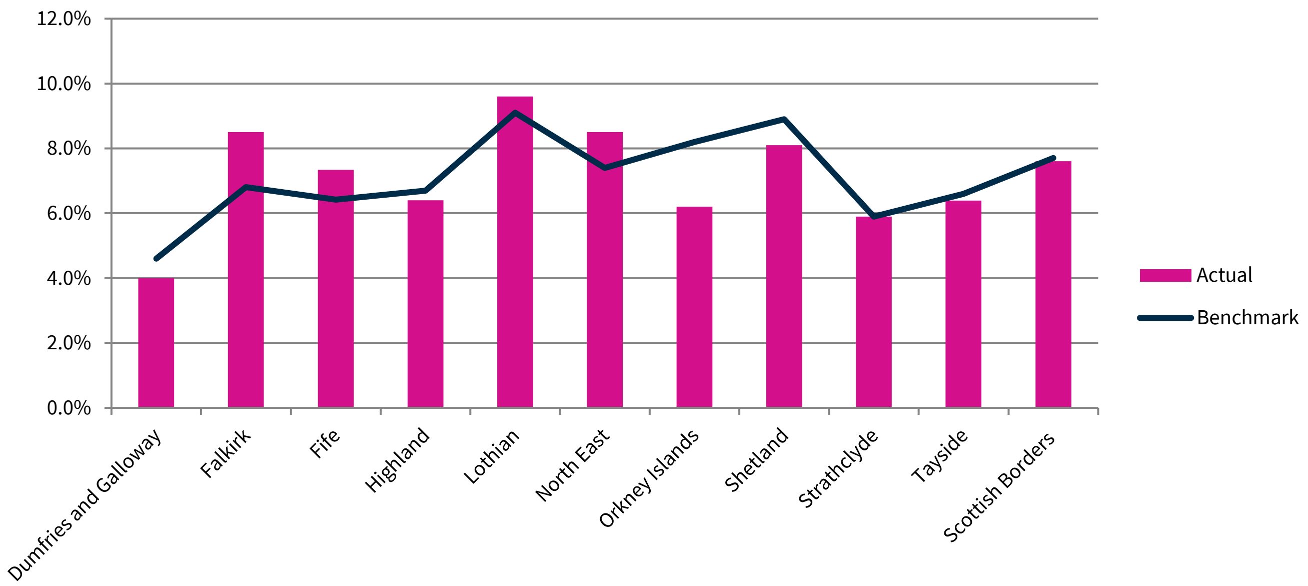
The net assets of Lothian Pension fund have risen in 2018/19 and Scottish Homes Pension Fund assets have not moved. The promised retirement benefits have increased across all three funds.

Investment performance

103. The Funds report their performance with regards to returns on investments as part of the annual report and financial statements. As shown in Exhibit 8 below Lothian Pension Fund, reported performance above the 1 year benchmark. This is an improvement from 2017/18 where performance was significantly behind benchmark.

104. Investment performance across LGPS in Scotland was generally stronger in 2018/19 than in 2017/18. The average return on investments in 2018/19 was 7.1% a small increase from 6.12% in 2017/18.

Exhibit 8: One year investment performance across LGPS Funds



Source: Unaudited LGPS Scotland Annual Report and Accounts

105. In contrast to 2017/18 Lothian Pension fund was above the national average in 2018/19 and was one of only four funds to outperform the benchmark.

106. We have highlighted in the past that the focus of the funds is long term stability and we have noted in the Financial Sustainability section that the longer term performance is also above benchmark.

107. The short and long term results indicate that the investment portfolio is being managed appropriately.

Financial position

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

Exhibit 9: Lothian Pension Funds' Financial Position

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

Source: Lothian Pension Funds Annual Report and Accounts

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

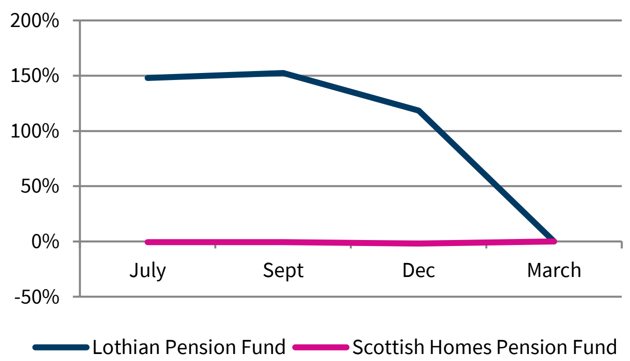
Financial Performance

110. As part of our audit we considered the Funds' systems of budgetary control and financial management and did not identify any significant deficiencies.

111. Service update reports are provided to each meeting of the Pensions Committee. The reports include forecasts to the year-end and explanations for any movements.

112. In year update reports highlighted that a net withdrawals position was expected, however, the forecasts were significantly above the year-end position.

Exhibit 10: Reported movement against the year-end position



Source: Pensions Committee Service Updates

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

Action plan point 1

Systems of internal control

114. We have evaluated the Funds' key financial systems and internal financial controls to determine whether they are adequate to prevent material misstatements in the annual accounts. Our approach has included documenting the key internal financial controls and performing walkthroughs to confirm that they are operating as intended.

115. We identified three areas where there was an opportunity to improve the control environment:

- registers of interest compliance monitoring;
- review of bank reconciliations by a senior member of the finance team; and
- verification of all key details on transfers of individuals from the scheme.

116. Full details of the controls weaknesses and our recommendations are outlined in appendix 2.

Action plan points 2 to 4

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

Prevention and detection of fraud and irregularity

118. Our audit was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity. Lothian Pension Fund was not required to participate in the National Fraud Initiative in 2018/19 but did so voluntarily.

119. We found the Funds' arrangements for the prevention and detection of fraud and other irregularities to be adequate and appropriate.

Standards of conduct

120. In our opinion the Funds' arrangements in relation to standards of conduct and the prevention and detection of bribery and corruption are adequate.

121. Our conclusion has been informed by a review of the arrangements for adopting and reviewing standing orders, financial instructions and scheme of delegation and for complying with national and local codes of conduct.

Internal audit

122. An effective internal audit service is an important element of the Funds' governance arrangements. The City of Edinburgh Council provide the Funds' internal audit service. During our audit we considered the work of internal audit wherever possible to avoid duplication of effort and make the most efficient use of the Funds' audit resource

123. In 2018/19 it was noted that the service did not fully comply with Public Sector Internal Audit Standards in relation to quality assurance reviews. The Pensions Committee were advised that the instances of non-conformance have had no direct impact on the quality of internal audit reviews completed for the Funds in 2018/19.

124. Internal audit has advised that quality assurance reviews will be reinstated with effect from 1 April 2019.

125. In 2018/19 we did not place formal reliance on the work of internal audit, however, we have considered their findings in respect of our wider scope responsibilities and we are grateful to the internal audit team for their assistance during the course of our work.

6. Governance and transparency

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

Governance arrangements at the Funds are deemed to be appropriate.

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

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

Significant audit risk

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

Governance and transparency: Lothian Buses Pension Fund merger

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

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

Excerpt from the 2018/19 External Audit Plan

127. An investment strategy review in 2016 highlighted that Lothian Buses Pension Fund was defined in regulations as a sub-fund of Lothian Pension Fund. It was determined at this stage that there was an option for the Fund to be subsumed into Lothian Pension Fund. It was agreed at the meeting to begin exploring options to proceed with the merger.

128. As noted in the annual report and accounts section of the report, Lothian Buses Pension Fund was established under the Local Government Superannuation (Funds) (Scotland) Regulations 1986 (the 1986 Regulations). Regulation 8 of the 1986 Regulations outlines the process for dissolution of further funds. The administering authority may if they think fit dissolve a further fund and transfer the assets thereof, to the administering fund. Any entitlement to participate in the benefits of the further fund shall become an entitlement to participate in the benefits of the fund and the fund shall become the appropriate superannuation fund for those participants.

129. The administering authority may not dissolve a further fund unless they have given notice of not less than 28 days to the bodies whose employees are entitled to participate in that fund of their intention to dissolve the fund.

130. A transfer agreement ('the Deed of Transfer') was put in place between Lothian Buses and the City of Edinburgh Council in January 2019. This outlines terms and conditions for the transfer of the Fund to within the Main Fund.

131. Subsequent to this Lothian Buses and the City of Edinburgh Council entered into a revised admission agreement which states "The Authority and the Admission Body (together the "Parties") have agreed that the Authority shall transfer all of the assets and liabilities of the Lothian Buses Fund to the Main Fund, so that all benefits payable or prospectively payable under the Lothian Buses Fund will instead be payable under the Main Fund, with future contributions in respect of the Admission Body's participation in the Local Government Pension Scheme being paid into the Main Fund."

132. Following a review by the Funds actuary and legal advisers, it was determined that a guarantee would be required from the shareholders of Lothian Buses (City of Edinburgh Council; West Lothian Council; East Lothian Council and Midlothian Council).

133. We have concluded that Lothian Pension Fund has correctly assessed Lothian Buses Pension Fund as a 'further fund' as defined by the 1986 regulations and that appropriate confirmations from Lothian Buses and the City of Edinburgh Council were in place to allow the transfer to take place. In addition we have confirmed that revised admission

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

Governance structure

134. The Pensions Committee, supported by an Audit Sub-Committee, has been delegated responsibility for governance by the City of Edinburgh Council, the administering authority.

135. As outlined by the City of Edinburgh Council Scheme of Delegation the Pensions Committee has responsibility for the administration, management and investment strategy for the Funds.

136. In line with the requirements of the Public Service Pension Act 2013 the Pensions Committee is supported by a Pensions Board.

137. The Pensions Board is responsible for establishing arrangements that ensure proper conduct of the affairs of the Board and meet quarterly on a concurrent basis with the Pension Committee.

138. The Funds complied with best practice and appointed an independent professional observer to the Board and Committee. The appointed independent observer resigned in February 2018 and a replacement was appointed in May 2018.

139. In line with legislation if more than half of the members of the Pension Board disagree with a decision of the Pension Committee then they can request in writing that the Pension Committee review that decision. There have been no requests to review decisions in 2018/19.

Training and development

140. Due to the specialised nature of the Funds, it is vital that members have the appropriate knowledge and understanding to provide appropriate challenge and operate effectively. Training is therefore seen as a fundamental requirement for all Committee and Board members.

141. Our review found that all current Pension Committee and Board members met the requirement to have a minimum of 21 hours training.

Joint Investment Strategy Panel

142. The Pensions Committee has delegated responsibility for investment strategy to the Executive Director of Resource who takes advice from a Joint Investment Strategy Panel made up of:

- Chief Executive, LPFI Ltd (until December 2018);
- Chief Investment Officer LPFI Ltd;
- Regulated investment advisor, LPFI Ltd (from December 2018); and
- two external independent investment consultants.

143. The joint Investment Strategy Panel covers joint working arrangement with Falkirk Pension Fund and Fife Pension Fund.

144. The Joint Investment Strategy Panel meets quarterly and considers the appropriate investment management structure required to implement the Funds' investment strategy. In addition it is responsible for:

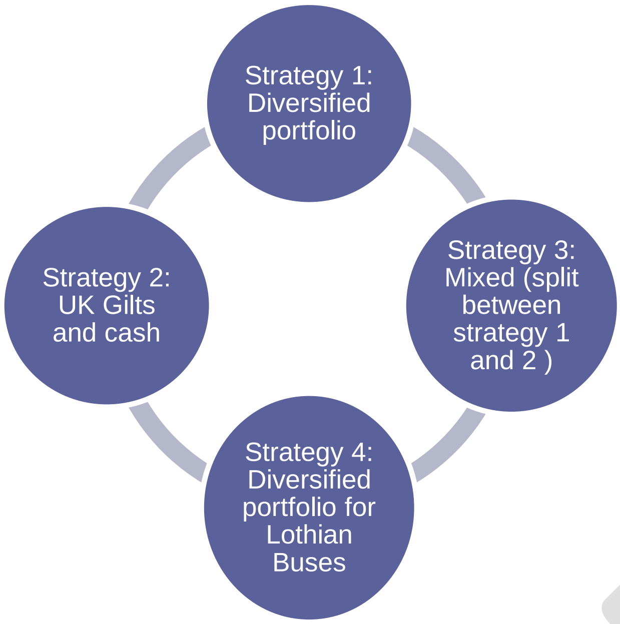
- making recommendations about investment strategy; and
- directing and monitoring strategy implementation and risk.

145. The primary focus of the panel during 2018/19 has been the implementation of existing strategies for Lothian Pension Fund, Lothian Buses Pension Fund (until merger with Lothian Pension Fund in February 2019) and Scottish Homes Pension Fund.

146. In addition to this following the merger of Lothian Buses Pension Fund with Lothian Pension Fund the Panel considered the Investment Strategy for the revised structure.

147. From December 2018, Lothian Pension Fund operated four investment strategies recognising the differing requirements of the various scheduled and admitted employers.

Exhibit 11: Lothian Pension Fund investment strategies



Source: Joint Investment Strategy Panel annual report

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

Openness & Transparency

149. Audit Scotland also cited a risk in relation to public sector organisations keeping pace with public expectations on openness and transparency.

150. In our opinion, the Funds demonstrates good practice with respect to openness and transparency in the following ways:

- Committee agendas and papers are published on the Funds' website in advance of meetings being held;
- Committee minutes and updates are available to the public;
- Key publications (including operational plan, results of annual review, annual accounts) are available on the Funds' website; and
- the quality of reports presented to the Pensions Committee is such that it supports the transparency of decision making.

In September 2018 the Pensions Committee considered a report as to whether their proceedings should be included as part of The council web-casting facility. It was agreed that the benefits arising from the existing format outweighed those that would arise from web-casting.

Impact of EU withdrawal

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

- Workforce;
- Funding; and
- Regulation.

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

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

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

Key supplier dependency

155. Following the collapse of Carillion, it became apparent that public sector bodies face significant risks where suppliers are experiencing difficult trading conditions.

156. We have evaluated the Funds' key suppliers and considered the contract management arrangements as part of our work on expenditure and value for money

157. There are a number of areas where the Funds use one key supplier e.g. custodian, pensions administration and investment managers. However, we are aware appropriate contract management is in place and that there is a range of potential suppliers should a change be necessary. We therefore consider this to be low risk.

158. The Funds ICT environment is through the City of Edinburgh Council and their supplier. In 2018/19 the Funds have encountered delays and service disruptions across a number of ICT areas.

159. The ongoing issues are on the risk register and graded high risk and the Funds attend quarterly meetings with City of Edinburgh Council ICT officers and the supplier.

160. We consider the actions of the Funds with regard to key suppliers to be appropriate and proportionate to the level of risk.

7. Value for money

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

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

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

Investment manager operations

161. Lothian Pension Fund operates two special purpose vehicles: LPFE Ltd and LPFI Ltd. Both companies are wholly owned and controlled by the Council.

162. The special purpose vehicles were established to support the investment programme of the in-house investment team by providing organisational arrangements consistent with the capability, systems and controls of authorised investment companies.

163. Effective leadership is key to the success of the Funds achievement of objectives. In 2018/19 there was a significant change to the leadership team at LPFI Ltd.

164. In June 2018 the Chief Executive announced her intention to leave the Funds with a planned leaving date of December 2018. A new Chief Executive was appointed and commenced his position in January 2019.

165. There has been no significant change to the operation of the Funds to date and the proportion of funds managed internally has remained steady at approximately 85% of investments since 2015/16.

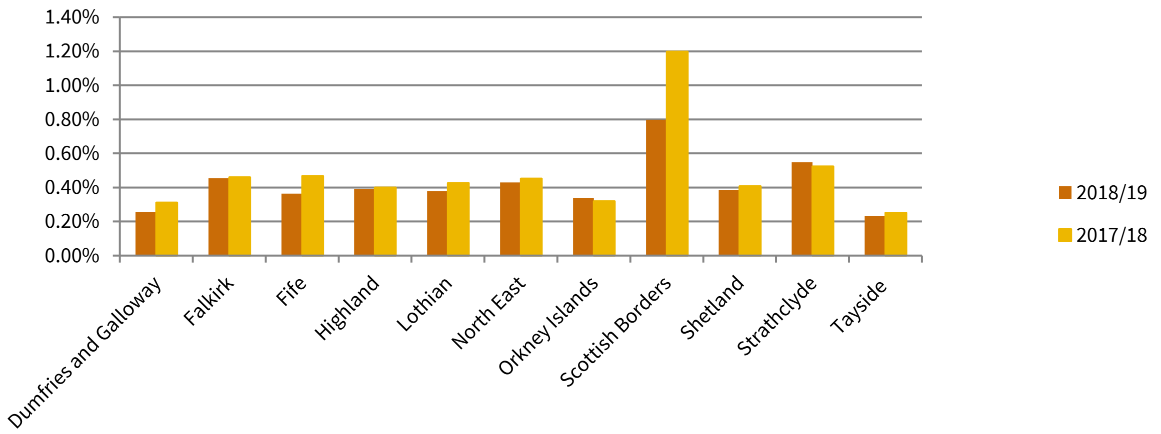
Management expenses

166. Lothian Pension Fund reported management expenses of £38.634 million in 2018/19, an increase of 1.8% from the prior year.

167. Management expenses are split into three main categories: administrative costs; investment manager expenses and oversight and governance costs. Investment management expenses account for 90% of total management expenses.

168. In year Lothian Pension Fund's investment manager expenses (excluding indirect expenses) fell marginally as a proportion of net assets. This is broadly in line with trends across the Local Government Pension Funds.

Exhibit 12: Lothian Pension Funds' Financial Position



Source: LGPS Scotland Unaudited Annual Report and Accounts

169. The analysis above does not include indirect investment management costs as CIPFA guidance states that only direct investment management costs i.e. those that the fund can control should be reported. Lothian Pension Fund reported £5.062 million of indirect manager expenses in 2017/18. It is not possible to benchmark the impact of indirect management costs across Scottish Local Government Pension Funds.

170. Investment manager expenses can vary due to a number of factors including actual returns on investments and the nature of the investments assets held.

171. The Funds undertake annual benchmarking exercises using externally provided data, covering 41 LGPS funds and a wider global universe of 346 funds.

172. Analysis of investment costs is carried out by an independent provider, CEM benchmarking Limited. In 2018/19 Lothian Pension Fund reported an actual investment cost of 0.43% of net assets which was below the benchmark of 0.55%.

173. The Funds credit the improved performance against benchmark to the high percentage of assets managed internally.

174. Analysis of pension administration costs was undertaken by the Chartered Institute of Public Finance Accountants. Pension cost per member was in 2018/19 £23.38, which is higher than the average cost of local authority funds of £21.74. The cost per member is broadly deemed to be in line with other local authority funds who operate within the range of costs of £11 to £61 per member.

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

Monitoring investment performance

176. There is an annual review of investment performance in June for each of the Funds. The report provides a detailed analysis of each of the Fund's investment performance against its investment strategy. We concluded that Pension Committee and Board Members are engaged in monitoring the performance of investments.

177. In addition to monitoring at a Committee level the Funds' performance is calculated by an external provider on a monthly basis. The external provider compiles information covering monthly, quarterly, yearly, 3, 5, 10 since inception yearly performance measures. This information is presented to the Joint Investment Strategy Panel to allow for scrutiny investment performance of the Funds.

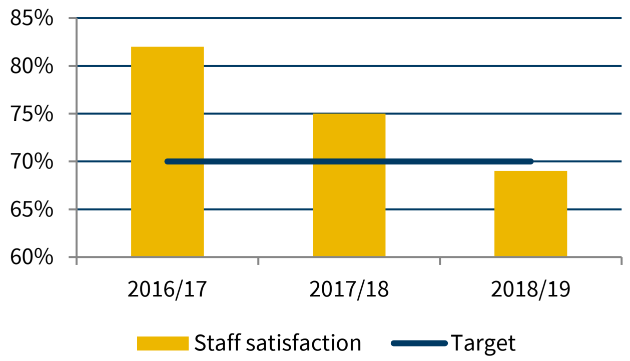
Administrative Performance

178. The Funds' have a Service Plan in place covering the period 2018- 2020. The Pensions Committee receive updates on the service plan at each meeting. The annual results for 2018/19 are presented in the Funds' Management Commentary.

179. The Performance Report highlights that the Funds are meeting the majority of their targets (90%) with only 1 area where performance was not in line with target levels:

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

Exhibit 13: Lothian Pension Funds' Financial Position



Source: Lothian Pension Funds unaudited annual report and accounts

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

Tendering for Services

182. The Funds make use of a range of service providers including investment managers, an actuary and a custodian. In order to ensure the Funds are achieving value for money it is good practice to tender for services at set intervals.

183. The Funds follow the City of Edinburgh Council procurement procedures and maintain a contract register.

184. A paper went to the Pensions Committee in December 2018 providing an update on the tender of custodian services.

185. We have concluded that contract arrangements in place at the Funds are appropriate.

8. Appendices

Appendix 1: Respective responsibilities of the Funds and the Auditor

Responsibility for the preparation of the annual report and accounts

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

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

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

The Chief Finance Officer is also responsible for

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

Auditor responsibilities

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

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

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

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

Wider scope of audit

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

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

Independence

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

Non-audit services

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

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

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

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

Confirmation of independence

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

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

Appendix 2: Action plan

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

Action plan grading structure

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

The rating structure is summarised as follows:

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

Current year action plan

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

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

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

Action plan point	Issue & recommendation	Management comments
4. Verification of pensioner details Rating **Grade 3** Paragraph Ref 117	**Issue** As part of our verification of controls we walked through a transfer out of a member. The sampled record did not have their date of birth confirmed or checked to supporting documentation. **Risk** This is a key control in confirming pension eligibility and could lead to an error in payments made. **Recommendation** We recommend that verification of key details are conducted in line with the stated procedures.	This case is an interfund transfer rather than a transfer to another pension scheme. An interfund transfer means that the member is transferring to the same scheme (LGPS) and the transfer value payment is simply a way of transferring the liability from one Fund to another. There is an agreement between the Scottish Funds that dates of birth do not need to be verified if already verified by one scheme. In this case, however, this did not happen in either fund. The existing documented LPF administration procedure already reflected requisite date of birth verification. In this case, the procedure had not been correctly followed (human error). The importance of the check has been re-iterated to the pensions administration team, both orally and by e-mail communication. **Responsible officer:** Chief Finance Officer, Lothian Pension Fund **Implementation date:** 30 September 2019

Follow up of prior year recommendations

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

1. Publication of the financial statements

Initial rating	Issue & recommendation	Management comments
Grade 2	**Observation** In 2017/18 Lothian Pension Fund received objections to the accounts relating to the public right to inspect the accounts. The objections related to the wording in the public inspection notice and the availability of the annual report and financial statements on the Lothian Pension Fund website. **Recommendation** We recommend that the annual report and financial statements are posted on the Lothian Pension Fund website, following approval from the Pensions Committee and in line with the public inspection notice.	Recommendation is accepted. Following consideration of the Annual Report 2019 (and Financial Statements) Unaudited by Pensions Committee, this will be posted on the Lothian Pension Fund website, supplementing the prior disclosure of all the reports to that Committee on the Council's website. **Responsible officer:** Chief Executive Officer, Lothian Pension Fund **Implementation date:** June 2019
Current status	**Audit Update**	**Management response**
Ongoing	In 2018/19 we received an objection to the notice of the public right to inspect. Upon review there was found to be a delay in publishing the public inspection notice which is required to be published prior to 17 June as outlined by the 2014 Regulations. The notice was published in the local newspaper and on the City of Edinburgh Council website by 17 June 2019, however, was not available at Council offices until 26 June 2019. We recommend procedures are put in place to ensure all the regulations are complied with in 2019/20.	While detailed procedure notes are already in place, these will be reviewed to introduce an element of independent review, thereby ensuring all key steps are undertaken by the required dates.

2. Bank accounts

Initial rating	Issue & recommendation	Management comments
Grade 3	**Observation** The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010. require administering authorities to hold a separate bank account for funds and to be used to hold pension fund money. There is an ongoing issue that although the Funds' held their own bank accounts, monies were transferred to the City of Edinburgh Council holding account and the money was managed through this account. Actions were taken in 2017/18 to progress the issue of compliance, however, significant delays mean that during the year the Funds were not in fully compliant with the regulations. **Recommendation** We recommend the Funds put arrangements in place to ensure compliance with the regulations.	Quotation for a stand-alone ledger for the Funds was also sought from CGI, the Council's ICT provider, but this did not offer a cost-effective solution. Whilst LPF now fully anticipates a successful project delivery by the Council and CGI, with integration of the LPF requirement in the ledger specification, the option of complete separation, i.e. LPF to procure an alternative to the Council solution, is retained as "last resort". **Responsible officer:** Chief Finance Officer, Lothian Pension Fund **Implementation date:** As soon as possible, subject to the implementation of a revised financial ledger system by the Council to incorporate this functionality, or alternatively a separate procurement by LPF.
Current status	**Audit Update**	**Management response**
Ongoing	The resolution of this issue is linked to the procurement of a new ledger system which has not progressed in 2018/19.	LPF has requested that responsibility for "unfunded (discretionary) payments" be transferred to Scottish Public Pensions Agency (SPPA). Should this be accepted by SPPA, then there would be no requirement for LPF to utilise the Council's bank account. The procurement of a new ledger is also linked to LPF's consideration of its broader ICT service requirements.

3. User access controls

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

review user access controls for the financial ledger.

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

4. Cyber essentials

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

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

Appendix 3: Unadjusted audit differences

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

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

Appendix 2

Audited Annual Report and Accounts 2018/19

Lothian Pension Fund
Scottish Homes Pension Fund

Contents

Foreword

Report by the Convener of the Pensions Committee

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

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

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

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

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

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

Councillor Alasdair Rankin
Convener, Pensions Committee

Report by the Convener of the Pensions Audit Sub-Committee

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

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

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

Councillor Cameron Rose
Convener, Audit Sub-Committee

Report by the Chair of the Pension Board

The Pension Board, whilst not a directly decision-making body, holds an important scrutiny function and its role is in ensuring the Fund compliance with the Scheme's rules and other pensions regulations; Including those set out by The Pensions Regulator which relate to the running of the Lothian Pension Fund, thereby ensuring both its effective and efficient governance and administration.

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

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

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

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

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

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

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

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

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

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

Jim Anderson
Union representative and Chair of the Pension Board

Report by the Independent Professional Observer

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

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

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

Andy McKinnell
Independent Professional Observer

Management commentary

OUR MISSION

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

Introduction

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

Change in structure

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

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

As a result, Lothian Buses, like any other sponsoring employer in our Fund, pays only the costs of their members but now shares the benefit of lower administration costs from the merged Fund.

Funding Levels

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

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

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

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

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

Affordability of scheme membership

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

Our people

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

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

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

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

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

Scottish LGPS (SLGPS) consultation

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

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

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

Economic and investment market developments

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

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

Interaction with regulators

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

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

Future developments

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

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

DOUG HERON
Chief Executive Officer
Lothian Pension Fund
26 June 2019

Governance and Risk

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

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

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

The Fund maintains a comprehensive website for easy access to all relevant pension information and this is found at www.lpf.org.uk. This includes the Annual Report & Accounts of the Fund, Statement of Investment Principles, Funding Strategy Statement and Pensions Administration Strategy and Pensions Discretions Policy.

The Pensions Committee and Pensions Audit Sub-Committee

The day-to-day running of the Fund is delegated to a specialist team who undertake pension administration, accounting and investment functions, managing the majority of the Fund's assets internally.

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

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

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

The Pension Board

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

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

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

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

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

Pensions Committee and Pension Board training

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

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

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

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

Joint Investment Strategy Panel

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

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

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

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

Lothian Pension Fund employees

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

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

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

The investment responsibilities include carrying out in-house investment management and the monitoring and selection of external investment managers, as well as external facing collaborative initiatives with other like-minded pension funds.

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

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

And senior officers from Lothian Pension Fund were:

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

Scheme Advisory Board

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

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

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

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

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

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

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

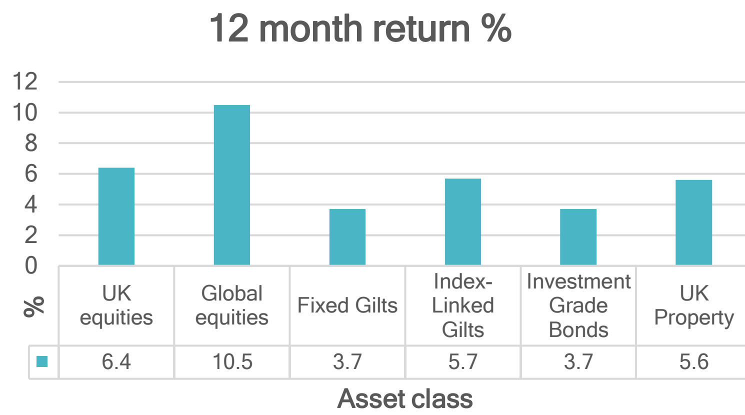
Investment

Investment markets

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

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

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



Index: Bloomberg, MSCI UK Property

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

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

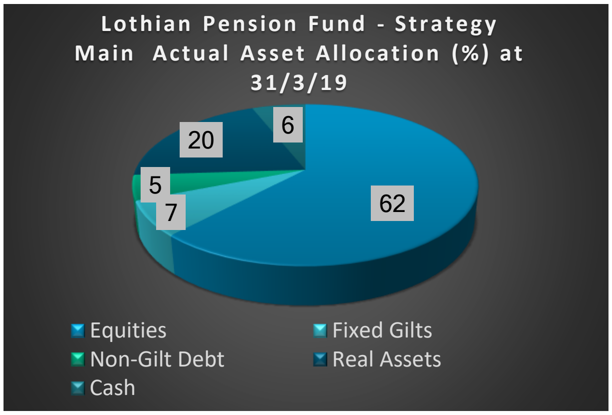
Investment strategies

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

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

Lothian Pension Fund

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

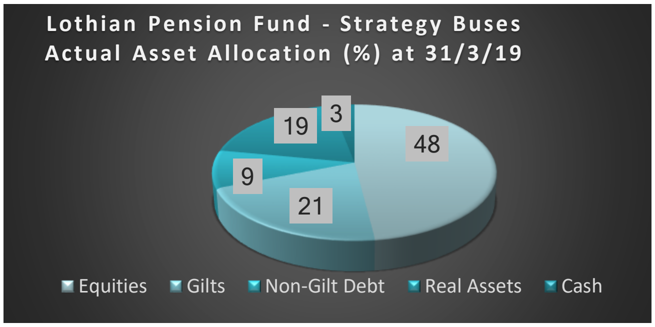


To provide suitable investment strategies for the differing employer requirements, the Fund currently operates four investment strategies. More than 90% of employer liabilities are funded under the Main Strategy, which adopts a long-term investment strategy aiming to maximise the investment return within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

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

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

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

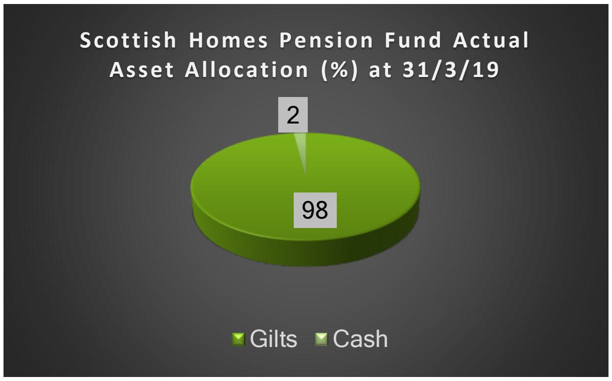


Scottish Homes Pension Fund

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

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

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



Internal investment team

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

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

Responsible Investment

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

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

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

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

PRI Annual Assessment

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

PRI rates Lothian's approach to RI highly

Summary Scorecard

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

Ethics and Lobbyist Activity

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

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

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

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

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

Stewardship Code

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

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

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

Voting

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

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

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

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

Engagement

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

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

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

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

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

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

Collaboration

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

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

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

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

Climate Change

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

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

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

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

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

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

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

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

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

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

Climate Change - Governance

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

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

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

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

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

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

Climate Change - Strategy

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

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

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

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

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

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

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

Climate Change - Risk Management

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

Climate Change - Monitoring and Metrics

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

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

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

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

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

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

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

Infrastructure Investment

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

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

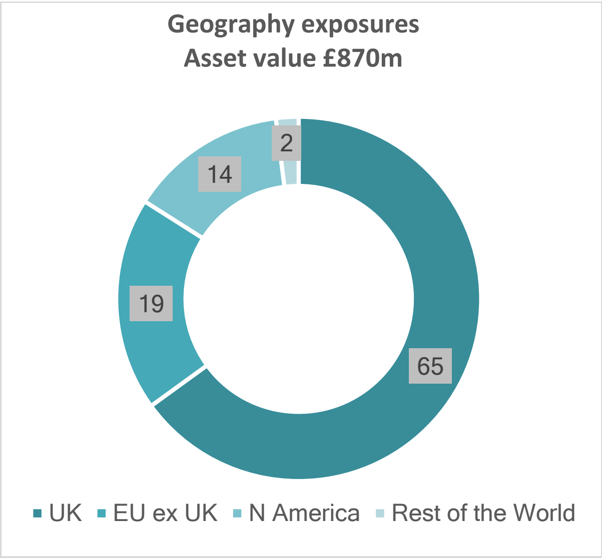
Lothian Pension Fund has a long-standing commitment to responsible investment. In addition to becoming a signatory of the UNPRI (United Nations Principles of Responsible Investment) in 2008, the Fund has subscribed to GRESB (Global Real Estate Sustainability Benchmark) to further enhance our analysis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

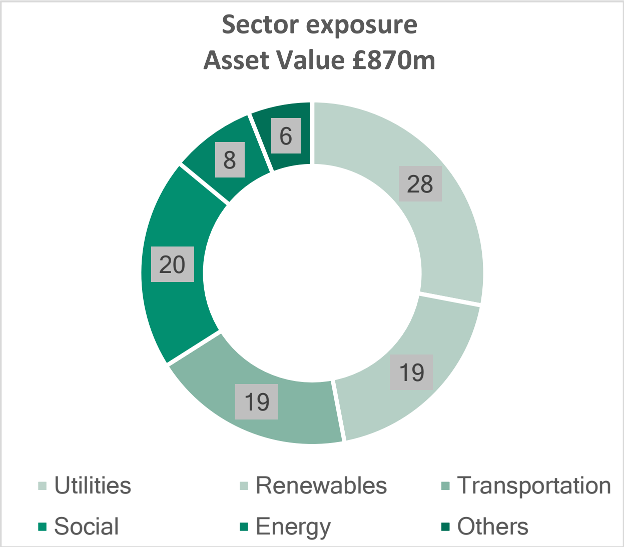
Infrastructure investments represented 11.1% of the value of Lothian Pension Fund assets at 31 March 2019, comprising one of the largest and most diversified allocations among UK LGPS funds. Of the total infrastructure investment of £870 million (31 March 2018: £795 million) invested in infrastructure,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

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

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

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



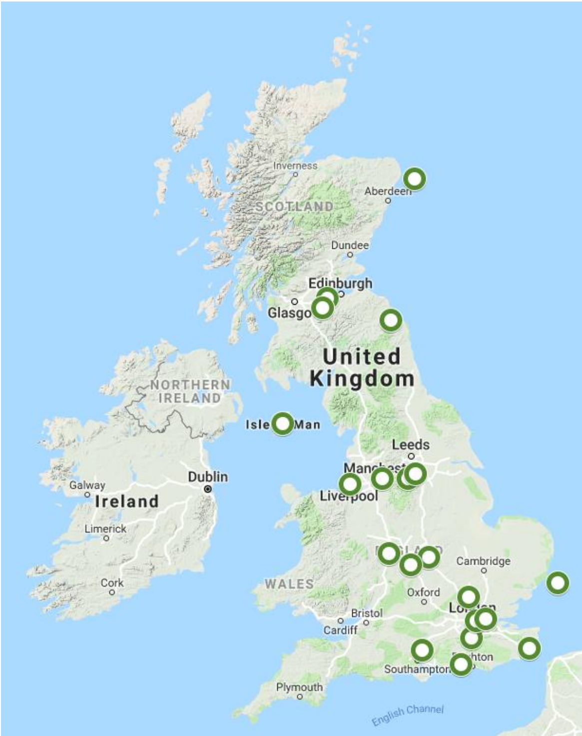


Infrastructure investments in the UK contributed 64% (or £559 million) of the total. The Funds' 20 largest UK investments, representing £400 million of value, are shown in the map below.

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

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

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



Funding Strategy Statement

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

The purpose of the Funding Strategy Statement is:

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

These objectives are desirable individually but may be mutually conflicting.

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

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

The Funding Strategy Statement was revised at the 2017 Actuarial Valuation and reflects CIPFA guidance "Preparing and maintaining a funding strategy statement in the Local Government Pension Scheme 2016". In addition to updates required as a result of changes to the Scheme Regulations and other pensions legislation, these included:

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

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

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

Financial Performance

Administration expenses

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

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

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

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

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

Reconciliation to total costs

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

Cash-flow

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

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

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

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

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

2017 Actuarial Valuations

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

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

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

Investment management cost transparency

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

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

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

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

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

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

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

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

Investment cost benchmarking

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

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

Performance and Administration

Key Performance Indicators 2018/19

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

The table shows our performance against these targets.

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

Value for money

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

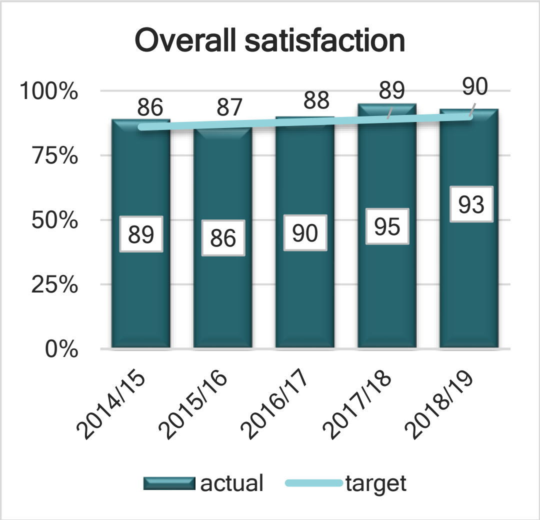
- comparison between costs and performance
- the provision of evidence to support decisions on budget relating to the sustainability and capability of the investment and administrative teams to enhance customer satisfaction

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

The outputs and analyses have served to supplement internal performance management information. However, the Chartered Institute of Public Finance and Accountancy (CIPFA) has stated that, in order to protect its commercial interests, its benchmarking reports “cannot be put in the public domain. It is for internal uses only within the authority....and for contacting and communicating with other members of the club”. We are therefore unable to include full information on the results in the Annual Report.

A summary of the benchmarking is as follows:

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



Customer and complaint feedback

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

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

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

Internal Dispute Resolution Procedure (IDRP)

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

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

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

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

Our data

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

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

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

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

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

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

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

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

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

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

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

Guaranteed Minimum Pension (GMP)

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

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

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

Pension Administration

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

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

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

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

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

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

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

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

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

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

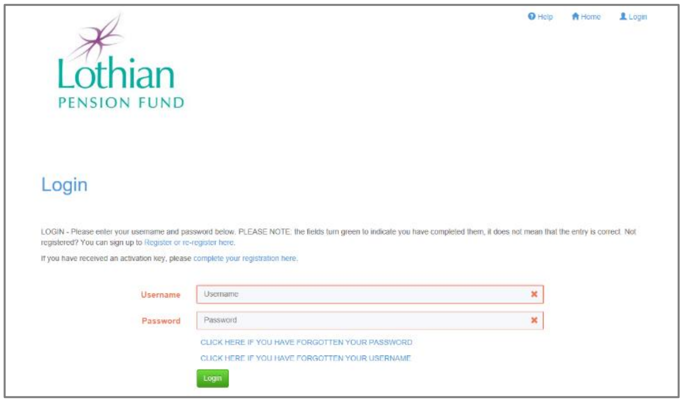
The Fund also participates in the National Fraud Initiative which is a data matching exercise led by Audit Scotland and is carried out every two years. The 2018/19 matching exercise started in Autumn 2018 and matches were made available to the Fund from 31 January 2019. We are currently investigating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

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

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

Online services

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



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

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

Unclaimed Monies Account

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

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

Employer performance

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

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

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

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

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

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

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

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

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

Employer contributions

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

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

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

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

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

Management commentary approved by:

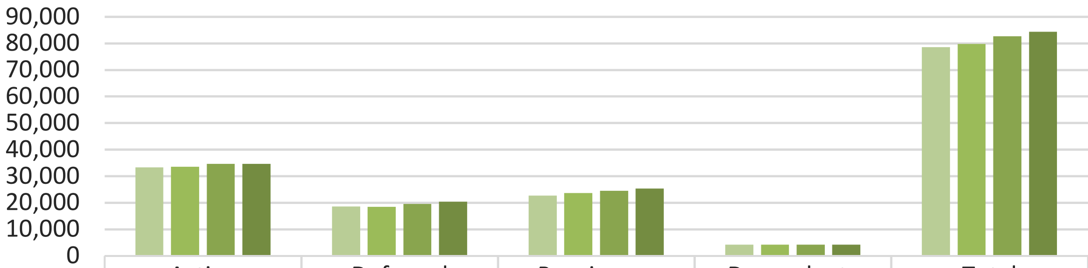
ANDREW KERR
Chief Executive Officer
The City of Edinburgh Council
25 September 2019

DOUG HERON
Chief Executive
Lothian Pension Fund
25 September 2019

JOHN BURNS
Chief Finance Officer
Lothian Pension Fund
25 September 2019

Lothian Pension Fund

Lothian Pension Fund membership



	Active	Deferred	Pensioners	Dependants	Total
31 March 2016	33,209	18,548	22,624	4,199	78,580
31 March 2017	33,526	18,381	23,595	4,202	79,704
31 March 2018	34,528	19,437	24,430	4,195	82,590
31 March 2019	34,569	20,280	25,299	4,169	84,317

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

Investment Strategy

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

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

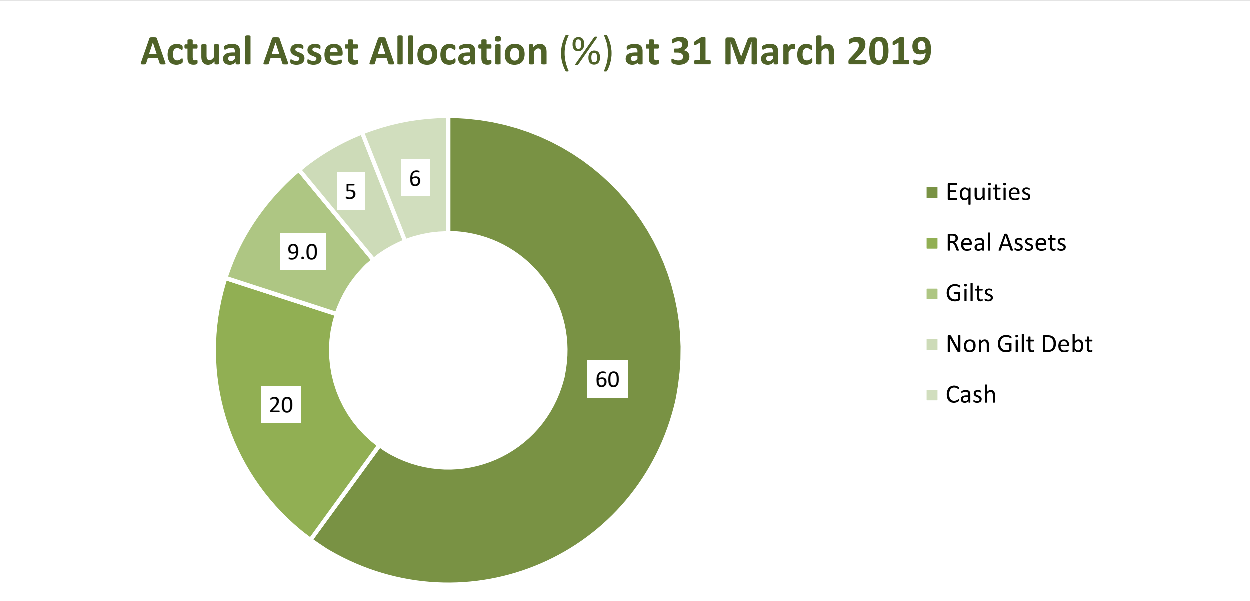
The 50/50 Strategy enables another small group of less mature employers to fund liabilities with a 50/50 mix of the Main Strategy and the Mature Employers Strategy. The liabilities funded by the 50/50 Strategy represent just over 1% of total liabilities.

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

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

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

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



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

The activity in recent years (2012-2015) has been to increase the proportion of internally managed global equity strategies to reduce investment risk. The resultant equity pool of assets is expected to perform relatively well when equity markets are weak and produce good positive absolute returns in rising equity markets.
Almost 85% of the Fund's listed equities are managed internally with the majority of these in low cost, low turnover strategies, which are expected to enhance the Fund's risk-adjusted returns over the long term. The Fund also hedges exposures to the currencies of overseas listed equities with the explicit aim of reducing volatility rather than seeking to generate improved returns. The Fund therefore maintains exposure to currencies that are expected to reduce volatility, such as the US Dollar and Japanese Yen which tend to fall as equities rise, and hedges exposure to currencies that are expected to increase volatility, such as the Australian Dollar which tends to rise as equities rise.

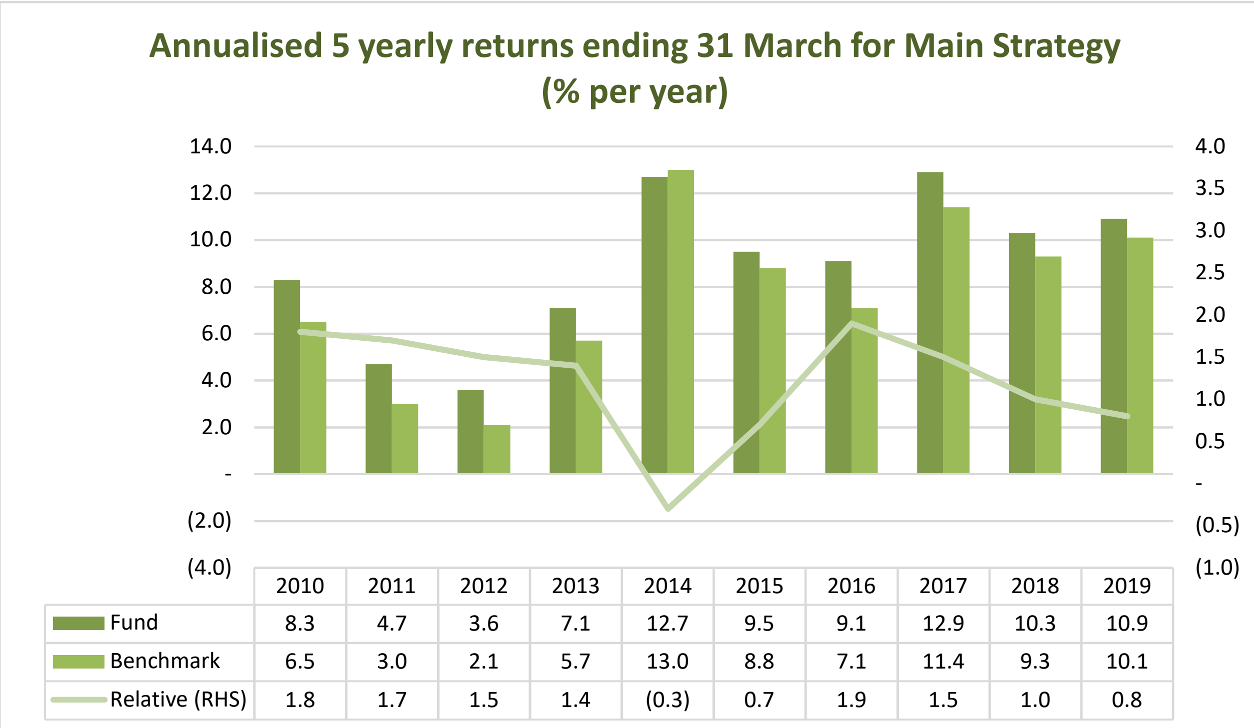
Investment performance

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

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

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

**estimated



The objectives of the Fund are:

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

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

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

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

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

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

Lothian Pension Fund

Fund Account for year ended 31 March 2019

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

Lothian Pension Fund Parent Restated 2017/18 £000	Lothian Pension Fund Group Restated 2017/18 £000		Note	Lothian Pension Fund Parent 2018/19 £000	Lothian Pension Fund Group 2018/19 £000
		Income			
156,402	156,402	Contributions from employers	**5**	175,672	175,672
45,409	45,409	Contributions from members	**6**	47,416	47,416
4,204	4,204	Transfers from other schemes	**7**	3,852	3,852
206,015	**206,015**			**226,940**	**226,940**
		Less: expenditure			
158,139	158,139	Pension payments including increases	**8**	167,997	167,997
45,117	45,117	Lump sum retirement payments	**9**	50,270	50,270
6,642	6,642	Lump sum death benefits	**10**	5,542	5,542
600	600	Refunds to members leaving service		720	720
129	129	Premiums to State Scheme		(82)	(82)
13,174	13,174	Transfers to other schemes	**11**	13,028	13,028
2,049	2,250	Administrative expenses	**12b**	2,283	2,532
225,850	**226,051**			**239,758**	**240,007**
(19,835)	**(20,036)**	**Net (withdrawals)/additions from dealing with members**		**(12,818)**	**(13,067)**
		Returns on investments			
171,948	171,948	Investment income	**13**	190,975	190,975
(25,539)	(25,539)	Change in market value of investments	**15, 20b**	503,734	503,734
(35,067)	(35,685)	Investment management expenses	**12c**	(35,938)	(36,102)
111,342	**110,724**	**Net returns on investments**		**658,771**	**658,607**
91,507	**90,688**	**Net increase in the Fund during the year**		**645,953**	**645,540**
7,083,573	7,083,034	**Net assets of the Fund at 1 April 2018**		7,175,080	7,173,722
7,175,080	**7,173,722**	**Net assets of the Fund at 31 March 2019**		**7,821,033**	**7,819,262**

Lothian Pension Fund

Net Assets Statement as at 31 March 2019

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

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

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

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

Notes to the net asset statement

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

Notes to the Financial Statements

1 Statement of Accounting Policies

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

2 Prior Year Restatement of Financial Statements

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

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

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

Lothian Pension Fund Parent 2017/18 £000	Lothian Pension Fund Group 2017/18 £000	Lothian Buses 2017/18 £000		RESTATED Lothian Pension Fund Parent 2017/18 £000	RESTATED Lothian Pension Fund Group 2017/18 £000
			Income		
148,821	148,821	7,581	Contributions from employers	156,402	156,402
43,421	43,421	1,988	Contributions from members	45,409	45,409
4,191	4,191	13	Transfers from other schemes	4,204	4,204
196,433	**196,433**	**9,582**		**206,015**	**206,015**
			Less: expenditure		
149,384	149,384	8,755	Pension payments including increases	158,139	158,139
42,533	42,533	2,584	Lump sum retirement payments	45,117	45,117
6,359	6,359	283	Lump sum death benefits	6,642	6,642
596	596	4	Refunds to members leaving service	600	600
129	129	-	Premiums to State Scheme	129	129
12,517	12,517	657	Transfers to other schemes	13,174	13,174
1,950	2,151	99	Administrative expenses	2,049	2,250
213,468	**213,669**	**12,382**		**225,850**	**226,051**
(17,035)	**(17,236)**	**(2,800)**	**Net (withdrawals)/additions from dealing with members**	**(19,835)**	**(20,036)**
			Returns on investments		
163,869	163,869	8,079	Investment income	171,948	171,948
(43,288)	(43,288)	17,749	Change in market value of investments	(25,539)	(25,539)
(32,643)	(33,261)	(2,424)	Investment management expenses	(35,067)	(35,685)
87,938	**87,320**	**23,404**	**Net returns on investments**	**111,342**	**110,724**
70,903	**70,084**	**20,604**	**Net increase in the Fund during the year**	**91,507**	**90,688**
6,595,430	6,594,891	488,143	**Net assets of the Fund at 1 April 2017**	7,083,573	7,083,034
6,666,333	**6,664,975**	**508,747**	**Net assets of the Fund at 31 March 2018**	**7,175,080**	**7,173,722**

Notes to the Financial Statements

2 Prior Year Restatement of Financial Statements (cont)

Lothian Pension Fund Parent 31 March 2018 £000	Lothian Pension Fund Group 31 March 2018 £000	Lothian Buses 31 March 2018 £000		RESTATED Lothian Pension Fund Parent 31 March 2018 £000	RESTATED Lothian Pension Fund Group 31 March 2018 £000
			Investments		
6,633,467	6,633,467	506,382	Assets	7,139,849	7,139,849
(5,112)	(5,112)	(250)	Liabilities	(5,362)	(5,362)
6,628,355	**6,628,355**	**506,132**	**Net investment assets**	**7,134,487**	**7,134,487**
1,753	**1,985**	**-**	**Non current assets**	**1,753**	**1,985**
			Current assets		
2,784	2,784	299	The City of Edinburgh Council	3,083	3,083
47,024	47,117	1,809	Cash balances	48,833	48,926
15,564	15,634	842	Debtors	16,406	16,476
65,372	**65,535**	**2,950**		**68,322**	**68,485**
-	**(1,715)**	**-**	**Non current liabilities**	**-**	**(1,715)**
			Current liabilities		
(29,147)	(29,185)	(335)	Creditors	(29,482)	(29,520)
(29,147)	**(29,185)**	**(335)**		**(29,482)**	**(29,520)**
6,666,333	**6,664,975**	**508,747**	**Net assets of the Fund at 31 March 2018**	**7,175,080**	**7,173,722**

Prior year comparative figures in the notes that follow will be marked with * if they have been affected by the merger.

3 Lothian Pension Fund Group

Basis of consolidation, presentation of financial statements and notes

Commencing with the year ended 31 March 2018, Consolidated Financial Statements have been prepared for Lothian Pension Fund. The Financial Statements of Scottish Homes Pension Fund continue to be prepared on a single entity basis.

The Consolidated Financial Statements for Lothian Pension Fund are prepared by combining the Financial Statements of the Fund (the parent entity) and its controlled entities (LPFE Limited and LPFI Limited) as defined in accounting standard IAS27 - Consolidated and Separate Financial Statements. Consistent accounting policies are employed in the preparation and presentation of the Consolidated Financial Statements. All inter-entity balances and transactions between entities, including any unrealised profits or losses, have been eliminated on consolidation.

Because the controlled entities activities are primarily focused on the provision of services to the Fund, its consolidation has a limited impact on the figures included in the Fund Account and Net Assets Statement of Lothian Pension Fund. An additional column has been added in both the Fund Account and Net Assets Statement, with the figures prior to consolidation being identified as "Parent" and after consolidation as "Group". In the notes to the accounts, where there is a difference between the parent and group figures they are identified as either "Parent " or "Group".

Notes to the Financial Statements

3 Lothian Pension Fund Group (cont)

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

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

4 Events after the Reporting Date

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

5 Contributions from employers

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

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

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

5 Contributions from employers (cont)

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

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

Included within the above contributions are accruals for:

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

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

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

6 Contributions from members

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

7 Transfers in from other pension schemes

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

8 Pensions payable

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

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

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

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

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

9 Lump sum retirement benefits payable

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

10 Lump sum death benefits payable

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

11 Transfers out to other pension schemes

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

12a Total management expenses

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

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

12b Administrative expenses

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

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

Notes to the Financial Statements

12c Investment management expenses

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

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

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

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

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

Notes to the Financial Statements

13 Investment income

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

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

Notes to the Financial Statements

14 Net investment assets

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

Notes to the Financial Statements

15a Reconciliation of movement in investments and derivatives

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

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

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

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

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

15d Reconciliation of fair value measurements within level 3

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

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

16 Derivatives - forward foreign exchange

Summary of contracts held at 31 March 2019

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

Open forward currency contracts at 31 March 2019	3,025	(854)
Net forward currency contracts at 31 March 2019		2,171
Prior year comparative		
Open forward currency contracts at 31 March 2018*	12,121	(204)
Net forward currency contracts at 31 March 2018		11,917

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

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

Notes to the Financial Statements

17 Investment managers and mandates

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

Notes to the Financial Statements

17 Investment managers and mandates (cont)

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

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

18 Securities lending

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

19 Property holdings

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

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

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

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

Notes to the Financial Statements

20 Financial Instruments

20a Classification of financial instruments

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

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

Classification of financial instruments - parent	**31 March 2018**			**31 March 2019**		
	Designated as fair value through fund account £000	**Loans and receivables £000**	**Financial liabilities at amortised cost £000**	**Designated as fair value through fund account £000**	**Loans and receivables £000**	**Financial liabilities at amortised cost £000**
Investment assets						
Bonds	736,477	-	-	855,430	-	-
Equities	4,287,464	-	-	4,559,841	-	-
Pooled investments	1,264,553	-	-	1,372,379	-	-
Property Leases	4,376	-	-	2,284	-	-
Derivative contracts	12,121	-	-	3,025	-	-
Margin balances	-	-	-	-	-	-
Cash	-	426,380	-	-	569,189	-
Other balances	-	20,110	-	-	18,828	-
	6,304,991	446,490	-	6,792,959	588,017	-
Other assets						
City of Edinburgh Council	-	3,083	-	-	884	-
Cash	-	48,833	-	-	35,897	-
Share Capital	-	60	-	-	60	-
Debtors - current	-	16,406	-	-	22,345	-
Debtors - non-current	-	1,525	-	-	3,457	-
	-	69,907	-	-	62,643	-
Assets total	6,304,991	516,397	-	6,792,959	650,660	-
Financial liabilities						
Investment liabilities						
Derivative contracts	(204)	-	-	(854)	-	-
Other investment balances	-	-	(5,158)	-	-	(1,058)
	(204)	-	(5,158)	(854)	-	(1,058)
Other liabilities						
Creditors	-	-	(29,482)	-	-	(30,799)
Liabilities total	(204)	-	(34,640)	(854)	-	(31,857)
Total net assets	6,304,787	516,397	(34,640)	6,792,105	650,660	(31,857)

	31 March 2018	31 March 2019
Total net financial instruments	6,786,544	7,410,908
Amounts not classified as financial instruments	388,536	410,125
Total net assets - parent	7,175,080	7,821,033

Notes to the Financial Statements

20a Classification of financial instruments (cont)

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

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

	31 March 2018	31 March 2019
Total adjustments to net financial instruments	(1,358)	(1,771)
Total net assets - group	7,173,722	7,819,262

20b Net gains and losses on financial instruments

	2017/18 £000	2018/19 £000
Designated as fair value through fund account	(19,843)	489,399
Loans and receivables	(18,269)	16,390
Financial liabilities at amortised cost	-	-
Total	(38,112)	505,789

	2017/18 £000	2018/19 £000
Gains and losses on directly held freehold property	12,573	(2,055)
Change in market value of investments per fund account	(25,539)	503,734

Notes to the Financial Statements

20c Fair Value Hierarchy

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

Level 1

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

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

Level 2

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

Level 3

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

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

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

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

20c Fair Value Hierarchy

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

21 Nature and extent of risk arising from financial instruments

Risk and risk management

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

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

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

Types of investment risk

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

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

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

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

The Fund manages these risks in a number of ways:

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

Sensitivity analysis

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

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

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

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

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

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

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

[1] No allowance for correlations between assets

[2] Including allowance for correlations between assets

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

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

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

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

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

Credit risk

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

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

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

Notes to the Financial Statements

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

Cash deposits

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

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

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

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

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

Notes to the Financial Statements

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

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

(a) UK Government and other UK local Authorities with no limit, other public bodies up to £20 million per

(b) Money market funds (MMFs) no more than £30 million or 15% with any one Fund.

(c) Financial Institutions: Banks and Building Societies with multiple criteria based on a range of short and long term credit ratings, as well as any security, provided from maximum of £60 million / 20% of assets under management (AUM) for institutions with the highest criteria to £10 million / 5% of AUM for institutions with the lowest acceptable criteria.

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

Securities lending

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

Derivatives

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

Refinancing risk

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

Liquidity risk

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

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

22 Actuarial statement

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

23 Actuarial present value of promised retirement benefits

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

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

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

Longevity assumptions

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

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

Commutation assumption

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

24 Non-current Debtors

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

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

The above debtors all relate to community admission bodies.

25 Debtors

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

26 Creditors

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

27 Additional Voluntary Contributions

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

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

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

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

28 Related parties

The City of Edinburgh Council

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

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

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

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

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

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

Scheme employers

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

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

Notes to the Financial Statements

28 Related parties (cont)

Governance

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

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

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

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

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

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

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

LPFE Limited & LPFI Limited- loan facility

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

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

LPFE Limited - staffing services

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

Notes to the Financial Statements

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

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

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

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

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

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

30 Retirement benefits obligation - group

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

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

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

Fund assets

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

30 Retirement benefits obligation - group (cont)

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

Amounts recognised in the Net Assets Statement	LPF Group 31 March 2018 £000	LPF Group 31 March 2019 £000
Fair value of Fund assets	8,652	10,285
Present value of Fund liabilities	(10,367)	(12,594)
	(1,715)	(2,309)

Notes to the Financial Statements

30 Retirement benefits obligation - group (cont)

Movement in the defined benefit obligation during the period

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

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

Movement in the fair value of Fund assets during the period

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

Amounts recognised in the Fund Account

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

30 Retirement benefits obligation - group (cont)

Principal actuarial assumptions used in this valuation	**31 March 2018 % p.a.**	**31 March 2019 % p.a.**
Inflation / pensions increase rate	2.3	2.4
Salary increase rate	4.0	4.1
Discount rate	2.7	2.5

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

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

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

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

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

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

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

31 Contractual commitments

Investment commitments

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

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

31 Contractual commitments (cont)

Office accommodation - 144 Morrison Street, Edinburgh

The Fund is committed to making the following future payments.

	31 March 2018 £000	31 March 2019 £000
Within one year	115	115
Between one and five years	345	345
After five years	762	647
	1,222	1,107

Recognised as an expense during the year	92	92

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

32 Contingent assets and liabilities

Contribution refunds

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

Employer Cessations

a) Funding Agreements

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

b) Homeless Action Scotland

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

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

32 Contingent assets and liabilities (cont)

EU Tax claims & income recovery

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

Variable pay arrangements

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

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

Guaranteed Minimum Pension (GMP) – Reconciliation to HMRC records

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

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

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

Guaranteed Minimum Pension (GMP)

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

32 Contingent assets and liabilities (cont)

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

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

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

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

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

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

33 Impairment losses

During the year the Fund recognised an increase in impairment losses in respect of specific benefit over payments for which reimbursement has been requested of £15k. This increased the impairment to £42.7k at the year end.

Lothian Pension Fund

Actuarial Statement for 2018/19

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The funding policy is set out in the Administering Authority's Funding Strategy (FSS), dated March 2018. In summary, the key funding principles are as follows:

- to ensure the long-term solvency of the overall Fund;
- to ensure the solvency of each individual employers' share of the Fund based on their expected term of participation in the Fund;
- to minimise the degree of short-term change in employer contribution rates;
- maximise the returns from investments within reasonable and considered risk parameters, and hence minimise the cost to the employer;
- to ensure that sufficient cash is available to meet all liabilities as they fall due for payment;
- to help employers manage their pension liabilities; and
- where practical and cost effective, to make allowance for the different characteristics of different employers and groups of employers.

The FSS sets out how the Administering Authority seeks to achieve these objectives.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2014 was as at 31 March 2017. This valuation revealed that the Fund's assets, which at 31 March 2017 were valued at £6,598 million, were sufficient to meet 98% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2017 valuation was £145 million. For the avoidance of doubt, these results are based on the assumptions that apply to the Fund's Primary investment strategy.

Each employer had contribution requirements set at the valuation with the aim of achieving full funding within a given time horizon. Contribution rates were set using one of two approaches depending on each employer's circumstances:

- Certain low risk and open employers participate in a contribution stability mechanism which limits annual changes in contribution rates. The mechanism is tested at each valuation to make sure it achieves the desired funding objectives.
- Other employers pay the contributions required to cover the cost of future service benefits and to recover the deficit/surplus identified as at 31 March 2017 over a given time period.

Individual employers' contributions for the period 1 April 2018 to 31 March 2021 were set in accordance with the Fund's funding policy as set out in its FSS, which includes further detail on the approaches mentioned above.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the 2017 valuation report.

Lothian Pension Fund

Actuarial Statement for 2018/19

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth and inflation to retirement or expected earlier date of leaving pensionable membership.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market value.

The key financial assumptions adopted under the Primary investment strategy for the 2017 valuation were as follows:

Financial assumptions	31 March 2017 % p.a.
Discount rate	3.2%
Salary increase assumption	4.1%
Benefit increase assumption (CPI)	2.4%

The key demographic assumption was the allowance made for longevity. The life expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2016 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.25% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	21.7 years	24.3 years
Future Pensioners *	24.7 years	27.5 years

*Aged 45 as at 31 March 2017

Copies of the 2017 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2017

Asset returns under the Primary investment strategy over the period have been higher than the valuation discount rate but real bond yields have fallen slightly since 31 March 2017. Combining the impact of these may mean that the overall funding level at 31 March 2019 is broadly similar to the last valuation.

The next actuarial valuation will be carried out as at 31 March 2020. The Funding Strategy Statement will also be reviewed at that time.

Richard Warden FFA
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
20 Waterloo Street, Glasgow, G2 6DB
26 April 2019

List of active employers at 31 March 2019

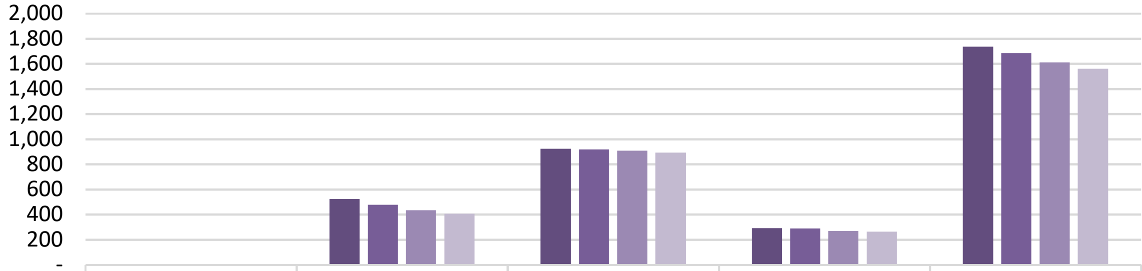
Scheduled Bodies	
City of Edinburgh Council (The)	Scottish Fire and Rescue Service
East Lothian Council	Scottish Police Authority
Edinburgh College	Scottish Water
Heriot-Watt University	SESTRAN
Lothian Buses	Visit Scotland
Lothian Valuation Joint Board	West Lothian College
Midlothian Council	West Lothian Council
Scotland's Rural College (SRUC)	

Admitted Bodies	
Amey Services	Improvement Service (The)
Audit Scotland	Into Work
Barony Housing Association Ltd	ISS UK Ltd
Baxter Storey	LPFE Ltd
Bellrock Property and Facilities Management	Melville Housing Association
Canongate Youth Project	Mitie (Edinburgh College)
Capital City Partnership	Mitie PFI
CGI UK Ltd	Morrison Facilities Services Ltd
Children's Hearing Scotland	Museums Galleries Scotland
Children's Hospice Association Scotland	Newbattle Abbey College
Citadel Youth Centre	North Edinburgh Dementia Care
Compass Chartwell	NSL Services Ltd
Convention of Scottish Local Authorities	Penumbra
Cyrenians	Pilton Equalities Project
Dacoll Limited	Queen Margaret University
Edinburgh Business School	Royal Edinburgh Military Tattoo
Edinburgh Development Group	Royal Society of Edinburgh
Edinburgh International Festival Society	Scotland's Learning Partnership
Edinburgh Leisure	Scottish Adoption Agency
Edinburgh Napier University	Scottish Futures Trust
ELCAP	Scottish Legal Complaints Commission
Enjoy East Lothian	Scottish Schools Education Research Centre (SSERC)
Family Advice and Information Resource	Skanska UK
Family and Community Development West Lothian	Sodexo Ltd
First Step	St Andrew's Children's Society Limited
Forth and Oban Ltd	St Columba's Hospice
Four Square (Scotland)	Stepping Out Project
Freespace Housing Association	Waverley Care
Granton Information Centre	University of Edinburgh (Edinburgh College of Art)
Handicabs (Lothian) Ltd	Weslo Housing Management
Hanover (Scotland) Housing Association	West Granton Community Trust
Health in Mind	West Lothian Leisure
Homes for Life Housing Partnership	Young Scot Enterprise
HWU Students Association	Youthlink Scotland

There are currently 13 ceased employers not included in the above list that are currently or in the process of setting up funding agreements to repay cessation debt over a number of years.

Scottish Homes Pension Fund

Scottish Homes Pension Fund membership



	Active	Deferred	Pensioners	Dependants	Total
31 March 2016	-	522	922	291	1,735
31 March 2017	-	478	919	289	1,686
31 March 2018	-	433	908	269	1,610
31 March 2019	-	406	892	263	1,561

Investment strategy

The Fund's actuary estimated that the funding level of the Scottish Homes Pension Fund was 104.7% at 31 March 2017.

Achievement of full funding meant that the Fund no longer needed to take investment risk by investing in equities and property. Instead, the Fund was able to minimise risk by investing solely in bonds, specifically UK gilts. These financial instruments move proportionately with liability values.

After a year of significant change, the year to 31 March 2019 brought no change to the strategy allocation of 100% bonds and this should not change until at least the results of the next actuarial valuation (March 2020) are known. At that point in time, the actuary will amend financial and demographic estimates based on actual experience over the prior three years.

The strategic and actual asset allocations for the Fund at the end of the 2018 and 2019 financial years are shown in the table below.

	Strategic Allocation 31 March 2018 %	Actual Allocation 31 March 2018 %	Strategic Allocation 31 March 2019 %	Actual Allocation 31 March 2019 %
Equities	-	-	-	-
Bonds	100.0	91.9	100.0	97.8
Property	-	2.7	-	-
Cash	-	5.4	-	2.2
Total	**100.0**	**100.0**	**100.0**	**100.0**

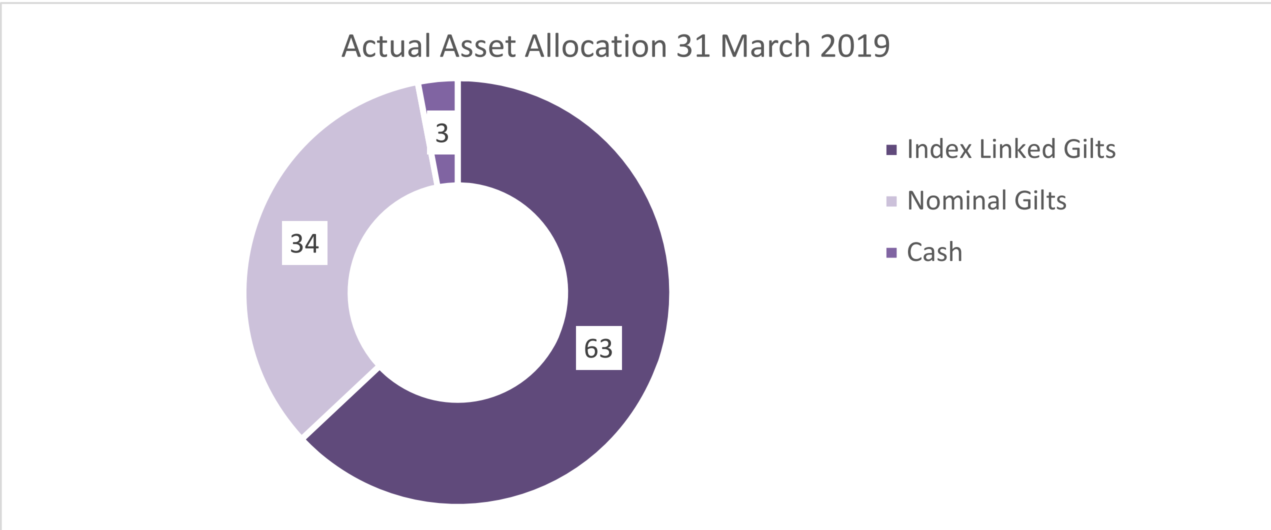
Shortly after the end of March 2018, the final sale of property assets was completed, leaving the Fund entirely invested in index-linked gilts and cash. The index linked gilts were structured to broadly match the expected liability payments as they fall due.

Given that the Fund had achieved full funding, the Pensions Committee approved a new investment objective in June 2018:

"to match the cash flow from gilt income and redemption payments as closely as possible with the expected liability payments of the fund"

Detailed analysis of the Scottish Homes liabilities was undertaken during 2018/19 to ensure that the invested assets are as closely matched with the liability profile as possible, taking into consideration the expected duration of liabilities and whether they are fixed or index-linked in nature.

This resulted in a portion of index-linked gilts being sold and reinvested in nominal gilts to achieve a closer asset-liability match. At 31 March 2019, the Fund is 'cash flow matched' up to one year beyond the next actuarial valuation expected at 31 March 2020, and 'duration matched' liabilities beyond that. This is because there is greater certainty in the earlier period - funding levels will continue to be subject to the actuary's financial or demographic assumptions of future experience, which will be reassessed during 2020/21.



Investment movements

As the Scottish Homes Pension Fud is mature, it must sell assets to pay pensions. Cash or cash equivalents are held to enable pensions to be paid in between the dates when gilts redeem.

The Fund's assets have increased in value by 4.6% over the year, adjusted for cash flow movements to pay pensions, while a proxy for the value of liabilities increased by 4.4%, which suggests that the asset-liability match is quite effective.

Scottish Homes Pension Fund

Fund Account for year ended 31 March 2019

This statement shows a summary of the income and expenditure that the Pension Fund has generated and consumed in delivering the Local Government Pension Scheme. Included is the income from investment dealings and as well as the cost of providing benefits and administration of the Fund.

Restated 2017/18 £000		Note	2018/19 £000
	Income		
575	Contributions from the Scottish Government	***2, 4***	-
-	Transfers from other schemes		-
575			**-**
	Less: expenditure		
6,666	Pension payments including increases		6,572
767	Lump sum retirement payments		591
4	Lump sum death benefits		5
47	Transfers to other schemes	***5***	129
(31)	Administrative expenses	***2, 6b***	(19)
7,453			**7,278**
(6,878)	**Net withdrawals from dealing with members**		**(7,278)**
	Returns on investments		
2,474	Investment income	***7***	1,824
(1,615)	Change in market value of investments	***8, 11b***	5,767
(165)	Investment management expenses	***6c***	(84)
694	**Net returns on investments**		**7,507**
(6,184)	**Net increase/(decrease) in the Fund during the year**		**229**
170,644	**Net assets of the Fund at 1 April 2018**		164,460
164,460	**Net assets of the Fund at 31 March 2019**	***11***	**164,689**

Scottish Homes Pension Fund

Net Assets Statement as at 31 March 2019

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

31 March 2018 £000		Note	31 March 2019 £000
	Investment Assets		
148,064	Bonds - UK		158,743
9,094	Cash Deposits		3,650
4,904	Other investment assets		618
162,062			**163,011**
	Investment Liabilities		
-	Other investment liabilities		-
-			-
162,062	**Net investment assets**	***9***	**163,011**
	Current assets		
194	The City of Edinburgh Council	***17***	10
2,240	Cash balances	***12, 17***	1,741
12	Debtors	***15***	1
2,446			**1,752**
	Current liabilities		
(48)	Creditors	***16***	(74)
(48)			**(74)**
2,398	**Net current assets**		**1,678**
164,460	**Net assets of the Fund at 31 March 2019**	***11***	**164,689**

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

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

Note to the net asset statement

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

Notes to the Financial Statements

1 Statement of Accounting Policies

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

2 Prior Year Adjustment

During the year, the Fund has changed its accounting policy in respect to the recognition of income received by the Fund from Scottish Government in relation to the administration of the Fund.

Previously this income was recognised within the employer contributions received by the Fund in relation to deficit funding. As the Scottish Homes Pension Fund now has a funding surplus no deficit funding is required and the Fund has reviewed its previous treatment. The administration charge is no longer recognised in employer contribution and is now recognised as income against the administrative expenses of the Fund.

	2017/18 Audited £000	Adjustment £000	2017/18 Restated £000
Contributions from the Scottish Government	675	(100)	575
Administrative expenses	(69)	100	31

3 Events after the Reporting Date

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

4 Contributions from the Scottish Government

The Scottish Homes Pension Fund (SHPF) is a single employer pension fund for former employees of Scottish Homes (subsequently Communities Scotland) (and persons who were employed by the Scottish Special Housing Association, but who did not become employees of Scottish Homes). The City of Edinburgh Council was selected by the Scottish Executive to be the administering authority of a fund created prior to the wind up of the Scottish Homes Residuary Body and therefore became the administering authority of SHPF on 1 July 2005, pursuant to section 2(a)(1A) of The Local Government Pension Scheme (Scotland) Amendment (No. 2) Regulations 2005 (SSI 315/2005) (the 2005 Regs).

SHPF is a mature, non-active fund (that is, the fund has no contributions paid into it by active members but consists only deferred and pensioner members and therefore only pays money out to the pensioners).

Section 2 (1C) of the 2005 Regs stipulates that:
Where the actuary determines, after having regard to the existing and prospective liabilities of the fund, that additional funding is necessary to maintain the solvency of the fund (SHPF), then Scottish Ministers will make payments to the administering authority to maintain that solvency.

In this way, the Scottish Government acts as the 'Guarantor' for SHPF's liabilities, as confirmed in the Funding agreement, signed on behalf of the Scottish Executive and dated 6 July 2005.

As at the latest triennial actuarial valuation date of 31 March 2017, SHPF showed a funding surplus of £7.7million with a funding level of 104.7%, derived from a market valuation of assets of £170.6million and liabilities of £162.9million.

Notes to the Financial Statements

4 Contributions from the Scottish Government (cont)

Having implemented the investment strategy as required by the Funding Agreement, the assets of SHPF are invested entirely in low risk, index-linked gilts. With a funding surplus, the Scottish Government is not required to provide any contribution, but as Guarantor has the reponsibility to pay towards the administration expenses of the Fund estimated to be £70,000 per annm (for years 2018 to 31 March 2021.

In addition the Guarantor is responsible for meeting the cost of investment expenses . Given the Fund's surplus the Fund are comfortable that investment expenses can be met directly by the Fund until the next triannual valuation.

5 Transfers out to other pension schemes

	2017/18 £000	2018/19 £000
Group transfers	-	-
Individual transfers	47	129
	47	129

6a Total Management expenses

	Restated 2017/18 £000	2018/19 £000
Administrative costs	(31)	15
Investment management expenses	107	19
Oversight and governance costs	58	31
	134	65

This analysis of costs for the Scottish Homes Pension Fund has been prepared in accordance with CIPFA guidance. The analysis looks at the combined administration and investment management expenses in note 6b and c and splits out the costs to include a third heading covering oversight and governance expenditure.

6b Administrative expenses

	Restated 2017/18 £000	2018/19 £000
Employee costs	24	28
System costs	8	8
Actuarial fees	30	8
External audit fees	1	1
Printing and postage	2	2
Depreciation	1	1
Office costs	2	2
Sundry costs less sundry income	1	1
	69	51
Administration fee received	(100)	(70)
	(31)	(19)

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

Notes to the Financial Statements

6c Investment management expenses

	2017/18 £000	2018/19 £000
External management fees - deducted from capital (direct)	54	-
Transaction costs	30	2
Employee costs	31	44
Custody fees	7	6
Engagement and voting fees	2	2
Performance measurement fees	10	3
Consultancy fees	16	3
System costs	7	9
Legal fees	1	2
Office costs	2	2
Sundry costs less sundry income	5	11
	165	84

The Fund has not incurred any performance-related investment management fees in 2018/19 or 2017/18.

7 Investment income

	2017/18 £000	2018/19 £000
Income from fixed interest securities	1,449	1,749
Dividends from equities	799	-
Income from pooled investments - property	270	-
Interest on cash deposits and sundries	29	75
	2,547	1,824
Irrecoverable withholding tax	(73)	-
	2,474	1,824

8 Reconciliation of movement in investments

	Market value at 31 March 2018 £000	Purchases at cost £000	Sales & proceeds £000	Change in market value £000	Market value at 31 March 2019 £000
Bonds	148,064	54,948	(50,036)	5,767	158,743
Equities	-	-	-	-	-
Pooled investment vehicles	-	-	-	-	-
	148,064	54,948	(50,036)	5,767	158,743
Other financial assets / (liabilities)					
Cash deposits*	9,094			-	3,650
Investment income due/amounts payable*	4,904			-	618
	13,998			-	4,268
Net financial assets	162,062			5,767	163,011

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

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

Notes to the Financial Statements

8 Reconciliation of movement in investments (cont)

	Market value at 31 March 2017 £000	Purchases at cost £000	Sales & proceeds £000	Change in market value £000	Market value at 31 March 2018 £000
Bonds	127,970	33,345	(11,838)	(1,413)	148,064
Equities	28,221	932	(28,451)	(702)	-
Pooled investment vehicles	7,998	-	(8,621)	623	-
	164,189	34,277	(48,910)	(1,492)	148,064
Other financial assets / (liabilities)					
Cash deposits*	3,602			(123)	9,094
Investment income due/amounts payable*	459			-	4,904
	4,061			(123)	13,998
Net financial assets	168,250			(1,615)	162,062

** Per CIPFA disclosure guidance the change in market value intentionally does not balance opening/closing market values*

9 Investment managers and mandates

Manager	Mandate	Market value at 31 March 2018 £000	% of total 31 March 2018 %	Market value at 31 March 2019 £000	% of total 31 March 2019 %
In-house	High Div Equity	87	0.1	31	0.0
Total global equities		87	0.1	31	0.0
In-house	UK Index linked gilts	148,858	91.9	159,330	97.8
Total fixed interest and	**inflation linked bonds**	148,858	91.9	159,330	97.8
Schroders	Property	4,363	2.7	-	-
Total property		4,363	2.7	-	-
In-house	Cash	8,754	5.4	3,650	2.2
Total cash		8,754	5.4	3,650	2.2
Net financial assets		162,062	100.0	163,011	100.0

10 Investments representing more than 5% of the net assets of the Fund

	Market value at 31 March 2018 £000	% of total 31 March 2018 %	Market value at 31 March 2019 £000	% of total 31 March 2019 %
UK Gov 2.5% Index Linked 16/04/20	12,309	7.5	11,619	7.1
UK Gov 4.25% 07/06/32	-	-	9,366	5.7
UK Gov 4.125% Index Linked 22/07/30	-	-	9,124	5.5
UK Gov 2.5% Index Linked 17/07/24	12,431	7.6	9,053	5.5
UK Gov 1.25% Index Linked 22/11/27	11,149	6.8	8,914	5.4
UK Gov 1.875% Index Linked 22/11/22	12,530	7.6	8,240	5.0
UK Gov 4.125% Index Linked 22/11/17	21,410	13.0	-	-
UK Gov 1.125% Index Linked 22/11/37	12,465	7.6	-	-

Notes to the Financial Statements

11 Financial Instruments

11a Classification of financial instruments

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

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

	31 March 2018			31 March 2019		
Financial assets	Designated as fair value through fund account £000	Loans and receivables £000	Financial liabilities at amortised cost £000	Designated as fair value through fund account £000	Loans and receivables £000	Financial liabilities at amortised cost £000
Investment assets						
Bonds	148,064	-	-	158,743	-	-
Equities	-	-	-	-	-	-
Pooled investments	-	-	-	-	-	-
Cash	-	9,094	-	-	3,650	-
Other balances	-	4,904	-	-	618	-
	148,064	13,998	-	158,743	4,268	-
Other assets						
City of Edinburgh Council	-	194	-	-	10	-
Cash	-	2,240	-	-	1,741	-
Debtors	-	12	-	-	1	-
	-	2,446	-	-	1,752	-
Assets total	148,064	16,444	-	158,743	6,020	-
Financial liabilities						
Other liabilities						
Creditors	-	-	(48)	-	-	(74)
Liabilities total	-	-	(48)	-	-	(74)
Total net assets	148,064	16,444	(48)	158,743	6,020	(74)
Total net financial instruments			164,460			164,689

11b Net gains and losses on financial instruments

	2017/18 £000	2018/19 £000
Designated as fair value through fund account	(1,492)	5,767
Loans and receivables	(123)	-
Financial liabilities at amortised cost	-	-
Total	(1,615)	5,767

Notes to the Financial Statements

11c Valuation of financial instruments carried at fair value

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

Level 1

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

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

Level 2

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

Level 3

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

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

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

	31 March 2019			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Investment assets				
Designated as fair value through fund account	-	158,743	-	158,743
Total investment assets	-	158,743	-	158,743
Investment liabilities				
Designated as fair value through fund account	-	-	-	-
Total investment liabilities	-	-	-	-
Net investment assets	-	158,743	-	158,743

Notes to the Financial Statements

11c Valuation of financial instruments carried at fair value (cont)

	31 March 2018			
	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
Investment assets				
Designated as fair value through fund account	-	148,064	-	148,064
Total financial assets	-	148,064	-	148,064
Investment liabilities				
Designated as fair value through fund account	-	-	-	-
Total financial liabilities	-	-	-	-
Net investment assets	-	148,064	-	148,064

12 Nature and extent of risk arising from financial instruments

Risk and risk management

The Fund's primary aim is to ensure that all members and their dependants receive their benefits when they become payable. As directed by Scottish Governemnt, after 31 March 2017 triennial valuation showed a funding level of 104.7%, the assets of the Fund were invested entirely in low risk gilts. In addition, the Fund ensures that sufficient cash is available to meet all liabilities when they are due to be paid.

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

Types of investment risk

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

Market risk also changes over time as economic conditions and investor sentiment change. The market risk of Scottish Homes Pension Fund has to some extent been mitigated. The Fund's assets have been matched to its liabilities as at the 31 March 2017 triennial valuation so interest rate risk has been minimised and as all assets held are valued in Pound Sterling no exchange risk occurs. A review of the asset matching of the Fund will next take place to coincide with the results of 31 March 2020 triennial valuation.

Sensitivity analysis

Asset prices have a tendency to fluctuate. The degree of such fluctuation is known as "volatility" and it differs by asset class. The table sets out the long-term volatility assumptions used by the Fund's investment adviser KPMG:

Asset type	Potential price movement (+ or -)
Index-Linked Gilts	11.2%
Cash	0.9%

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

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

Asset classes don't always move in line with each other. The extent to which assets move together is known as their "correlation". A lower correlation means that there is less risk of assets losing value at the same time. The overall Fund benefits from "diversification" because it invests in numerous different asset classes, which don't all move in line with each other. Consequently, the aggregate risk at the Fund level is less than the total risk from all the individual assets in which the Fund invests.

The following table shows the risks at the asset class level and the overall Fund level.

	Value at 31 March 2019 £000	% of fund %	Potential Change +/- %	Value on increase £000	Value on decrease £000
Index-Linked Gilts	159,329	97.7	11.2	177,174	141,484
Cash	3,681	2.3	0.9	3,714	3,648
Total [1]	163,010	100.0	11.0	180,888	145,132
Total [2]			11.0	180,892	145,128
Total [3]			4.8	170,834	n/a

[1] No allowance for correlations between assets

[2] Including allowance for correlations between assets

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

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

It can be seen that the risk to the overall Fund assets [2] is lower than the total of the risks to the individual assets [1].

However, because the purpose of a pension scheme is to make payments to scheme beneficiaries, the true risk of a pension scheme is not measured in absolute terms, but relative to its liabilities [3]. The risk is lower than the absolute asset risk, due to the impact of correlation with the discount rate used to value the liabilities.

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

Credit risk

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

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

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

Cash deposits are the major areas of credit exposure where credit risk is not reflected in market prices.

Cash deposits

At 31 March 2019, cash deposits represented £9m, 5.5% of total net assets. This was held with the following institutions:

	Moody's Credit Rating at 31 March 2019	Balances at 31 March 2018 £000	Balances at 31 March 2019 £000
Held for investment purposes			
Northern Trust Company - cash deposits	A2	1,077	580
The City of Edinburgh Council - treasury management	See below	8,017	3,070
		9,094	3,650
Held for other purposes			
The City of Edinburgh Council - treasury management	See below	2,240	1,741
Total cash		11,334	5,391

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

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

(a) UK Government and other UK local Authorities with no limit, other public bodies up to £20 million per organisation.

(b) Money market funds (MMFs) no more than £30 million or 15% with any one Fund.

(c) Financial Institutions: Banks and Building Societies with multiple criteria based on a range of short and long term credit ratings, as well as any security provided, from maximum of £60 million / 20% of assets under management (AUM) for institutions with the highest criteria to £10 million / 5% of AUM for institutions with the lowest acceptable criteria.

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

	Moody's Credit Rating at 31 March 2019	Balances at 31 March 2018 £000	Balances at 31 March 2019 £000
Money market funds			
Deutsche Bank AG, London	Aaa-mf	44	129
Goldman Sachs	Aaa-mf	-	2
Aberdeen Standard Sterling Liquidity Fund	Aaa-mf	-	706
Standard Life Investments	Aaa-mf	1,520	-
Bank call accounts			
Bank of Scotland	Aa3	1,013	473
Royal Bank of Scotland	A3	37	19
Santander UK	Aa3	27	-
Barclays Bank	A1	1	-
Svenska Handelsbanken	Aa2	50	-
HSBC Bank PLC	Aa3	4	-
Notice accounts			
HSBC Bank PLC	Aa3	-	569
UK Pseudo-Sovereign risk instruments			
Other Local Authorities [1]	Aa1	7,561	2,913
		10,257	4,811

[1] Very few Local Authorities have their own credit rating but they are generally assumed to have a pseudo-sovereign credit rating (which in the UK at 31 March 2018 was 'Aa1').

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

Refinancing risk

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

Liquidity risk

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

All of the Fund’s investments could be converted to cash within three months in a normal trading environment.

13 Actuarial statement

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

Notes to the Financial Statements

14 Actuarial present value of promised retirement benefits

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standard 19 (IAS19) assumptions, is estimated to be £135m (2018 £134m). This figure is used for statutory accounting purposes by Scottish Homes Pension Fund and complies with the requirements of IAS26. The assumptions underlying the figure match those adopted for the Administering Authority's IAS19 reports at each year end.

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

	31 March 2018 % p.a.	31 March 2019 % p.a.
Inflation/pensions increase rate	2.4%	2.5%
Discount rate	2.7%	2.4%

Longevity assumptions

The life expectancy assumption is based on Fund specific statistical analysis with improvements in line with the CMI 2016 model, assuming that the current rate of improvements has reached a peak and will converge to a long term rate of 1.75% p.a.. Based on these assumptions, the average future life expectancies, in years, at age 65 are summarised below:

	31 March 2018		31 March 2019	
	Males	Females	Males	Females
Current pensioners	22.4 years	24.8 years	22.4 years	24.8 years
Future pensioners (assumed to be currently 45)	24.8 years	27.8 years	24.8 years	27.8 years

Commutation assumption

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

15 Debtors

	31 March 2018 £000	31 March 2019 £000
Sundry debtors	12	1
	12	1

16 Creditors

	31 March 2018 £000	31 March 2019 £000
Benefits payable	3	73
Miscellaneous creditors and accrued expenses	45	1
	48	74

17 Related party transactions

The City of Edinburgh Council

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

17 Related party transactions (cont)

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

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

	31 March 2018 £000	31 March 2019 £000
Year end balance of holding account	194	10
	194	10

Part of the Fund's cash holdings are invested on the money markets by the treasury management operations of the Council, through a service level agreement. During the year to 31 March 2019, the fund had an average investment balance of £10.6m (2018 £6.3m). Interest earned was £74k (2018 £29k).

Year end balance on treasury management account	31 March 2018 £000	31 March 2019 £000
Held for investment purposes	8,011	3,070
Held for other purposes	2,240	1,741
	10,251	4,811

Fund Guarantor

The Fund guarantor (by definition) is a related party to the scheme. The Scottish Government's contributions to the Fund can be found in note 4 (page 89) of the notes to the Financial Statements.

LPFE Limited - staffing services

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

Governance

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

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

17 Related party transactions (cont)

During the period from 1 April 2018 to the date of issuing of these accounts, the Fund was charged by City Of Edinburgh Councils via its service level agreement for time spent by its Executive Management team on pension fund issues. All other staff that held key positions in the financial management of Lothian Pension Fund were employed by LPFE Limited. Total compensation paid in relation to key management personnel employed by LPFE Limited during the period was as follows:

	31 March 2018 £000	31 March 2019 £000
Short-term employee benefits	415	567
Post-employment benefits - employer pension contributions	85	111

Key management personnel employed by LPFE, had accrued pensions totalling £120,245 (1 April 2018: £97,456) and lump sums totalling £132,375 (1 April 2018: £110,889) at the end of the period.

Staff are either employed by City of Edinburgh Council or LPFE Limited, and their costs reimbursed by the Pension Funds. The Councillors, who are members of the Pensions Committee, are also remunerated by City of Edinburgh Council.

18 Contingent assets/liabilities

Request for direction by Scottish Ministers to transfer the assets and liabilities of Homeless Action Scotland from the Lothian Pension Fund to the Scottish Homes Pension Fund

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

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

Guaranteed Minimum Pension (GMP)

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

Notes to the Financial Statements

18 Contingent assets/liabilities (cont)

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

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

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

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

19 Contractual commitments

The Fund had no contractual commitments at the year end.

20 Impairment losses

No impairment losses have been identified during the year.

Actuarial Statement for 2018/19

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2014. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of Funding Policy

The Administering Authority's Funding Strategy Statement (FSS), dated March 2018, states that a bespoke funding strategy has been adopted for the Fund.

The strategy aims for the Fund to be 100% solvent by 2044 using a discount rate based on government bonds. It includes target funding levels at each actuarial valuation. Contributions from the Scottish Government are determined by reference to the target funding levels. The deficit recovery period is 8 years.

As the Fund was well ahead of its Target Funding Level at the 2017 valuation, it took the decision to derisk its investment strategy and now invests 100% of its assets in index-linked gilts.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2014 was as at 31 March 2017. This valuation revealed that the Fund's assets, which at 31 March 2017 were valued at £170.6 million, were sufficient to meet 104.7% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting surplus at the 2017 valuation was £7.7 million.

The Guarantor's contributions for the period 1 April 2018 to 31 March 2021 were set in accordance with the Fund's funding policy as set out in its FSS.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the 2017 valuation report.

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund's assets at their market value.

The key financial assumptions adopted for the 2017 valuation were as follows:

Financial assumptions	31 March 2017
Discount Rate	Bank of England nominal yield curve
Benefit increase assumption (CPI)	Bank of England implied (RPI) curve less 1.0% p.a.

Actuarial Statement for 2018/19

The key demographic assumption was the allowance made for longevity. The life expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2016 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.75% p.a.

Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	22.4	24.8
Future Pensioners *	24.8	27.8

*Aged 45 as at 31 March 2017

Copies of the 2017 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2017

Since the last formal valuation, real bond yields have fallen placing a higher value on the liabilities but there have been positive asset returns over the 2 years. Both events are of broadly similar magnitude with regards to the impact on the funding position.

The next actuarial valuation will be carried out as at 31 March 2020. The Funding Strategy Statement will also be reviewed at that time.

Richard Warden FFA
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
20 Waterloo Street
Glasgow
G2 6DB

26 April 2019

Statement of Accounting Policies and General Notes

1 Basis of preparation

The Financial Statements have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

The Financial Statements summarise the transactions of the funds for the 2018/19 financial year and report on the net assets available to pay pension benefits as at 31 March 2019. The Financial Statements do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present values of promised retirement benefits, valued on an International Accounting Standard (IAS) 19 basis, are disclosed in the Notes to the Financial Statements.

2 Summary of significant accounting policies

General

a) Basis of consolidation

i) Group accounts

Commencing with the year ended 31 March 2016, Consolidated Financial Statements have been prepared for Lothian Pension Fund. The Financial Statements of Scottish Homes Pension Fund continue to be prepared on a single entity basis.

The Consolidated Financial Statements for Lothian Pension Fund are prepared by combining the Financial Statements of the Fund (the parent entity) and its controlled entities (LPFE Limited and LPFI Limited) as defined in accounting standard IAS27 - Consolidated and Separate Financial Statements. Consistent accounting policies are employed in the preparation and presentation of the Consolidated Financial Statements. All inter-entity balances and transactions between entities, including any unrealised profits or losses, have been eliminated on consolidation.

Further details of the consolidation are provided in the Notes to the Financial Statements of Lothian Pension Fund.

LPFE Limited (LPFE) and LPFI Limited (LPFI) are wholly owned by the City of Edinburgh Council in its capacity as administering authority for the Local Government Pension Scheme in the Lothian area.

The purpose of LPFE is to provide staff services in respect of management of the Fund. LPFI's purpose is to provide FCA regulated services to the Fund and other Local Government Pension Scheme funds. It is considered appropriate to consolidate the Financial Statements of the two companies with those of Lothian Pension Fund.

ii) Lothian Buses Pension Fund merger

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

Section 2.5 of the Code states that 'The combination of two or more local authorities into one new authority, or the transfer of functions from the responsibility of one authority to another, shall be accounted for under the principles that apply to group reconstructions and shall be accounted for as either a transfer by absorption or a transfer by merger.' 'Transfers by merger are rare transactions but may occur when legal transfers take place and management of the local government entity consider that in substance for a true and fair presentation of the local government entity the financial statements would be best presented as if the entity had always existed in its newly combined form.

The results and cash flows of all of the combining bodies (or functions) should be brought into the financial statements of the combined body from the beginning of the financial year in which the combination occurred…..'.

Specialist legal opinion had been sought prior to the merger of Lothian Buses Pension Fund. This concluded that "…Lothian Buses Pension Fund was set up as a 'further fund', within the meaning of the Local Government Superannuation (Funds) (Scotland) Regulations 1986 (the 'Funds Regulations')….At the time when the Admission Agreement was entered into, there was a clear mechanism under legislation whereby a 'further fund' could be dissolved and transferred back into the Main Fund." Also, "It is worth noting that, under the Admission Agreement…, Lothian Buses was admitted first of all to the Main Fund (immediately following which) the further Fund was set up".

Accordingly, with such assurance that "the newly combined body or functions has always existed", the consolidation of Lothian Buses Pension Fund "sub-fund" into Lothian Pension Fund has been accounted for by the 'transfer by merger'.

Fund account - revenue recognition

b) Contribution income

Normal contributions, both from the members and from employers, are accounted for on an accruals basis at the rate certified by the Scheme Actuary in the payroll period to which they relate.

Similarly, employer deficit funding contributions are accounted for on the due date on which they are payable as certified by the Scheme Actuary.

Employers' pensions strain contributions are accounted for in the period in which the liability arises. Any amount due but unpaid will be classed as a current financial asset. Amounts not due until future years are classed as long-term financial assets.

c) Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the Local Government Pension Scheme Regulations.

Individual transfers in/out are accounted for when received/paid, which is normally when the member liability is accepted or discharged.

Transfers in from members wishing to use the proceeds of their additional voluntary contributions to purchase scheme benefits are accounted for on a receipts basis and are included in transfers in.

Bulk (group) transfers are accounted for on an accruals basis in accordance with the terms of the transfer agreement.

d) Investment income

i) Interest income

Interest income is recognised in the Fund accounts as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination. Income includes the amortisation of any discount or premium, transaction costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

ii) Dividend income

Dividend income is recognised on the date the shares are quoted ex-dividend. Any amount not received by the end of the reporting period is disclosed in the Net Assets Statement as a current financial asset.

iii) Distributions from pooled funds

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the Net Assets Statement as a current financial asset.

iv) Income from unquoted private equity and infrastructure investments

Income from the above sources is recognised when it is notified by the manager. Distributions are split into capital and income elements with the latter being included under investment income in the Fund Account.

v) Property related income

Property-related income consists primarily of rental income. Rental income from operating leases on properties owned by Lothian Pension Fund is recognised on a straight-line basis over the term of the lease. Any lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

Rental income is reported gross with the operational costs of the properties included in investment management expenses.

Contingent rents based on the future amount of a factor that changes other than with the passage of time, such as turnover rents, are only recognised when contractually due.

vi) Movement in the net market value of investments

Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during the year.

Fund Account - expense items

e) Benefits payable

Pensions and lump sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the Net Assets Statement as current liabilities.

f) Taxation

i) Pension Funds

The Local Government Pension Scheme is a registered public service scheme under section 1(1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax is accounted for as a fund expense as it arises.

ii) Controlled entities - LPFE and LPFI

The Companies are mutual traders and are therefore not liable to corporation tax on any surpluses generated from services provided in respect of the Fund. The tax charges for the period are based on any profit for the period from non-mutual trade, adjusted for any non-assessable or disallowed items. They are calculated using tax rates that have been enacted or are substantively enacted by the period end date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Financial Statements. No deferred tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

g) Administrative expenses

All administrative expenses are accounted for on an accruals basis. The Lothian Pension Fund is responsible for administering the two Funds. The costs include charges from LPFE and LPFI for services rendered. The Fund receives an allocation of the overheads of the Council, this is based on the amount of central services consumed. In turn, these costs are allocated to the two Funds.

Costs directly attributable to a specific fund are charged to the relevant Fund. Investment management costs that are common to all funds are allocated in proportion to the value of each Fund as at the end of the year. Other administration costs are allocated in proportion to the number of members in each of the Funds at the end of the year.

h) Investment management expenses

All investment management expenses are accounted for on an accruals basis.

Fees of the external investment managers and custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.

For some investment managers, an element of their fee is performance related. The amount of any performance related fees paid is disclosed in the note to the accounts on investment management expenses provided for each Fund.

The cost of administering the Local Government Pension Scheme in the UK has come under increasing scrutiny in recent years. As a result, it has been decided to recognise investment management costs that are deducted from the value of an investment and recognised this as a cost in the Fund Account rather than as a reduction in the change in market value of investments. Investment transaction costs that are added to an investment purchase price or deducted from the proceeds of a sale are also recognised as a cost in the Fund Account rather than as a reduction in the change in market value of investments.

In June 2016, CIPFA revised and updated its guidance “Accounting for Local Government Pension Scheme Management Costs”. Whilst the underlying principle of transparency of investment costs remains unchanged, there has been a degree of relaxation to full cost disclosure. Specifically, for complex “fund of funds” structures, the new guidance states that “Investment costs incurred by a separate legal entity, or in respect of investment decisions over which the pension fund has no control, should not be included in the (Pension) Fund Account......If pension funds wish to provide information about the total cost of “fund of fund” investments, this should be included as part of the Investments section in the Annual Report”.

The impact of this is that investment management costs deducted from any underlying fund in a "fund of funds" investment would not be included in the costs disclosed in the Fund Account. As this would significantly under-report investment management costs the decision has been made not to adopt this element of the CIPFA guidance. However, this type of cost is separately identified as "external management fees - deducted from capital (indirect)" in the notes on investment management expenses.

Any indirect costs incurred through the bid-offer spread on some pooled investment vehicles are not treated as an expense. Such costs are accounted for as part of the acquisition costs or sale proceeds.

The cost of obtaining investment advice from external consultants is included in investment management charges.

The costs of the in-house investment management team are charged to the Fund. The basis of allocation is as described in section g.

Securities lending revenue is reported gross and their fees are disclosed in investment management expenses.

i) Operating lease

Lease payments under an operating lease are recognised as an expense on a straight-line basis over the term of the lease. In accordance with Standard Interpretations Committee (SIC) 15, subsequently endorsed by the International Accounting Standards Board (IASB), lease incentives are recognised as a reduction in the lease expense over the term of the lease on a straight-line basis.

Net Assets Statement

j) Financial assets

Financial assets are included in the Net Assets Statement on a fair value basis as at the reporting date. A financial asset is recognised in the Net Assets Statement on the date the Fund becomes party to the contractual acquisition of the asset. From this date, any gains or losses arising from changes in the fair value of asset are recognised by the Fund.

The values of investments as shown in the Net Assets Statement have been determined at fair value in accordance with the requirements of the Code and IFRS13. For the purposes of disclosing levels of fair value hierarchy, the Fund has adopted the classification guidelines recommended in Practical Guidance on Investment Disclosures (PRAG/Investment Association, 2016).

The basis of the valuation of each class of investment assets is set out below. There has been no change in the valuation techniques used during the year. All assets have been valued using fair value techniques which represent the highest and best price available at the reporting date.

Description of asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivity affecting the valuations provided
Market quoted investments - Equities	Level 1	Closing bid value on published exchanges	Not required	Not required
Exchange traded pooled investments	Level 1	Closing bid value on published exchanges	Not required	Not required
Future derivative contracts	Level 1	Determined using exchange prices at the reporting date. Amounts due from or owed to the broker are the amounts outstanding in respect of the initial margin and variation margin.	Not required	Not required

Description of asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivity affecting the valuations provided
Forward foreign exchange derivatives	Level 1	Based on market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year-end with an equal and opposite contract.	Not required	Not required
Government bonds - fixed interest / index linked gilts	Level 2	Recorded at net market value based on their current yields.	Evaluated price feeds	Not required
Freehold and leasehold properties	Level 3	Valued at fair value at the year-end using the investment method of valuation by John Symes-Thompson FRICS of independent valuers, CBRE Ltd in accordance with RICS Valuation – Global Standards 2017	Existing lease terms and rentals. Independent market research. Nature of tenancies. Covenant strength for existing tenants. Assumed vacancy levels. Estimated rental growth. Discount rate	Significant changes in rental growth, vacancy levels or the discount rate could affect valuations as could more general changes to market price
Unquoted Pooled investments – Private Equity, Infrastructure, Timber, Private Secured Loans & Property	Level 3	Comparable valuation of similar companies in accordance with International Private Equity and Venture Capital Guidelines (2015)	EBITDA multiple Revenue multiple. Discount for lack of marketability. Control premium.	Valuations could be affected by material events occurring between the date of the financial statements provided and the Fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts.

Sensitivity of assets valued at level 3

Having analysed historical data and current market trends, and consulted with independent investment advisers, the Fund has determined that the valuation methods described above are likely to be accurate to within the following ranges, and has set out below the consequent potential impact on the closing value of investments held at 31 March 2019.

Lothian Pension Fund Unquoted	Assessed Valuation range (+ or -)	Value at 31 March 2019 £m	Value on increase £m	Value on decrease £m
Private Equity	30%	76.1	98.9	53.3
Infrastructure	12%	844.9	946.3	743.5
Timber	18%	124.0	146.3	101.7
Private Secured Loans	7.5%	205.0	220.4	189.6
Property	13%	461.0	520.9	401.1
		1,711.0	1,932.8	1,489.2

Scottish Homes Pension Fund has no assets valued at Level 3.

k) Foreign currency transactions and balances

Dividends, interest and purchases and sales of investments in foreign currencies have been accounted for at the spot market rates at the date of the transaction. End-of-year spot market exchange rates are used to value cash balances held in foreign currency bank accounts, market values of overseas investments and purchases and sales outstanding at the end of the reporting period.

l) Cash and cash equivalents

Cash comprises cash in hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal risk of changes in value.

m) Financial liabilities

The Fund recognise financial liabilities at fair value as at the reporting date. A financial liability is recognised in the Net Assets Statement on the date the Fund becomes party to the liability. From this date, any gains or losses arising from changes in the fair value of the liability are recognised.

n) Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits of each of the Fund is assessed on an annual basis by the Scheme Actuary in accordance with the requirements of IAS 19 and relevant actuarial standards.

As permitted under IAS26, the Fund have opted to disclose the actuarial present value of promised retirement benefits by way of a note to the Net Assets Statements.

o) Additional voluntary contributions

The Lothian Pension Fund and Lothian Buses Pension Fund provide an additional voluntary contributions (AVC) scheme for their members, the assets of which are invested separately from those of the Fund. The Fund has appointed Standard Life and Prudential as their AVC providers. AVCs are paid to the AVC providers by employers and are specifically for providing additional benefits for individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and the movements in the year.

In accordance with regulation 5(2)(b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 1998, AVCs are not included in pension fund financial statements. Details of contributions paid and the total value of funds invested are disclosed by way of note.

p) Contingent assets and contingent liabilities

A contingent liability arises where an event has taken place prior to the year-end giving rise to a possible financial obligation whose existence will only be confirmed or otherwise by the occurrence of future events. Contingent liabilities can also arise in circumstances where a provision would be made, except that it is not possible at the balance sheet date to measure the value of the financial obligation reliably.

A contingent asset arises where an event has taken place giving rise to a possible asset whose existence will only be confirmed or otherwise by the occurrence of future events.

Contingent assets and liabilities are not recognised in the Net Assets Statement but are disclosed by way of narrative in the notes.

q) Employee benefits

The employees of LPFE are eligible to participate in Lothian Pension Fund.

In the Consolidated Financial Statements, the current service cost for the period is charged to the Fund Account. The assets of Lothian Pension Fund are held separately from those of the Company. The Company has fully adopted the accounting principles as required by IAS19 – Employee Benefits.

The liability recognised in the Net Asset Statement in respect of the defined benefit pension plan is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs.

The defined benefit obligation is calculated annually, by the Scheme Actuary, using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in a currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to the Fund Account in the period in which they arise.

Past-service costs are recognised immediately in the Fund Account, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

3 Accounting Standards that have been issued but not yet adopted

The Code requires the disclosure of information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted. This applies to the adoption of the following new or amended standards within the 2019/20 Code:

The Code requires implementation from 1 April 2019 and there is therefore no impact on the 2018/19 financial statements.

- Amendments to IAS 40 Investment Property: Transfers to Investment Property
- Annual Improvements to IFRS Standards 2014-2016 Cycle
- IFRIC 22 Foreign Currency Transactions and Advance Consideration
- IFIRC 23 Uncertainty over Income Tax Treatments
- Amendments to IAS 9 Financial Instruments

The amendments are generally minor or principally providing clarification. Overall, these new or amended standards are not expected to have a significant impact on the financial statements.

4 Critical judgements in applying accounting policies

Unquoted private equity and infrastructure investments

It is important to recognise the highly subjective nature of determining the fair value of private equity and infrastructure investments.

They are inherently based on forward-looking estimates and judgements involving many factors. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of IFRS.

For the Lothian Pension Fund, the value of unquoted private equity, infrastructure, timber and secured loan investments at 31 March 2019 was £1,250.0m (2018 £1,125.1m).

Actuarial present value of promised retirement benefits

Each Fund is required to disclose the estimated actuarial present value of promised retirement benefits as at the end of the financial year. These estimates are prepared by the Fund Actuary. These values are calculated in line with International Accounting Standard 19 (IAS19) assumptions and comply with the requirements of IAS26. However, the results are subject to significant variances based on changes to the underlying assumptions.

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

5 Assumptions made about the future and other major sources of estimation uncertainty

The Financial Statements contain estimated figures that are based on assumptions made by the Council; private equity and infrastructure managers; other providers of valuation information; and the Scheme Actuary about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because amounts cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

The items in the Net Assets Statement at 31 March 2019 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

a) Actuarial present value of promised retirement benefits

Uncertainties

Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on the Fund's assets. The Fund Actuary advises on the assumptions to be applied and prepares the estimates.

Effect if actual results differ from assumptions - Lothian Pension Fund

The effects on the net pension liability of changes in individual assumptions can be illustrated as follows:

Change in assumptions - year ended 31 March 2019	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in the real discount rate	11	1,017
1 year increase in member life expectancy	4	330
0.5% increase in salary increase rate	2	166
0.5% increase in pensions increase rate	8	782

Effect if actual results differ from assumptions - Scottish Homes Pension Fund

The effects on the net pension liability of changes in individual assumptions can be illustrated as follows:

Change in assumptions - year ended 31 March 2019	Approx % increase in liabilities %	Approx monetary amount £m
0.5% decrease in the real discount rate	5	7
1 year increase in member life expectancy	4	6
0.5% increase in pensions increase rate	5	7

b) Valuation of unquoted private equity and infrastructure investments

Uncertainties

These investments are not publicly listed and therefore there is a degree of estimation involved in their valuation, see 2j above for more details on the valuation methodology.

Effect if actual results differ from assumptions

There is a risk that these investments may be under or overstated in the accounts at any point in time. The actual financial return of this type of investment is only known with certainty when they reach the end of their lifecycles and the final distributions are made to investors. A sensitivity analysis can be found in note 2j above.

c) Quantifying the cost of investment fees deducted from capital

Uncertainties

Section 2 h) describes the accounting policy for investment management expenses in relation to expenses deducted from the capital value of investments. Quantification of these costs involves asking the relevant managers for information and only some of this information can be independently verified. In cases where the charges relate to an investment as a whole, an estimate needs to be made of the costs applicable to the holding owned by the relevant Fund.

Effect if actual results differ from assumptions

There is a risk that the cost of investment fees deducted from capital may be under or overstated. However, as the costs are included in the Fund Account by adjusting the change in market value of investments, any inaccuracy in the cost estimate will not change the reported net change in the Fund for the year.

Statement of responsibilities for the Annual Accounts

The responsibilities of the Administering Authority

The Administering Authority's responsibilities require it to:

- Make arrangements for the proper administration of the financial affairs of the Fund in its charge and to secure that one of its officers has the responsibility for the administration of those affairs. The Head of Finance serves as the Section 95 Officer for all the Council's accounting arrangements, including those of Lothian Pension Fund and Scottish Homes Pension Fund. For the Fund, this Section 95 responsibility has been delegated to the Chief Finance Officer, Lothian Pension Fund.
- Manage its affairs to secure economic, efficient and effective use of its resources and safeguard its assets.
- Ensure the Annual Accounts are prepared in accordance with legislation (The Local Authority Accounts (Scotland) Regulations 2014) and, so far as is compatible with that legislation, in accordance with proper accounting practices (section 12 of the Local Government in Scotland Act 2003).
- Approve the Audited Annual Accounts for signature.

HUGH DUNN
Head of Finance
The City of Edinburgh Council
25 September 2019

The responsibilities of the Chief Finance Officer, Lothian Pension Fund

The Chief Finance Officer, Lothian Pension Fund, is responsible for the preparation of the Fund's Financial Statements which, in terms of the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 (the Code of Practice), is required to present a true and fair view of the financial position of the Fund at the accounting date and their income and expenditure for the year (ended 31 March 2019).

In preparing this statement of accounts, the Chief Finance Officer, Lothian Pension Fund, has:

- Selected suitable accounting policies and then applied them consistently
- Made judgements and estimates that were reasonable and prudent
- Complied with the Code of Practice.

The Chief Finance Officer, Lothian Pension Fund, has also:

- Kept proper accounting records which were up to date
- Taken reasonable steps for the prevention and detection of fraud and other irregularities.

The Statement of Accounts presents a true and fair view of the financial position of the Fund as at 31 March 2019, and their income and expenditure for the year ended 31 March 2019.

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

Independent auditor's report

to the members of City of Edinburgh Council as administering authority for Lothian Pension Fund and Scottish Homes Pension Fund and the Accounts Commission

Report on the audit of the financial statements

Opinion on financial statements

We certify that we have audited the financial statements in the annual report of Lothian Pension Fund and its group and Scottish Homes Pension Fund (the funds) for the year ended 31 March 2019 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Lothian Pension Fund Fund Account, the Lothian Pension Fund Net Assets Statement, the Scottish Homes Pension Fund Fund Account, the Scottish Homes Pension Fund Net Assets Statement and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 (the 2018/19 Code).

In our opinion the accompanying financial statements:

- give a true and fair view in accordance with applicable law and the 2018/19 Code of the financial transactions of the funds during the year ended 31 March 2019 and of the amount and disposition at that date of their assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2018/19 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Basis for opinion

We conducted our audit in accordance with applicable law and International Standards on Auditing (UK) (ISAs (UK)) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report. We were appointed by the Accounts Commission on 31 May 2016. The period of total uninterrupted appointment is three years. We are independent of the funds in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. Non-audit services prohibited by the Ethical Standard were not provided to the council. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern basis of accounting

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Chief Finance Officer has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the funds' ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Risks of material misstatement

We have reported in a separate Annual Audit Report, which is available from the Audit Scotland website, the most significant assessed risks of material misstatement that we identified and our conclusions thereon.

Responsibilities of the Chief Finance Officer and the City of Edinburgh Council for the financial statements

As explained more fully in the Statement of Responsibilities for the Annual Accounts, the Chief Finance Officer is responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Chief Finance Officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Chief Finance Officer is responsible for assessing the funds' ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless deemed inappropriate.

The City of Edinburgh Council is responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of the auditor's responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Other information in the annual report

The Chief Finance Officer is responsible for the other information in the annual report. The other information comprises the information other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except on matters prescribed by the Accounts Commission to the extent explicitly stated later in this report.

In connection with our audit of the financial statements, our responsibility is to read all the other information in the annual report and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Report on other requirements

Opinions on matters prescribed by the Accounts Commission

In our opinion, the audited part of the Remuneration Report has been properly prepared in accordance with The Local Authority Accounts (Scotland) Regulations 2014.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with statutory guidance issued under the Local Government in Scotland Act 2003;
- the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016); and
- the information given in the Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations 2018.

Matters on which we are required to report by exception

We are required by the Accounts Commission to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Conclusions on wider scope responsibilities

In addition to our responsibilities for the annual accounts, our conclusions on the wider scope responsibilities specified in the Code of Audit Practice, including those in respect of Best Value, are set out in our Annual Audit Report.

Use of our report

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 120 of the Code of Audit Practice, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Nick Bennett (for and on behalf of Scott-Moncrieff Audit Services)
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL
25 September 2019

Annual Governance Statement

Roles and responsibilities

The City of Edinburgh Council (the Council) has statutory responsibility for the administration of the Local Government Pension Scheme (LGPS) in the Lothian area of Scotland. This responsibility is for two separate funds: the Lothian Pension Fund and Scottish Homes Pension Fund (the Fund). The Lothian Pension Fund group comprises the investment and pensions team employed by LPFE Limited (LPFE) supporting the Council in its separate statutory capacity as the administering authority of the Fund (Administering Authority) and LPFI Limited (LPFI), the Group's regulated investment vehicle (together the LPF Group).

The main functions of the Administering Authority are administration of scheme benefits and the investment of the assets of the Fund. These functions are conducted in accordance with the Local Government Pension Scheme (Scotland) Regulations which are statutory instruments made under the Superannuation Act 1972. The role of Administering Authority is carried out via:

- the Pensions Committee and the Pensions Audit Sub-Committee
- the Pension Board
- the Joint Investment Strategy Panel; and
- the LPF Group.

Further details on the above arrangements can be found in the Governance section of the Management Commentary towards the front of this document.

Scope of responsibility

As the Administering Authority of the Fund, the Council is responsible for ensuring that its business in administering the Fund, is conducted in accordance with the law and appropriate standards, and that monies are safeguarded, properly accounted for, and used economically, efficiently and effectively. The Council also has a statutory duty under the Local Government in Scotland Act 2003, to make arrangements to secure best value, which is defined as continuous improvement in the way its functions are carried out.

In discharging these overall responsibilities, elected members, senior officers and external representatives are responsible for implementing effective arrangements for governing the affairs of the LPF Group, and facilitating the effective exercise of its functions, including arrangements for the management of risk. The Pensions Committee oversees the operational administration of the Fund by the LPF Group.

The LPF Group has adopted a Local Code of Corporate Governance that is consistent with the principles of the Chartered Institute of Public Finance and Accountancy (CIPFA) and Society of Local Authority Chief Executives (SOLACE) framework 'Delivering Good Governance in Local Government'.
This statement explains how the LPF Group has complied with the Local Code of Corporate Governance and how it meets the CIPFA Code of Practice on Local Authority Accounting in the United Kingdom.

The governance framework

The LPF Group operates within the wider governance framework of the Council but within specific ringfenced governance structures focused on the Fund themselves. The governance framework comprises the systems, controls, processes, cultures and values by which the LPF Group directs and controls the Fund. It also describes the way the LPF Group engages with and accounts to its stakeholders in relation to the management of the administration of the Fund. It enables the LPF Group to monitor the achievement of its objectives and consider whether those objectives have led to the delivery of appropriate, cost-effective services. The framework also applies to any subsidiary companies which are members of the LPF Group, namely LPFI and LPFE. The LPF Group is also directly regulated by The Pensions Regulator, the Financial Conduct Authority (regarding its regulated investment activity), the Scottish Information Commissioner and is subject to other corporate and public sector rules and regulations.

The LPF Group's ongoing compliance with its governance framework and regulatory obligations is monitored on an ongoing basis by the Pensions Committee, the Audit Sub-Committee and the Pension Board and the respective boards of LPFI and LPFE.

The wider Council's Local Code of Corporate Governance is regularly reviewed and considered by the Governance, Risk & Best Value Committee. It has implemented arrangements for monitoring each element of the framework and providing evidence of compliance. The Council's Democracy, Governance and Resilience Senior Manager reviewed the arrangements and is satisfied that the Code continues to be adequate and effective. Internal Audit has also reviewed the annual assurance questionnaire process in relation to Arms-Length Companies and has found that this provides the Chief Executive Officer with a level of assurance on the adequacy of the governance arrangements. The Council's Corporate governance framework meets the principles of effective governance.

The LPF Group places reliance upon certain of the internal financial controls within the Council's financial systems and the monitoring in place to ensure the effectiveness of these controls. The relevant key elements of the LPF Group and the Fund governance framework within the Council, include:

- Identifying the objectives of the Fund in the Funding Strategy Statement, Statement of Investment Principles, Pension Administration Strategy and Service Plan.
- Since April 2015, The Pensions Regulator has been responsible for setting standards of governance and administration for the Local Government Pension Scheme. The LPF Group has taken steps to fully integrate compliance with these standards within the overall governance framework.
- A systematic approach to monitoring service performance by the Pensions Committee, Pensions Audit Sub-Committee, Pension Board (each including external stakeholder representation), Independent Professional Observer and senior officers.
- A structured programme to ensure that Pensions Committee and Pension Board members have the required standard of knowledge and understanding of Local Government Pension Scheme matters.
- Operating within clearly established investment guidelines defined by the Local Government Pension Scheme Investment Regulations and the Fund's Statement of Investment Principles.

- Compliance with the CIPFA Principles for Investment Decision Making and Disclosure in the Local Government Pension Scheme.
- With the exception of managed funds, unlisted investments and property, all investments are held under custody by a global custodian. The Fund benefits from the custodian's extensive internal control framework.
- Benchmarking of services in terms of standards and cost against other pension funds.
- LPFE and LPFI operating within their respective constitutional documentation and the relevant companies regulations.
- LPFI operating within the relevant governance policies and procedures to ensure compliance with the Financial Conduct Authority's rules, regulations and guidance.
- For LPF Group and Fund matters, the Pensions Committee, Pensions Audit Sub-Committee and Pension Board are responsible for scrutiny and challenge and a quarterly risk reporting process is in place to ensure full consideration of such matters.
- Officers of the LPF Group are managed separately through the processes and procedures of LPFE, overseen by its board of directors, with terms and conditions and a human resources performance review and management strategy tailored to the express needs of the Fund and their stakeholders.
- The directors of LPFE and LPFI have obligations to report to the Pensions Committee as the governing body for the Fund and Council in being the sole shareholder. In addition, the board and staff of LPFI are each individually regulated by the Financial Conduct Authority and so bound by the associated Principles and Standards of governance best practice.

Elements of the governance framework of the Council that are relevant to the LPF Group and Fund include:

- The Council is embedding a culture of commercial excellence to ensure that its services always deliver Best Value. That is ongoing and seeks to improve standards in buying practices and processes across the Council including, to the extent applicable, the LPF Group and the Fund which bear the cost of its operation and administration
- The submission of reports, findings and recommendations from the external auditor, other inspectorates and internal audit, to the Pensions Committee, Pensions Audit Sub-Committee for all matters affecting the LPF Group and Fund and, in certain circumstances strictly for Council wide oversight purposes, the Corporate Leadership Team, Governance, Risk and Best Value Committee and wider Council.
- The roles and responsibilities of Elected Members and Officers are defined in Procedural Standing Orders, Committee Terms of Reference and Delegated Functions, Contract Standing Orders, Scheme of Delegation to Officers, the Member/officer protocol and Financial Regulations. These are subject to annual review.
- The Chief Executive Officer has overall accountability to Council, for all aspects of operational management and overall responsibility for ensuring the continued development and improvement of systems and processes concerned with ensuring appropriate direction, accountability and control.
- The Section 95 Officer has overall responsibility for ensuring appropriate advice is given to the Council and the LPF Group on all financial matters, keeping proper financial records of accounts and maintaining an effective system of internal financial control. For the Fund, the Section 95 officer responsibility has been sub-delegated to the Chief Finance Officer of the LPF Group.

- The Chief Internal Auditor has overall responsibility to review, appraise and report to management and the Governance, Risk and Best Value Committee, and for matters relating to the LPF Group and Fund to the Pensions Committee and Pensions Audit Sub-Committee, on the adequacy of relevant internal control and corporate governance arrangements and on risks relating to approved policies, programmes and projects.
- The Council's Democracy, Governance and Resilience Manager, reporting to the Head of Strategy and Communications, has responsibility for advising the Council on corporate governance arrangements and supports the LPF Group on certain aspects of its governance arrangements.
- The Governance, Risk and Best Value Committee, and for LPF Group and Fund matters the Pensions Committee and Pensions Audit Sub-Committee, provides the Council with independent assurance of the adequacy of the governance and risk management frameworks and internal control environment. Also providing independent scrutiny of financial and non-financial performance, approving and monitoring the progress of the Internal Audit risk-based plan, and monitoring performance of the internal audit service.
- The risk management policy and framework set out the responsibilities of elected members, Governance, Risk and Best Value Committee, and for LPF Group and Fund matters the Pensions Committee and Pensions Audit Sub-Committee, management and staff for the identification and management of risks to corporate and service related priorities;
    - The Resources and Chief Executive's Risk Register and Council Risk Register all identify risks and proposed treatment and actions. These registers are regularly reviewed, updated and reported to the Corporate Leadership Team, which reviews Council-wide risk and reports to the Governance, Risk and Best Value Committee for scrutiny and challenge.
    - Resilience and business continuity plans are in place for all essential Council services. These set out arrangements for continuing to deliver essential services in the event of an emergency or other disruption.
    - Senior management and Heads of Service have formal objectives, with performance reviewed by the appropriate chief officer. Officers have personal work objectives and receive feedback on their performance through the Council-wide performance review and development process.
    - An Elected Members remuneration and expenses scheme is in place and is consistent with the Scottish Government's 'Councillors Remuneration: allowances and expenses – Guidance'. Information on the amounts and composition of elected members salaries, allowances and expenses is published on the Council's website.
    - The Council's Democracy, Governance and Resilience Senior Manager ensures that induction training on roles and responsibilities, and ongoing development opportunities, are provided for Elected Members. A separate policy on Pensions Committee and Pension Board member training has been adopted and is overseen by the LPF Group's officers.
    - Mandatory training for Councillors newly appointed to the Pensions Committee is programmed within the Induction and Training programme for Elected Members. This focuses on governance, investment management and strategy and how the LPF Group and Fund work. Committee members are reminded of the requirement to undertake a minimum of 21 hours of training per financial year to fulfil their role on the Pensions Committee.
    - Codes of Conduct, that set out the standards of behaviour expected from Elected Members and officers, are in place.

- The Employee Code of Conduct, Anti Bribery Policy and Policy on Fraud Prevention set out the responsibilities of officers and Elected Members in relation to fraud and corruption, and are reinforced by the Councillors' Code of Conduct, the Code of Ethical Standards and the Financial Regulations. The LPF Group has adapted policies to take into account the specific nature of its business and regulation.
- The Whistleblowing policy provides a process for disclosure in the public interest about the Council and its activities by officers, Elected Members and others. The LPF Group has an adapted policy to take into account the specific nature of its business and regulation.
- A Register of Members' Interests and Registers of Officers' interests are maintained and available for public inspection.

A significant element of the governance framework is the system of internal controls, which is based on an ongoing process to identify and prioritise risks to the achievement of the Council's objectives, including those relevant to the LPG Group and Fund. Following the establishment of the wholly-owned subsidiary companies, LPFE and LPFI, the Council continues to have appropriate assurance processes and procedures in relation to the responsible officers involved in the administration of those companies and so the wider LPF Group administering the Fund.

Review of Effectiveness

The Local Code of Governance details the Council's arrangements for monitoring each element of the framework and providing evidence of compliance. The Council's Governance and Democratic Services Manager has reviewed the effectiveness of the Code.

The Chief Internal Auditor has also provided an assurance statement on the effectiveness of the system of internal control. The opinion in the assurance statement states: "Internal Audit considers that the LPF control environment and governance and risk management frameworks are generally adequate but with enhancements required and is therefore reporting a 'amber' rated opinion, with our assessment towards the middle of this category."

In compliance with standard accounting practice, the Head of Finance, of the City of Edinburgh Council has provided the Chief Executive Officer with a statement of the effectiveness of the Group's internal financial control system for the year ended 31st March 2019. It is the Head of Finance's opinion that "… that although a degree of assurance can be placed upon the adequacy and effectiveness of the Group's systems of internal financial control, further improvements, including embedding of actions taken in response to previous recommendations, are still required.

In this context, I would particularly highlight improvements in train to address a number of systemic weaknesses in respect of payroll-related controls, including those to address historic, and prevent recurring, overpayments."

The Chief Finance Officer of the LPF Group has provided a statement of the effectiveness of the internal financial control system for the year ended 31st March 2019 for the Fund. It is the Chief Finance Officer's opinion "that reasonable assurance can be placed upon the adequacy and effectiveness of the system of internal financial control for the LPF Group in administering the Lothian Pension Fund and Scottish Homes Pension Fund".

Certification

It is our opinion, in light of the foregoing, that reasonable assurance can be placed upon the adequacy and effectiveness of the systems of governance that operate within the LPF Group in its administration of the Fund. We consider the governance and internal control environment operating during the financial year from 1 April 2017 to 31 March 2019 to provide reasonable and objective assurance that any significant risks impacting on the LPF Group and its ability to achieve its objectives in properly administering the Fund have and will continue to be identified and suitably proportionate actions have and will be taken to avoid or mitigate the impact of any such risks.

The LPF Group has identified certain key areas for improvement, summarised as follows:

- ICT: Continuing to engage with ICT service provider and the City of Edinburgh Council to monitor and drive improvements in the ICT services which the LPF Group receives, whilst in tandem continuing to assess the position around the LPF Group procuring a separate ICT provider to solely and independently service its specific ICT requirements in support of its strategic business plan.
- Human resources: To continue to implement the new human resources strategy specific to LPF Group's requirements.
- Pension Board: To ensure that vacancies in the Pension Board are filled timeously and by suitable candidates and that this body of external stakeholder representatives receives the training and support that it requires on an ongoing basis.
- Business continuity: To continue to assess and refresh the business continuity plan on an ongoing basis ensuring sufficient engagement with staff.
- Information governance: Having completed a full information governance compliance project prior to the implementation of new data protection laws on 25 May 2018, to continue to implement ongoing actions to ensure continuing best practice information governance and security within the LPF Group, including monitoring and engaging with third party suppliers where appropriate.
- Financial services regulatory compliance: To continue to instruct external compliance audits on the operations and governance of LPFI in order to ensure best practice compliance and assurance around its existing operations (and in preparation for its extended collaborative business model) and take action to address the recommendations from those audits on an ongoing basis.
- Wider governance: To continue to maintain and reinforce separate governance and controls specific to the needs of the LPF Group, the pensions funds it administers and its distinct duties to employer and member stakeholders; consistently throughout the LPF Group's governance structures. To ensure that oversight by the City of Edinburgh Council is supported in a manner consistent with these duties.

The LPF Group will continue to ensure that these are treated as a priority and that progress towards implementation will be reviewed through the governance structures and processes established for the LPF Group and summarised herein.

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

DR STEPHEN S MOIR
Executive Director of Resources
The City of Edinburgh Council
25 September 2019

DOUG HERON
Chief Executive Officer
Lothian Pension Fund
25 September 2019

Governance Compliance Statement

The Regulations that govern the management of Local Government Pension Scheme in Scotland require that a Governance Compliance Statement is published. This statement sets out the extent to which governance arrangements comply with best practice.

The statement below describes arrangements at 31 March 2019 and over the financial year.

Principle		Full Compliance	Comments
Structure	The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing Council.	Yes	The City of Edinburgh Council acts as administering authority and delegates all pension scheme matters to a committee of seven members (Pensions Committee) made up as follows: - Five City of Edinburgh Council elected members - Two external members, one drawn from the membership of the Fund and one drawn from the employers that participate in the Fund.
	That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.	Yes	The Pensions Committee includes two external places for pension fund stakeholders i.e. one each from the employer and member representatives. Fund members and employers are also represented within the Fund's Pension Board. Membership includes five employer representatives and five member representatives. All members of the Pension Board are invited to attend the meeting of the Pensions Committee and receive the relevant papers prior to those meetings. Two members of the Pension Board attend the Pensions Audit Sub-Committee.

Principle		Full Compliance	Comments
Structure	That where a secondary committee or board has been established, the structure ensures effective communication across both levels.	Yes	The Pensions Audit Sub-Committee, consisting of three members of the Pensions Committee, report to the Pensions Committee on their findings and recommendations. Two members of the Pension Board attend the Pensions Audit Sub-Committee in a non-voting capacity. The Pension Board attends the Pensions Committee meetings and takes part in training events. Implementation of investment strategy is delegated to the Executive Director of Resources who then delegates to the Head of Finance, who takes advice from the Joint Investment Strategy Panel. The Panel meets quarterly and reports to the Pensions Committee annually. The advisers on the Joint Investment Strategy Panel consists of the Chief Investment Officer and on other portfolio manager of LPFI plus two experienced independent external industry advisers. The Pensions Committee receives annual updates from LPFE and LPFI.
Representation	That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include employing authorities (including non-scheme employers, e.g. admitted bodies) and scheme members (including deferred and pensioner scheme members).	Yes	The Pension Board consists of a mix of representatives: - Five employer representatives from non-administering authority employers; - Five member representatives appointed by the Trade Unions in accordance with the approach required under Scottish statute.
	Where appropriate, independent professional observers, and expert advisers (on an ad-hoc basis).	Yes	An Independent Professional Observer was appointed in March 2013 to help Committee scrutinise advice. This contract expired in February 2018 and a new Observer was appointed in September 2018.

Principle		Full Compliance	Comments
Representation	Where appropriate, independent professional observers, and expert advisers (on an ad-hoc basis).	Yes	As mentioned previously, external investment advisers sit on the Joint Investment Strategy Panel. A separate specialist Pensions Audit Sub-Committee consisting of three members (including at least two elected members from the City of Edinburgh Council) undertake the audit scrutiny of the funds. A non-executive director was appointed to the board of LPFI on 7 February 2017 and LPFE on 19 March 2018. An external compliance consultant supports the LPF Group on its ongoing compliance with the Financial Conduct Authority rules, regulations and guidance.
	That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision-making process, with or without voting rights.	Yes	The Pension Board attends the Pensions Committee meetings to help ensure that the operation of the pension funds is in accordance with the applicable law and regulation. The Pension Board takes part in all Committee training events. The Pensions Committee takes account of the views of the Pension Board when making decisions.
Selection and Role of Lay Members	That committee or board members are made fully aware of the status, role and function that they are required to perform on either a main or secondary committee.	Yes	A comprehensive training programme including induction is in place. Members of the Pensions Committee and Pension Board are expected to attend no less than three days of training (21 hours) per year. The non-elected members confirm that they have read, signed and will abide by a Code of Conduct (specifically tailored for the Pensions Committee and Pension Board) prior to their appointment to those bodies. The elected members are required to read, sign and abide by the Councillors' Code of Conduct.

Principle		Full Compliance	Comments
Selection and Role of Lay Members	That at the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.	Yes	The declaration of members' interests is a standard item on the agenda for meetings of the Pensions Committee, Pensions Audit Sub-Committee and Pension Board. A Code of Conduct also applies to all members of the Pensions Committee and the Pension Board. The declaration of board members interest is a standard item on the agenda for the meetings for the LPFE and LPFI board meetings.
Voting	The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees.	Yes	Five of the seven places of the Pensions Committee are held by elected members of the City of Edinburgh Council, which is required to retain a 2/3 majority in line with the Local Government (Scotland) Act 1973. The LPF Group's Nomination and Appointments Policy clearly documents how employer and member representatives will be elected to the Pensions Committee and Pension Board. LPFI and LPFE board members conduct meetings and other matters in accordance with their respective articles of association and shareholders' agreements.
Training / Facility Time / Expenses	a) That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process.	Yes	A Training and Attendance Policy is in place covering training requirements and reimbursement of expenses. The policy is available on the LPF Group's website www.lpf.org.uk. Board members and staff working for LPFI and LPFE also attend separate training for the purposes of their knowledge, understanding and (where appropriate) compliance with Financial Conduct Authority regulations.
	b) That where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	Yes	The Training and Attendance Policy applies to both the Pensions Committee and the Pension Board. Advisers have their own professional development obligations.

Principle		Full Compliance	Comments
Training / Facility Time / Expenses	c) That the administering authority considers the adoption of annual training plans for committee and board members and maintains a log of all such training.	Yes	Each Pensions Committee and Pension Board member is expected to attend no less than three days training per year (21 hours) per year. Attendance at meetings and training is monitored and reported.
Meetings frequency	a) That an administering authority's main committee or committees meet at least quarterly.	Yes	The Pensions Committee meets at least four times a year.
	b) That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committees sits.	Yes	The Pensions Audit Sub-Committee is held before the Pensions Committee at least three times a year with further meetings held if necessary. The Joint Investment Strategy Panel meets quarterly or more frequently as required. The Pension Board attends all the Pensions Committee meetings and separately meets in advance of such meetings. Further meetings are held if necessary. The LPFE board now meet five time a year (in February, May, August, October and December) and the LPFI board at least quarterly.
	c) That an administering authority who does not include lay members in their formal governance arrangements must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	Not applicable	
Access	That subject to any rules in the council's constitution, all members of main and secondary committees or boards have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	Yes	Pensions Committee papers and minutes are publicly available on the Council's website and all Pensions Committee and Pension Board members have equal access. Members of the Pensions Committee and Pension Board have equal access to the Independent Professional Observer who holds surgeries ahead of Committee meetings.

Principle		Full Compliance	Comments
Scope	That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Yes	The Pensions Committee deals with all matters relating to both the administration and investment of the Fund and the LPF Group. A separate specialist Pensions Audit Sub-Committee consisting of three members (including at least two elected members from the City of Edinburgh Council) undertake the audit scrutiny of the Fund.
Publicity	That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express an interest in wanting to be part of those arrangements.	Yes	Governance documents, policies and details of Pension Board membership are on the LPF Group's website. The LPF Group also communicates regularly with employers and scheme members.

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

DR STEPHEN S MOIR
Executive Director of Resources
The City of Edinburgh Council
25 September 2019

DOUG HERON
Chief Executive Officer
Lothian Pension Fund
25 September 2019

REMUNERATION REPORT

Remuneration Policy for Employees

Officers and employees of Lothian Pension Fund are employed by LPFE, an arms-length organisation owned by the City of Edinburgh Council, the administering authority for the Lothian Pension Fund. In recent years LPFE has been incorporated as a standalone entity to allow the Fund to compete with private sector investment management firms for recruitment and retention of skilled and experienced investment managers and analysts.

Operating this model allows Lothian Pension Fund to achieve significantly lower costs, and therefore improved net returns or lower investment risk, than would be possible by appointing private sector asset managers to invest the Fund's assets. The LPFE Board acts as a Remuneration Committee for officers and employees determining pay arrangements based on comparison to well-researched market benchmarks and performance against pre-agreed performance targets, and always linked to the principle of delivering value-for-money for the members of the Fund and their sponsoring employers.

Each year the Fund participates in a range of benchmarking exercises to measure operating costs and net investment returns against peers and indices relevant to the investment strategy, and this information is reported to the oversight bodies who review pay arrangements and terms of appointments of officers. Pay arrangements in LPFE reflect the market for investment expertise and recognise the qualifications and experience levels required to perform the roles and, more fundamentally, represent value-for-money for employee members and their sponsoring employers who bear the costs of operating the pension fund and securing retirement benefits.

Number of Employees by Pay Band

The numbers of employees whose remuneration during the year exceeded £50,000 were as follows:

Remuneration Bands	2017/18	2018/19	Remuneration Bands	2017/18	2018/19
£50,000 - £54,999	1	1	£95,000 - £99,999	1	1
£55,000 - £59,999	3	3	£100,000 - £104,999	1	2
£60,000 - £64,999	1	1	£105,000 - £109,999	-	2
£65,000 - £69,999	1	-	£110,000 - £114,999	-	-
£70,000 - £74,999	2	-	£115,000 - £119,999	-	-
£75,000 - £79,999	2	1	£120,000 - £124,999	-	-
£80,000 - £84,999	1	1	£125,000 - £129,999	-	1
£85,000 - £89,999	3	-	£130,000 - £134,999	-	4
£90,000 - £94,999	-	-			
			Total No. of Employees	16	17

During the year, the company introduced three variable pay schemes, two of which have vesting periods. The Portfolio Manager and Senior Management schemes entitle staff to receive an assessed percentage of their salary as an additional variable pay award if they meet certain objectives during the year. The assessment year runs from 1 February 2018 to 31 January 2019. The award then vests over three years.

The first part is payable at the end of the first year if the objectives are met and the remaining two parts are payable in the following two years if the requirement that the employee is still employed by the company at such time is met. Payment one has been made in January 2019. A liability has been raised at 31 March 2019 for the 2 months of service which the employees have delivered with regards to the second and third payments in the scheme.

Senior Employees Remuneration

The remuneration paid to the Fund's senior employees is as follows:

	Total Remuneration 2017/18	Salary, Fees and Allowances	Variable Remuneration	Total Remuneration 2018/19
Name and Post Title	**£000**	**£000**	**£000**	**£000**
Doug Heron, Chief Executive Officer (from February 2019)*	-	18	-	18
Clare Scott, Chief Executive Officer (to December 2018)**	101	80	-	80
Bruce Miller, Chief Investment Officer	96	106	26	132
John Burns, Chief Finance Officer	76	82	20	102
Struan Fairbairn, Chief Risk Officer (Head of Legal, Risk and Compliance)	76	81	19	100
	349	**367**	**65**	**432**

* Full time equivalent for 2018/19 £108,000

** Full time equivalent for 2018/19 £108,000

The senior employees detailed above have responsibility for management of the LPF group to the extent that they have power to direct or control the major activities of the group (including activities involving the expenditure of money), during the year to which the Remuneration Report relates, whether solely or collectively with other persons.

Senior officers of the City of Edinburgh Council are also fully remunerated via the Council and no additional remuneration is paid by the Fund. This remuneration is disclosed in the Financial Statements of the City of Edinburgh Council.

Senior Employees Pension Entitlement

Pension benefits for employees are provided through the Local Government Pension Scheme.

For employees the Local Government Pension Scheme became a career average pay scheme on 1 April 2015. Benefits built up to 31 March 2015 are protected and based on final salary. Accrued benefits from 1 April 2015 will be based on career average salary.

The Scheme's normal retirement age for employees is linked to the State Pension Age (with a minimum of age 65).

From 1 April 2009, a five-tier contribution system was introduced with contributions from Scheme members being based on how much pay falls into each tier. This is designed to give more equality between the cost and benefits of scheme membership. Prior to 2009, contributions rates were set at 6% for all non-manual employees.

The tiers and members' contribution rates for 2018/19 were as follows:

Pensionable Pay (2018/2019)	Rate (%)
On earnings up to and including £21,300 (2017/2018 £20,700)	5.5%
On earnings above £21,300 and up to £26,100 (2017/2018 £20,700 to £25,300)	7.25%
On earnings above £26,100 and up to £35,700 (2017/2018 £25,300 to £34,700)	8.5%
On earnings above £35,700 and up to £47,600 (2017/2018 £34,700 to £46,300)	9.5%
On earnings of £47,600 and above (2017/2018 £46,300)	12%

If a person works part-time, their contribution rate is worked out on the whole-time pay rate for the job, with actual contributions paid on actual pay earned.

There is no automatic entitlement to a lump sum. Members may opt to give up (commute) pension for lump sum up to the limit set by the Finance Act 2004.

The value of the accrued benefits has been calculated on the basis of the age at which the person will first become entitled to receive a pension on retirement without reduction on account of its payment at that age; without exercising any option to commute pension entitlement into a lump sum; and without any adjustment for the effects of future inflation.

The pension figures shown relate to the benefits that the person has accrued as consequence of their total local government service, and not just their current appointment.

The pension entitlement of the LPF Group's senior employees is as follows:

	In-year Pension Contributions			Accrued Pension Benefits	
	2017/18	2018/19		As at 31 March 2019	Increase from 31 March 2018
Name and post title	**£000**	**£000**		**£000**	**£000**
Doug Heron, Chief Executive Officer (from February 2019)	-	4	Pension	-	-
			Lump Sum	-	-
Clare Scott, Chief Executive Officer (to December 2018)	21	19	Pension	23	3
			Lump Sum	14	1
Bruce Miller, Chief Investment Officer	20	27	Pension	29	7
			Lump Sum	28	7
John Burns, Chief Finance Officer	16	21	Pension	41	7
			Lump Sum	78	12
Struan Fairbairn, Chief Risk Officer (Head of Legal, Risk and Compliance)	16	21	Pension	10	2
			Lump Sum	-	-
Total	**73**	**92**			

Exit Packages

Exit packages include compulsory and voluntary redundancy costs, pension contributions in respect of added years, ex-gratia payments and other departure costs. There was no payment of any exit packages in 2018/19 or in the previous year.

All information disclosed in the above tables at paragraphs in this Remuneration Report has been audited.
The other sections of the Remuneration Report have been reviewed by the appointed auditor to ensure that they are consistent with the annual accounts.

Remuneration for Councillors on the Pensions Committee

Councillors on the Pensions Committee are remunerated by the City of Edinburgh Council, no additional remuneration is paid by the Fund.

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

DR STEPHEN S MOIR
Executive Director of Resources
The City of Edinburgh Council
25 September 2019

JOHN BURNS
Chief Finance Officer
Lothian Pension Fund
25 September 2019

Additional information

Key documents online

You can find further information on what we do and how we do it, on our website at www.lpf.org.uk. To view individual policy documents, click on the links below if viewing online or visit www.lpf.org.uk/publications.

- Actuarial Valuation reports
- Pension Board constitution
- Annual Report and Accounts
- Statement of Investment Principles
- Pension Administration Strategy
- Communications strategy
- Funding Strategy Statement
- Service Plan
- Training and attendance policy

Fund advisers

Actuaries:	Hymans Robertson LLP, Exchange Place One, 1 Semple Street, Edinburgh, EH3 8BL
Bankers:	Royal Bank of Scotland, 36 St Andrew Square, Edinburgh, EH2 2YB
Investment consultancy:	Gordon Bagot and Scott Jamieson
Investment custodians:	The Northern Trust Company, 50 Bank Street, Canary Wharf, London, E14 5NT
Investment managers:	Details can be found in the notes to the accounts.
Additional Voluntary Contributions (AVC) managers:	Standard Life, Standard Life House, 30 Lothian Road, Edinburgh, EH1 2DH Prudential plc, 1 Angel Court, London, EC2R 7AG
Property valuations:	CB Richard Ellis Limited, St Martin's Court, 10 Paternoster Row, London, EC4M 7HP
Solicitors:	Lothian Pension Fund In-house

Comments and suggestions

We appreciate your comments and suggestions on this report. Please let us know which sections you found useful and if you have any suggestions for items to be included in the future. Please email your comments to pensions@lpf.org.uk.

Accessibility

You can get this document on tape, in Braille, large print and various computer formats on request. Please contact the Interpretation and Translation Service (ITS) on 0131 242 8181 and quote reference number 00819. The ITS can also give information on community language translations.

Contact details

If you would like further information about Lothian Pension Fund and Scottish Home Pension Fund, please contact us the details on the back page if this report.

LOTHIAN PENSION FUND

pensions@lpf.org.uk

0131 529 4638

www.lpf.org.uk

Lothian Pension Fund, Atria One, 144 Morrison Street, Edinburgh EH3 8EX

LPFE Limited

Financial Statements

For the year ended 31 March 2019

Registered number SC497543

LPFE LIMITED

Financial statements

For the year ended 31 March 2019

Contents

LPFE LIMITED

Company information

Board of Directors:	***Chairman***
	Stephen Moir
	Executive Directors
	Hugh Dunn Alasdair Rankin Katy Miller Douglas Heron
	Non-executive Director
	Leslie Robb
Company Secretary:	Struan Fairbairn
Registered office	4th Floor Saltire Court 20 Castle Terrace Edinburgh Lothian EH1 2EN
Bankers:	The Royal Bank of Scotland plc
Auditor:	Scott-Moncrieff Chartered Accountants Exchange Place 3 Semple Street Edinburgh EH3 8BL

LPFE LIMITED

Directors' Report

For the year ended 31 March 2019

The directors present their report and audited financial statements for the year ending 31 March 2019.

Principal activity

The principal activity of the company is the provision of seconded staff to the City of Edinburgh Council acting in its capacity as the administering authority of the Lothian Pension Fund ("LPF") and LPFI Limited in support of the administration of the Lothian Pension Fund and the Scottish Homes Pension Fund ("the Funds") and separately (on a limited basis) to Falkirk Council in its capacity as the administering authority of the Falkirk Council Pension Fund. All pension funds are part of the Local Government Pension Scheme in Scotland (LGPS).

Results, dividends and mutual trading surplus

The loss for the year after tax was £306,388 (2018 - £1,535,060 loss) and after allowing for items included under "Other comprehensive income" a loss of £473,408 (2018 - £853,960 loss). The directors do not recommend payment of dividend.

The company's aim is to make a modest trading surplus before adjustments required under IFRS. After allowing for an addition to costs of £69,314 (2018 - £40,112) in respect of accrued holiday and variable pay and £326,000 (2018 - £1,536,000) for adjustments to pension costs under IAS19, the underlying trading profit is £88,926 (2018 - £41,052). The additional costs recognised under "Other comprehensive income" amounting to £167,020 (2018: £681,100 additional gains) all relates to further adjustments required by IAS19 and the related deferred tax.

Under the mutual trading agreement with LPF, the company is required to consider if any of the profit arising from the mutual trade can be returned to the Council. Although there was an underlying trading profit of £88,926 (2018: £41,052, Company Law requires that only "distributable profits" are available for distribution. The company's auditor has confirmed that the various adjustments required under IFRS must be taken into account when determining if profits are distributable. As a result, there are no distributable profits available for return to LPF in respect of the period.

Business review

The company is wholly owned by LPF and has entered into a shareholder agreement with LPF to appropriately address certain governance matters. The company also has a loan facility provided by LPF for the purpose of the provision of short-term working capital.

Staffing services are provided to LPF for the purposes of administering the Funds under an intra-group resourcing agreement. The agreement also provides for the running costs of the company to be covered as part of a service charge and the provision of staffing services to LPFI Limited (also wholly owned by LPF).

The company also has a secondment agreement with Falkirk Council to provide legal staff to assist with certain aspects of the administration of the Falkirk Council Pension Fund as part of a mutually beneficial collaboration between those LGPS funds.

Future prospects

The company's future prospects are primarily linked to the needs of LPF. The company is securely funded by LPF, which means that it is in a position to adapt to any future staffing requirements. Arrangements are in hand to increase the number of investment staff to extend LPF's ability to manage investments (including direct property) in-house.

The directors are of the view that the current "Brexit" uncertainty and its outcome is unlikely to directly impact the prospects of the company. This is because LPF will still have a need for investment management and pension administration services.

Directors

The directors who served during the period were:

Hugh Dunn	
Clare Scott	Resigned 26 December 2018
Alasdair Rankin	
Katy Miller	
Stephen Moir	
Leslie Robb	
Douglas Heron	Appointed 1 February 2019

Statement of directors' responsibilities

The directors are responsible for preparing the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. The directors have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law, the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of its results for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Disclosure of information to auditor

As far as each of the directors at the time the report is approved are aware:

a) there is no relevant information of which the company's auditor is unaware, and
b) the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of the information.

Auditor

The auditor, Scott-Moncrieff, is deemed to be reappointed under Section 487 (2) of the Companies Act 2006.

Small company provisions

This report has been prepared in accordance with the special provisions for small companies under Part 15 of the Companies Act 2006.

This report was approved by the board and signed on its behalf by:

[redacted]

Stephen Moir
Chairman

Date: 21 May 2019

Independent Auditor's Report to the Members of LPFE Limited

For the year ended 31 March 2019

Opinion

We have audited the financial statements of LPFE Limited ('the company') for the year ended 31 March 2019 which comprise the Statement of Profit or Loss and Other Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows and related notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2019 and its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the United Kingdom, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate, or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Opinion on Other Matter(s) Prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Directors' Report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the directors' report.

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not exempt from the requirement to prepare a strategic report.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 3, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs(UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Councils website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our Auditor's report.

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an Auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

[redacted]

Nick Bennett, Senior Statutory Auditor
For and on behalf of Scott-Moncrieff, Statutory Auditor
Chartered Accountants
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

Date: 21 June 2019

LPFE LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2019

	Note	2019 £	2018 £
Continuing Operations			
Revenue	1e	3,915,842	1,592,314
Gross profit		3,915,842	1,592,314
Administrative expenses		(4,155,957)	(3,099,188)
Loss from operations	2	(240,115)	(1,056,874)
Finance costs	3	(51,434)	(28,380)
Loss before tax		(291,549)	(1,535,254)
Corporation tax (charge)/credit	4	(14,839)	194
Loss for the year		(306,388)	(1,535,060)
Other comprehensive income:			
Those that are not recyclable net of tax:			
Actuarial (loss)/gain on retirement benefit obligation	15	(268,000)	506,000
Deferred tax charge thereon	10	100,980	175,100
Total comprehensive loss for the year		(473,408)	(853,960)

The accompanying notes on pages 12 to 29 form part of these financial statements

LPFE LIMITED

Statement of Financial Position

As at 31 March 2019

	Note	As at 31 March 2019 £	As at 31 March 2018 £
Non-current assets			
Deferred tax asset	10	392,530	291,550
Total non-current assets		392,530	291,550
Current assets			
Trade and other receivables	7	396,240	340,881
Cash and cash equivalents	8	213,773	10,450
Total current assets		610,013	351,331
Total assets		1,002,543	642,881
Equity and Liabilities			
Equity attributable to equity holders of the parent			
Share capital	11	1	1
Retained earnings	12	(1,866,097)	(1,392,689)
		(1,866,096)	(1,392,688)
Liabilities			
Non-current liabilities			
Retirement benefits obligation	15	2,309,000	1,715,000
Trade and other payables	9	12,551	-
Total non-current liabilities		2,321,551	1,715,000
Current liabilities			
Trade and other payables	9	547,088	320,569
Total current liabilities		547,088	320,569
Total liabilities		2,868,639	2,035,569
Total equity and liabilities		1,002,543	642,881

The financial statements were authorised for issue by the Board of Directors on 21 May 2019
and were signed on its behalf by:

[redacted]

Chairman

Registered number: SC497543

The accompanying notes on pages 12 to 29 form part of these financial statements

LPFE Limited

Statement of Changes in Equity

As at 31 March 2019

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2017		1	(538,729)	(538,728)
Comprehensive income				
Loss for the year		-	(1,535,060)	(1,535,060)
Other comprehensive income				
Actuarial gains on retirement benefit obligation in year	15	-	506,000	506,000
Deferred tax on retirement benefit obligation	10	-	175,100	175,100
Balance at 31 March 2018		1	(1,392,689)	(1,392,688)

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2018		1	(1,392,689)	(1,392,688)
Comprehensive income				
Loss for the year		-	(306,388)	(306,388)
Other comprehensive income				
Actuarial losses on retirement benefit obligation in year	15	-	(268,000)	(268,000)
Deferred tax on retirement benefit obligation	10	-	100,980	100,980
Balance at 31 March 2019		1	(1,866,097)	(1,866,096)

The accompanying notes on pages 12 to 29 form part of these financial statements

LPFE LIMITED

Statement of Cash Flows

For the year ended 31 March 2019

	2019 £	2018 £
Cash flow from operating activities		
Loss for the year	(306,388)	(1,535,060)
Adjustments for:		
Defined benefit pension – current service cost	843,000	336,000
Defined benefit pension – employer contribution	(567,000)	(204,000)
Defined benefit pension – business combinations	-	1,377,000
Defined benefit pension – finance costs	50,000	27,000
Other finance costs	1,434	1,380
Corporation tax charge / (credit)	14,839	(194)
Changes in assets and liabilities:		
Increase in receivables and other financial assets	(55,574)	(199,476)
Increase in payables	234,112	159,5545
Cash flows from operations	214,423	(37,796)
Interest paid	(845)	(1,195)
Corporation tax credit received	215	1,321
Net cash flows from operating activities	213,793	(37,670)
Cash flow from investing activities	-	-
Net cash flows from investing activities	-	-
Cash flow from financing activities		
Movement in loan facility	(10,470)	34,739
Net cash flows from financing activities	(10,470)	34,739
Net increase/(decrease) in cash and cash equivalents	203,323	(2,931)
Cash and cash equivalents at beginning of year	10,450	13,381
Cash and cash equivalents at end of year	213,773	10,450
Cash at bank and in hand	213,773	10,450

The accompanying notes on pages 12 to 29 form part of these financial statements

1. Statement of significant accounting policies

LPFE Limited ('the company') is a limited company incorporated in Scotland. The address of its registered office and principal place of business are disclosed on page 1. The principal activities of the company are described within the directors' report on pages 2 to 4.

The financial statements of LPFE Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS), IFRIC Interpretation and the Companies Act 2006 applicable to companies reporting under IFRS.

Adoption of new and revised standards

The company has adopted the following new and amended IFRSs as of 1 April 2018:

- IAS 1 Presentation of Financial Statements
- IAS 39 Financial Instruments: Recognition and Measurement
- IFRS 7 Financial Instruments: Disclosures
- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IAS 1 has been amended after the issue of IFRS 9 with the main effect on the company being to amend the presentation and disclosure of assets held at amortised cost. Given the nature of the company's financial assets this standard has not had a material impact on the company's financial statements in the period of initial application.

IAS 39 requirements were replaced by IFRS 9 on Financial Instruments, with the main effect on the company being to re-categorise financial assets and liabilities together with IFRS 7 on Financial Instruments Disclosures. On initial application there has been no material impact or significant disclosure changes. The new impairment treatment required under IFRS 9 with impairment provisions for trade and other receivables based on expected credit losses has had no material impact on the company's financial statements.

IFRS 15 deals with contracts to provide goods or services. In recording income from service contracts the company currently recognises costs, particularly staff costs, when incurred. The service contract has one performance obligation and there is little ambiguity surrounding the transaction price as services are charged purely to cover costs incurred. Therefore the directors consider the company is already compliant with IFRS 15 and there have been no changes.

Guidance in issue but not in force

IAS 8 requires disclosure of guidance in issue but not in force. The minimum disclosure relates to guidance issued by 31 March 2018, and with potential effect.

International Accounting Standards and Interpretations	Effective for annual periods beginning on or after
IFRS 16 Leases	1 January 2019
IFRIC 23 Uncertainty over Income Tax Treatments	1 January 2019
IAS 12 Income Taxes*	1 January 2019

*Not yet adopted for use in the European Union.

1. Statement of significant accounting policies (continued)

Guidance in issue but not in force (continued)

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IAS 12 on Income Taxes states that all tax consequences of a dividend should be recognised at the time the liability to pay the dividend is recorded or paid if no liability is recorded prior. All income tax consequences of the dividend will be recorded in profit or loss, other comprehensive income or equity according to where the distributable profits were created.

Basis of preparation

The financial statements are presented in Sterling (£) as that is the company's functional currency and the currency in which the majority of the company's transactions are denominated. The financial statements have been prepared on the historical cost basis.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the company's accounting policies.

The following significant accounting policies, which are consistent with the previous period unless otherwise stated, have been adopted in the preparation of this report:

a. Going concern

The directors are of the opinion that the company has adequate resources to enable it to undertake its planned activities for a period of at least one year from the date that the financial statements are approved.

b. Current and deferred income tax

The company is a mutual trader and is therefore not liable to corporation tax on surpluses generated from mutual trade. The tax charge for the period is based on the profit for the year from non-mutual trade, adjusted for any non-assessable or disallowed items. It is calculated using tax rates that have been enacted or are substantively enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

b. Current and deferred income tax (continued)

Deferred income tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

c. Impairment

The carrying value of all assets are reviewed for impairment at each reporting date, with the recoverable amount being estimated when events or changes in circumstances indicate that the carrying value may be impaired.

The recoverable amount of all assets is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which it belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of the asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

d. Cash and cash equivalents

For the purposes of the statement of cash flows, cash includes cash on hand and at call deposits with banks or financial institutions, investments in money market instruments maturing within less than two months and is net of bank overdrafts.

e. Revenue

Revenue is recognised to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty.

Revenue is derived wholly from the provision of seconded staff in the United Kingdom. Revenue is recognised upon the delivery of the service to the customer.

All revenue is stated net of the amount of value added tax (VAT).

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

f. Value added tax

Revenues, expenses and assets are recognised net of the amount of value added tax (VAT), except:

i. Where the amount of VAT incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
ii. For receivables and payables, which are recognised inclusive of VAT.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Cash flows are included in the statement of cash flows on a gross basis. The VAT component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

g. Share capital

Ordinary shares are classified as equity.

h. Employee benefits

Lothian Pension Fund
The company contributes to a defined benefits scheme operated on behalf of its employees.

The employees of LPFE Limited participate in the Lothian Pension Fund, which is part of the Local Government Pension Scheme in Scotland and is administered by the City of Edinburgh Council.

The current service cost for the period is charged to the statement of profit or loss and other comprehensive income. The assets of the scheme are held separately from those of the company in independently administered funds. The company has fully adopted the accounting principles as required by International Accounting Standard 19 – Employee Benefits.

The liability recognised in the balance sheet in respect of defined benefit pension plan is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in a currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity through other comprehensive income in the period in which they arise.

Past-service costs are recognised immediately in income, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

h. Employee benefits (continued)

Variable pay arrangements
During the year, the company introduced three variable pay schemes, two of which have vesting periods. The Portfolio Manager and Senior Management schemes entitle staff to receive an assessed percentage of their salary as an additional variable pay award if they meet certain objectives during the year. The assessment year runs from 1 February to 31 January each year. This award then vests over the following three years. The first part is payable at the end of the first year if the objectives are met and the remaining two parts are payable in the following two years if the requirement that the employee is still employed by the company at such time is met. In line with IAS19 the payment is recognised when made and the liability has been accrued accordingly for the services which the employees have delivered with regards to the second and third payments in the scheme.

i. Financial instruments

Financial assets and financial liabilities are recognised when the company has become party to the contractual provisions of the instrument.

Trade receivables
Trade receivables are recognised initially at cost and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the company will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is recognised in the statement of profit or loss and other comprehensive income.

Trade payables
Trade payables are initially recognised at cost and subsequently at amortised cost using the effective interest method.

Financial liabilities
Financial liabilities are classified according to the substance of the contractual arrangements entered into.

An instrument will be classified as a financial liability when there is a contractual obligation to deliver cash or another financial asset to another enterprise.

Loans
All interest bearing loans and other borrowings are initially recorded at fair value, which represents the fair value of the consideration received, net of any issue costs associated with other borrowings. Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs.

Finance charges, including premiums payable on settlement or redemption, are accounted for on an amortised cost basis to the statement of comprehensive income using the effective interest method, being recognised in the statement of profit or loss and other comprehensive income over the term of such instruments at a constant rate on the carrying amount of the instrument to the extent that they are not settled in the year in which they arise.

Borrowings are classified as current liabilities unless the company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

1. Statement of significant accounting policies (continued)

Basis of preparation (continued)

j. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

k. Critical accounting estimates and judgements

The directors evaluate estimates and judgements incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the company.

Key estimates – defined benefit pension obligation

IAS 19 Employee Benefits, requires that certain assumptions are made in order to determine the amount to be recorded for retirement benefit obligations and pension plan assets. These are mainly actuarial assumptions such as expected inflation rates, long-term increase in health care costs, employee turnover, expected return on plan assets and discount rates. Substantial changes from the assumptions listed in any one of these variables may significantly change the group's retirement benefit obligation and pension assets (see note 15 for further details).

2. Loss from operations

	2019	2018
	£	£
Loss from operations has been determined after deducting:		
Auditor's remuneration:		
Audit services	5,500	4,900
Non-Audit services	12,775	8,100

3. Finance costs

	2019	2018
	£	£
Loan interest payable to group entities (note 14)	1,434	1,380
Pension interest costs (note 15)	50,000	27,000
	51,434	28,380

4. Corporation tax charge/(credit)

	2019 £	2018 £
Current tax:		
Corporation tax charge/(credit)	14,839	(194)
Tax on profits for the year	14,839	(194)

Corporation tax credit is calculated at 19% (2018: 19%) of the assessable profits for the year.

The charge for the year can be reconciled to the loss per the income statement as follows:

	2019 £	2018 £
Loss for the year before taxation	(291,549)	(1,535,254)
Loss for the year at the effective rate of corporation tax of 19% (2018 – 19%)	(55,394)	(291,698)
Effects of:		
Mutual trade adjustment	66,407	265,242
Expenses not deductible for tax purposes	3,866	26,262
Trading losses carried forward	-	-
Other adjustments	(40)	-
Current tax charge/(credit)	14,839	(194)

5. Employee benefits expense

The average number of persons employed by the company (including directors) during the year was 62 (2018: 20).

The aggregate payroll costs were as follows:

	2019 £	2018 £
Wages, salaries and variable pay	2,817,553	1,136,832
Social security costs	305,148	134,079
Defined benefit pension - current service cost	843,000	336,000
	3,965,701	1,606,911

5. Employee benefits expense (continued)

Variable Pay

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

Deferred variable pay

	2019 £	2018 £
Brought forward	-	-
Current service cost	38,261	-
	38,261	-

	2019 £	2018 £
Current liability	25,710	-
Non-current liability	12,551	-
	38,261	-

6. Directors' remuneration

Three (2018: two) directors received emoluments from the company during the period. The directors' emoluments for the period were as follows:

	2019 £	2018 £
Aggregate emoluments	106,308	102,801
Employer pension contributions	23,397	20,685

One director had an accrued pension entitlement of £22,829 (2018: £20,225) and a lump sum entitlement of £13,636 (2018: £12,938) at the end of the year. The other two directors do not have any accrued pension provision provided by the company.

All other directors are employed by the City of Edinburgh Council.

7. Trade and other receivables

	2019 £	2018 £
Trade receivables	53,577	35,927
Amounts due from group entities	333,412	295,304
Prepayments and accrued income	9,251	9,650
	396,240	340,881

The directors consider the fair value of receivables to be in line with carrying values.

8. Cash and cash equivalents

	2019 £	2018 £
Cash at bank and in hand	213,773	10,450

9. Trade and other payables

Current liabilities	2019 £	2018 £
Trade payables	3,053	13,315
Accruals and deferred income	144,658	140,782
Social security and other taxes	383,751	155,804
Amounts due to group entities	787	10,668
Corporation tax	14,839	-
	547,088	320,569

Non-current liabilities	2019 £	2018 £
Accruals and deferred income	12,551	-
	12,551	-

10. Deferred tax

	2019 £	2018 £
At 31 March 2018	291,550	116,450
Charge for the year to other comprehensive income	100,980	175,100
At 31 March 2019	392,530	291,550
The elements of deferred tax are as follows:		
Defined benefit pension scheme liability	392,530	291,550
	392,530	291,550

11. Share Capital

	2019 £	2018 £
Allotted, called up and fully paid		
Ordinary shares of £1 each	1	1
	1	1

12. Reserves

	Retained Earnings £
At 31 March 2017	(538,729)
Loss for the year	(1,535,060)
Actuarial gain on retirement benefit obligation	506,000
Deferred tax on retirement benefit obligation	175,100
At 31 March 2018	(1,392,689)
Loss for the year	(306,388)
Actuarial loss on pension plan	(268,000)
Deferred tax on retirement benefit obligation	100,980
At 31 March 2019	(1,866,097)

13. Controlling interest

The City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) owns all the issued share capital of the company. The company itself has been established to support the administration of the Lothian Pension Fund. Administering authorities are required to prepare separate financial statements for the Local Government Pension Scheme funds that they administer and so it is considered appropriate to consolidate the company's individual financial statements into Lothian Pension Fund's consolidated financial statements.

Group accounts are available to the public from the following address and will also be made available through the pension scheme website at www.lpf.org.uk:

Company Secretary
Lothian Pension Fund
Atria One
144 Morrison Street
Edinburgh
EH3 8EX

14. Related party transactions

	2019 £	2018 £
Lothian Pension Fund (pension fund administered by City of Edinburgh Council)		
Sale of services during the period	3,616,093	1,449,997
Receivables at the period end	222,584	287,782
Loan facility balance payable at the period end	-	10,470
Interest payable during the period	1,434	1,380
Interest payable but still accruing at the period end	787	198
LPFI Limited (company under common control)		
Sale of services during the period	119,279	20,236
Receivables at the period end	110,828	7,306
Balance receivable for group tax losses surrendered	-	215

The company has a loan facility agreement with Lothian Pension Fund for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the company returns any cash not immediately required and this can result in short periods when the company has returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Total compensation paid in relation to key management personnel during the period was as follows:

	2019 £	2018 £
Short-term employee benefits	647,017	472,188
Post-employment benefits - employer pension contributions	110,543	84,962
	757,560	557,150

Key management personnel had accrued pensions totalling £120,245 (2018: £97,456) and lump sums totalling £132,375 (2018: £110,889) at the end of the period.

15. Retirement benefits obligation

The Lothian Pension Fund, which is administered by the City of Edinburgh Council, is part of the Local Government Pension Scheme in Scotland. This is a pension scheme providing benefits based on pensionable pay, contributions being charged to the profit or loss so to spread the cost of pensions over employees' working lives. The contributions are determined by a qualified actuary.

The valuation of the pension fund is carried out triennially. The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at 31 March 2017 by Hymans Robertson LLP. The present value of the defined benefit obligation, and related current service cost and past service cost, were measured using the Projected Unit Credit Method.

Scheme assets

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

	%	2019 £'000	%	2018 £'000
Equity Securities:				
Consumer	11%	1,094	14%	1,187
Manufacturing	12%	1,265	15%	1,288
Energy and Utilities	8%	777	6%	542
Financial Institutions	8%	865	9%	769
Health and Care	5%	559	5%	425
Information Technology	3%	335	6%	528
Other	10%	1,003	6%	543
Debt Securities:				
Corporate Bonds (investment grade)	0%	-	0%	-
Corporate Bonds (non-investment grade)	0%	-	2%	169
UK Government	10%	1,045	10%	839
Other	0%	-	0%	-
Private Equity:				
All	1%	139	2%	158
Real Estate				
UK Property	7%	697	6%	556
Overseas property	0%	-	0%	9
Investment Funds and Unit Trusts:				
Equities	1%	102	1%	83
Bonds	3%	261	0%	-
Infrastructure	12%	1277	12%	1,025
Other	0%	-	0%	20
Derivatives:				
Foreign Exchange	0%	3	0%	-
Cash and Cash Equivalents:				
All	8%	863	6%	511
	100%	10,285	100%	8,652

15. Retirement benefits obligation (continued)

The amounts recognised in the statement of financial position are determined as follows:	2019 £'000	2018 £'000
Fair value of plan assets	10,285	8,652
Present value of scheme liabilities	(12,594)	(10,367)
Net pension liability	(2,309)	(1,715)

The movement in the defined benefit obligation over the year is as follows:

	2019 £'000	2018 £'000
Brought forward	10,367	3,513
Current service cost	843	336
Interest cost on obligation	294	131
Plan participants contributions	194	91
Benefits paid	(8)	(4)
Effects of business combinations	-	7,088
Actuarial losses/(gains) arising from changes in financial assumptions	904	(536)
Actuarial losses arising from changes in demographic assumptions	-	120
Other actuarial gains	-	(372)
Balance at year end	12,594	10,367

The movement in the fair value of plan assets of the year is as follows:

	2019 £'000	2018 £'000
Brought forward	8,652	2,828
Benefits paid	(8)	(4)
Effect of business combinations	-	5,711
Interest income on plan assets	244	104
Contributions by employer	567	204
Contributions by member	194	91
Return on assets excluding amounts included in net interest	636	(282)
Balance at year end	10,285	8,652

15. Retirement benefits obligation (continued)

The amounts recognised in the Statement of Profit or Loss are as follows:

	2019 £'000	2018 £'000
Interest received on pension scheme assets	(244)	(104)
Interest cost on pension scheme liabilities	294	131
Finance cost	50	27
Current service cost	843	336
Effect of business combinations	-	1,377
	893	1,740

Amounts recognised in other comprehensive income:

	2019 £'000	2018 £'000
Actuarial (losses)/gains in the defined benefit obligation	(904)	788
Actuarial gains/(losses) in the fair value of defined benefit assets	636	(282)
	(268)	506

The principal actuarial assumptions used in this valuation were:

	2019	2018
Inflation/pension increase rate	2.4%	2.3%
Salary increase rate	4.1%	4.0%
Discount rate	2.5%	2.7%

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

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

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

15. Retirement benefits obligation (continued)

The sensitivity of the overall pension liability to changes in the weighted principal assumptions is:

Change in assumption	Approximate % increase to employer liability		Approximate increase to employer liability (£'000)	
	2019	2018	2019	2018
0.5% decrease in real discount rate	13%	13%	1,666	1,354
0.5% increase in the salary increase rate	4%	4%	499	455
0.5% increase in the pension increase rate	9%	8%	1,118	859

Mortality rates:

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

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

	Male	Female
Current pensioners	21.7	24.3
Future pensioners	24.7	27.5

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

Contingent Liabilities

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

As a result of a ruling in The Court of Appeal (the McCloud judgement) in December 2018, which relates to age discrimination arising from public sector pension scheme transition arrangements, there is the potential for an impact on employer pension liabilities for LPF. Hymans Robertson LLP has advised that given the uncertainty around this judgement, with the government awaiting news of its right to an appeal, it is too early to know what the likely effect may be on LGPS members' benefits.

16. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable. Financial instruments do not include prepayments, VAT, taxation, social security and deferred income.

The company did not enter into any transactions that would be classed derivative financial instruments during the period.

The totals for each category of financial instruments, measured in accordance with IAS 39 and detailed in the accounting policies, are as follows:

	2019	2018
	£	£
Financial Assets		
Cash and cash equivalents	213,773	10,450
Trade and other receivables	389,372	333,531
Total Financial Assets	603,145	343,981
Financial Liabilities		
Trade and other payables	161,049	164,765
Total Financial Liabilities	161,049	164,765

Financial Risk Management Policies

The company aims to manage its overall capital structure to ensure it continues to operate as a going concern. The company's capital structure represents the equity attributable to the shareholders of the company together with cash equivalents.

The Board is charged with the overall responsibility of establishing and monitoring the company's risk management policies and processes in order to identify, analyse and monitor the risks that are faced by the company. The company does not enter into or trade financial instruments for speculative purposes.

The main risks that the company is exposed to through its financial instruments are credit risk, liquidity risk and market risk. These are managed as follows:

a. Credit risk

Exposure to credit risk relating to financial assets arises from the potential non-performance by counterparties of contractual obligations that could lead to a financial loss to the company.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance sheet date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the statement of financial position and notes to the financial statements. As at 31 March 2019 none of the company's financial assets were past due or impaired.

Credit risk is managed and reviewed regularly by senior management. It mainly arises from amounts owed by customers.

16. Financial Risk Management (continued)

Financial Risk Management Policies (continued)

a. Credit risk (continued)

The nature of the company's business means that it currently only has three customers. By far the largest customer is the City of Edinburgh Council and the company is securely funded by the Council. Falkirk Council is a smaller customer. The third customer is LPFI Limited which is a related party. Given the financial stature of both Councils and LPFI Limited the credit risk faced by the company is considered to be very small.

b. Liquidity Risk

Liquidity risk arises from the possibility that the company might encounter difficulty in settling its debts or otherwise meeting its financial obligations as they fall due. The company manages this risk through the following mechanisms:

- preparing forward-looking cash flow analysis in relation to its operational, investing and financing activities; and
- ensuring that adequate unutilised borrowing facilities are maintained.

The tables below reflect an undiscounted contractual maturity analysis for financial liabilities.

Financial liability and financial asset maturity analysis

	Note	Within 1 Year 2019 £	1 to 5 Years 2018 £	Total 2019 £
Financial liabilities due for payment				
Trade and other payables		(148,498)	(12,551)	(161,049)
Total expected outflows		(148,498)	(12,551)	(161,049)
Financial assets — cash flows realisable				
Cash and cash equivalents		213,773	-	213,773
Trade and other receivables		389,372	-	389,372
Total anticipated inflows		603,145	-	603,145
Net inflow of financial instruments		454,647	(12,551)	442,096

Cash flows realised from financial assets reflect management's expectation as to the timing of realisation. Actual timing may therefore differ from that disclosed. The timing of cash flows as presented in the table (to settle financial liabilities) reflects the earliest contractual settlement dates.

The company has been granted a £385,000 unsecured revolving loan facility by its parent, The City of Edinburgh Council. The ceiling of the facility has been set at a level to ensure sufficient cash is available to meet the company's short-term cash flow needs, should there be a delay in the City of Edinburgh Council settling invoices for seconded staff.

16. Financial Risk Management (continued)

Financial Risk Management Policies (continued)

c. Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the company's financial position. The company has no direct exposure to movements in foreign exchange or equity prices, and has very little exposure to interest rate movements, due to the low level of borrowing. The company monitors this risk but the directors are of the opinion that it is very unlikely to have a significant effect on the company's financial position.

17. Movements in financing (assets)/liabilities arising from financing activities

	Current loans & borrowings
At 1 April 2017	(24,269)
Cash flows	
Financing loans from group companies drawdown	34,739
At 31 March 2018	10,470

	Current loans & borrowings
At 1 April 2018	10,470
Cash flows	
Payment of group company financing loan	(10,470)
At 31 March 2019	-

18. Contingent Liabilities

The company's variable pay arrangements are described in note 5 above. In the event that all the staff involved in the arrangements at 31 January 2019 remain in the company's employment there is a contingent liability of £319,900 in excess of the current and non-current liabilities, as recognised in these financial statements in accordance with IAS19. This amount would be payable over two years.

LPFI Limited

Financial Statements

For the year ended 31 March 2019

Registered number SC497542

LPFI LIMITED

Financial statements

For the year ended 31 March 2019

Contents

LPFI LIMITED

Company information

Board of Directors:	***Chairman***
	Hugh Dunn
	Executive Directors
	Struan Fairbairn John Burns William Bruce Miller Douglas Heron
	Non-executive Director
	Leslie Robb
Registered office:	4th Floor Saltire Court 20 Castle Terrace Edinburgh Lothian EH1 2EN
Bankers:	The Royal Bank of Scotland plc
Auditor:	Scott-Moncrieff Exchange Place 3 Semple Street Edinburgh EH3 8BL

LPFI LIMITED

Directors' Report

For the year ended 31 March 2019

The directors present their report and audited financial statements for the year ended 31 March 2019.

Principal activity

The current principal activity of the company is the provision of Financial Conduct Authority ("FCA") regulated investment services to the City of Edinburgh Council acting in its capacity as the administering authority of the Lothian Pension Fund) ("LPF") and other Local Government Pension Scheme funds in Scotland and Northern Ireland .

Results, dividends and mutual trading surplus

The profit for the year after tax was £59,396 (2017: £34,619). The directors do not recommend payment of a dividend.

The company's aim is to make a modest trading surplus.

Under the mutual trading agreement with LPF, the company is required to consider if any of the profit arising from the mutual trade can be returned to LPF. Company Law requires that only "distributable profits" are available for distribution. None of the profit for the year is attributable to the mutual trade.

Business review

The company is wholly owned by LPF and has entered into a shareholder agreement with LPF to appropriately address certain governance matters. The company also has a loan facility provided by LPF for the provision of short term working capital.

LPFI Limited does not employ staff directly. Staffing and business support services are provided to the company under separate intra-group agreements with LPFE Limited and LPF respectively. LPFE Limited is also wholly owned by LPF. The company provides certain investment services to LPF via an intra-group investment services agreement and has appropriate terms of engagement with its external collaborative partners. During the year Fife Council Pension Fund was added as a new collaborative partner.

HMRC has agreed that any profits arising from trade between the company and LPF will be covered by the "Mutual Trading" rules and so not subject to Corporation Tax.

The company was granted authorised status by the FCA on 24 June 2016. During the year the company provided investment advising and transaction arranging services in relation to a broad scope of matters.

Future prospects

The company's prospects are linked to LPF's requirement for FCA regulated investment services and the LPF's strategy to work with other LGPS funds in the collaborative provision of such services. The company is securely funded by LPF which means that it can adapt to future trading needs.

The directors are of the view that the current "Brexit" uncertainty and its outcome is unlikely to directly impact the prospects of the company. This is because LPF and its external collaborative partners will still have a need for investment management services.

Directors

The directors who served during the year were:

Hugh Dunn	
Struan Fairbairn	
John Burns	
William Bruce Miller	
Clare Scott	Resigned on 26 December 2018
Leslie Robb	
Douglas Heron	Appointed on 1 February 2019

Statement of directors' responsibilities

The directors are responsible for preparing the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of its results for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Disclosure of information to auditor

As far as each of the directors at the time the report is approved are aware:

a) there is no relevant information of which the company's auditor is unaware, and
b) the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of the information.

Auditor

The auditor, Scott-Moncrieff, is deemed to be reappointed under Section 487 (2) of the Companies Act 2006.

Small company provisions

This report has been prepared in accordance with the special provisions for small companies under Part 15 of the Companies Act 2006.

This report was approved by the board and signed on its behalf by:

[redacted]

Date: 23 May 2019

Hugh Dunn
Chairman

Independent Auditor's Report to the Members of LPFI Limited

For the year ended 31 March 2019

Opinion

We have audited the financial statements of LPFI Limited ("the company") for the year ended 31 March 2019 which comprise the Statement of Profit or Loss and Other Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows and related notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2019 and its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the United Kingdom, including the FRC's Ethical Standard, and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate, or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our Auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Directors' Report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the directors' report.

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not exempt from the requirement to prepare a strategic report.

Responsibilities of the directors

As explained more fully in the directors' responsibilities statement set out on page 3, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an Auditor's Report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Councils website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

[redacted]

Nick Bennett, Senior Statutory Auditor
For and on behalf of Scott-Moncrieff, Statutory Auditor
Chartered Accountants
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

Date: 21 June 2019

LPFI LIMITED

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2019

	Note	2019 £	2018 £
Continuing Operations			
Revenue	1e	256,939	130,212
Gross profit		256,939	130,212
Administrative expenses		(183,610)	(87,305)
Profit from operations	2	73,329	42,907
Finance costs	3	-	(168)
Profit before income tax expense		73,329	42,739
Corporation tax charge	4	(13,933)	(8,120)
Profit for the year		59,396	34,619
Other comprehensive income		-	-
Total comprehensive income for the year		59,396	34,619

The accompanying notes on pages 12 to 23 form part of these financial statements

LPFI LIMITED

Statement of Financial Position

As at 31 March 2019

	Note	As at 31 March 2019 £	As at 31 March 2018 £
Current assets			
Trade and other receivables	6	160,593	58,965
Cash and cash equivalents	7	126,624	83,209
Total current assets		287,217	142,174
Total assets		287,217	142,174
Equity and Liabilities			
Equity attributable to equity holders of the parent			
Share capital	9	60,000	60,000
Retained earnings	10	94,447	35,051
		154,447	95,051
Liabilities			
Current liabilities			
Trade and other payables	8	132,770	47,123
Total current liabilities		132,770	47,123
Total equity and liabilities		287,217	142,174

The financial statements were authorised for issue by the Board of Directors on 23 May 2019 and were signed on its behalf by:

[redacted]

Hugh Dunn
Chairman

Registered number: SC497542

The accompanying notes on pages 12 to 23 form part of these financial statements

LPFI LIMITED

Statement of Changes in Equity

As at 31 March 2019

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2017		50,000	432	50,432
Comprehensive income				
Profit for the year		-	34,619	34,619
Share movements				
Shares allotted during the year		10,000	-	10,000
Balance at 31 March 2018	10	60,000	35,051	95,051

	Note	Share Capital £	Retained Earnings £	Total £
Balance at 1 April 2018		60,000	35,051	95,051
Comprehensive income				
Profit for the year		-	59,396	59,396
Balance at 31 March 2019	10	60,000	94,447	154,447

The accompanying notes on pages 12 to 23 form part of these financial statements

LPFI LIMITED

Statement of Cash Flows

For the year ended 31 March 2019

	2019 £	2018 £
Cash flow from operating activities:		
Profit for the year	59,396	34,619
Adjustments for:		
Finance costs	-	168
Corporation tax charge	13,933	8,120
Changes in assets and liabilities:		
Increase in receivables and other financial assets	(101,628)	(45,719)
Increase in payables	79,640	21,898
Cash flows from operations	51,341	19,086
Interest paid	-	(257)
Corporation tax paid	(7,926)	(281)
Net Cash flows from operating activities	43,415	18,548
Cash flow from financing activities:		
Loans repaid to group entities	-	(16,000)
Share capital issued	-	10,000
Net cash flows from financing activities	-	(6,000)
Net increase in cash and cash equivalents	43,415	12,548
Cash and cash equivalents at beginning of year	83,209	70,661
Cash and cash equivalents at end of year	126,624	83,209
Cash at bank and in hand	126,624	83,209

The accompanying notes on pages 12 to 23 form part of these financial statements

1. Statement of significant accounting policies

LPFI Limited ('the company') is a limited company incorporated in Scotland. The address of its registered office and principal place of business are disclosed on page 1. The principal activities of the company are described within the directors' report on pages 2 to 4.

The financial statements of LPFI Limited have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS), IFRIC Interpretation and the Companies Act 2006 applicable to companies reporting under IFRS.

Adoption of new and revised standards

The company has adopted the following new and amended IFRSs as of 1 April 2018:

- IAS 1 Presentation of Financial Statements
- IAS 39 Financial Instruments: Recognition and Measurement
- IFRS 7 Financial Instruments: Disclosures
- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IAS 1 has been amended after the issue of IFRS 9 with the main effect on the company being to amend the presentation and disclosure of assets held at amortised cost. Given the nature of the company's financial assets this standard has not had a material impact on the company's financial statements in the period of initial application.

IAS 39 requirements were replaced by IFRS 9 on Financial Instruments, with the main effect on the company being to re-categorise financial assets and liabilities together with IFRS 7 on Financial Instruments Disclosures. On initial application there has been no material impact or significant disclosure changes. The new impairment treatment required under IFRS 9 with impairment provisions for trade and other receivables based on expected credit losses has had no material impact on the company's financial statements.

IFRS 15 deals with contracts to provide goods or services. In recording income from service contracts the company currently recognises costs, particularly staff costs, when incurred. The service contract has one performance obligations and there is little ambiguity surrounding the transaction price as services are charged for purely to cover costs incurred. Therefore the directors consider the company is already compliant with IFRS 15 and there have been no changes.

Guidance in issue but not in force

IAS 8 requires disclosure of guidance in issue but not in force. The minimum disclosure relates to guidance issued by 31 March 2018, and with potential effect.

International Accounting Standards and Interpretations	Effective for annual periods beginning on or after
IFRS 16 Leases	1 January 2019
IFRIC 23 Uncertainty over Income Tax Treatments	1 January 2019
IAS 12 Income Taxes*	1 January 2019

*Not yet adopted for use in the European Union.

1. Statement of significant accounting policies (continued)

Guidance in issue but not in force (continued)

The directors have reviewed the requirements of the new standards and interpretations listed above and their effects are as follows:

IFRS 16 on leases is not expected to have a material impact on the financial statements as the company currently has no material lessee or lessor transactions.

IAS 12 on Income Taxes states that all tax consequences of a dividend should be recognised at the time the liability to pay the dividend is recorded or paid if no liability is recorded prior. All income tax consequences of the dividend will be recorded in profit or loss, other comprehensive income or equity according to where the distributable profits were created.

Basis of preparation

The financial statements are presented in Sterling (£) as that is the company's functional currency and the currency in which the majority of the company's transactions are denominated. The financial statements have been prepared on the historical cost basis.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the company's accounting policies.

The following significant accounting policies, which are consistent with the previous period unless otherwise stated, have been adopted in the preparation of this report:

a. Going concern

The directors are of the opinion that the company has adequate resources to enable it to undertake its planned activities for a period of at least one year from the date that the financial statements are approved.

b. Current and deferred income tax

The charge for income tax expense for the year is based on the profit for the year adjusted for any non-assessable or disallowed items. It is calculated using tax rates that have been enacted or are substantively enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

1. Statement of significant accounting policies (continued)

b. Current and deferred tax (continued)

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred income tax assets are recognised to the extent that it is probable that future profits will be available against which deductible temporary differences can be utilised.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

c. Impairment

The carrying value of all assets are reviewed for impairment at each reporting date, with the recoverable amount being estimated when events or changes in circumstances indicate that the carrying value may be impaired.

The recoverable amount of all assets is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which it belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of the asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

d. Cash and cash equivalents

For the purposes of the statement of cash flows, cash includes cash on hand and at call deposits with banks or financial institutions, investments in money market instruments maturing within less than two months and is net of bank overdrafts.

e. Revenue

Revenue is recognised to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty.

Revenue is derived wholly from the provision of FCA-regulated service in the United Kingdom. Revenue from a contract to provide services is recognised by reference to the stage of completion of the contract. The stage of completion of the contract is determined with reference to contractual rates as labour hours and direct expenses are incurred.

All revenue is stated net of the amount of value added tax (VAT).

1. Statement of significant accounting policies (continued)

f. Value added tax

Revenues, expenses and assets are recognised net of the amount of value added tax (VAT), except:

i. Where the amount of VAT incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
ii. For receivables and payables, which are recognised inclusive of VAT.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Cash flows are included in the statement of cash flows on a gross basis. The VAT component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

g. Share capital

Ordinary shares are classified as equity.

h. Financial instruments

Financial assets and financial liabilities are recognised when the company has become party to the contractual provisions of the instrument.

Trade receivables
Trade receivables are recognised initially at cost and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the company will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is recognised in the statement of profit or loss and other comprehensive income.

Trade payables
Trade payables are initially recognised at cost and subsequently at amortised cost using the effective interest method.

Financial liabilities
Financial liabilities are classified according to the substance of the contractual arrangements entered into.

An instrument will be classified as a financial liability when there is a contractual obligation to deliver cash or another financial asset to another enterprise.

Finance charges, including premiums payable on settlement or redemption, are accounted for on an amortised cost basis to the profit or loss and other statement of comprehensive income using the effective interest method, being recognised in the statement of comprehensive income over the term of such instruments at a constant rate on the carrying amount of the instrument to the extent that they are not settled in the year in which they arise.

Borrowings are classified as current liabilities unless the company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

1. Statement of significant accounting policies (continued)

h. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amount and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

i. Critical accounting estimates and judgements

The directors evaluate estimates and judgements incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the company. The directors are satisfied that the accounting policies are appropriate and that there are no significant estimates or judgements used in the preparation of the financial statements.

2. Profit from operations

	2019 £	2018 £
Profit from operations has been determined after deducting:		
Auditor's remuneration:		
Audit services	4,000	3,400
Non-Audit services	5,555	6,470

3. Finance costs

	2019 £	2018 £
Loan interest payable to group entities (note 12)	-	168
	-	168

4. Corporation tax charge

	2019 £	2018 £
Current tax:		
Corporation tax charge	13,933	7,926
Inter- company tax	-	194
Tax on profits for the year	13,933	8,120

Corporation tax expense is calculated at 19% (2018: 19%) of the assessable profits for the year.

The charge for the year can be reconciled to the profit per the income statement as follows:

	2019 £	2019 £
Profit for the year before taxation	73,329	42,739
Profit for the year at the effective rate of corporation tax of 19% (2018 – 19%)	13,933	8,120

5. Directors' remuneration

The aggregate payroll costs for the year consisted of fees paid to a non-executive director. These were as follows:

	2019	2018
	£	£
Wages and salaries	12,000	12,000
Social security costs	958	651
	12,958	12,651

No pension benefits were accrued by the director during the year. All other staff and directors are employed by LPFE Limited, a company under common control, and an appropriate portion of their employment costs recharged. LPFE Limited is a company under the control of Lothian Pension Fund (administered by the City of Edinburgh Council), and the City of Edinburgh Council. In addition to the payroll costs noted above, the company was also charged £1,010 (2018: £5,116) for services provided by directors employed by LPFE Limited during the year.

6. Trade and other receivables

	2019	2018
	£	£
Trade debtors	160,139	34,200
VAT recoverable	454	24,765
	160,593	58,965

The directors consider the fair value of receivables to be in line with carrying values.

7. Cash and cash equivalents

	2019	2018
	£	£
Cash at bank and in hand	126,624	83,209

8. Trade and other payables

	2019	2018
	£	£
Trade creditors	317	508
Accruals	7,250	30,084
Corporation tax	13,933	7,926
Amounts due to group entities	111,270	8,605
	132,770	47,123

9. Share Capital

	2019 £	2018 £
Allotted, called up and fully paid		
Ordinary shares of £1 each	60,000	60,000
	60,000	60,000

10. Reserves

	Retained Earnings £
At 31 March 2017	432
Profit for the year	34,619
At 31 March 2018	35,051
Profit for the year	59,396
At 31 March 2019	94,447

11. Controlling interest

The City of Edinburgh Council (acting in its capacity as the administering authority of the Lothian Pension Fund) owns all the issued share capital of the company. The company itself has been established to support the administration of the Lothian Pension Fund. Administering authorities are required to prepare separate financial statements for the Local Government Pension Scheme funds that they administer and so it is considered appropriate to consolidate the company's individual financial statements into Lothian Pension Fund's consolidated financial statements.

Group accounts are available to the public from the following address:

Account Dept.
Lothian Pension Fund
Atria One
144 Morrison Street
Edinburgh
EH3 8EX

12. Related parties

	2019 £	2018 £
Lothian Pension Fund (pension fund administered by City of Edinburgh Council)		
Business support costs	442	1,083
Payables at the period end	442	1,083
Loan facility repaid during the year	-	16,000
Interest payable during the period	-	168
LPFE Limited (company under common control)		
Staff and other cost recharges	10,988	20,236
Recharges to collaborative partner on behalf of LPFE	108,290	-
Payables at the period end	110,828	7,306
Group tax losses utilised	-	194
Balance payable for group tax losses utilised	-	215

The company has a loan facility agreement with Lothian Pension Fund for the purpose of the provision of short term working capital. The current agreement covers the period to 1 May 2020 and provides that interest is payable at 2% above the Royal Bank of Scotland base lending rate on the daily balance. In order to minimise the amount of interest payable, the company returns any cash not immediately required and this can result in short periods when the company has returned more cash than has been drawn. On such days the loan interest is negative, reducing the amount of interest payable.

Compensation paid in relation to key management personnel during the period was as follows:

	2019 £	2018 £
Directors' remuneration (note 5)	12,958	12,651
	12,958	12,651

All other key management personnel are employed by LPFE Limited, a company also under the control of Lothian Pension Fund (administered by the City of Edinburgh Council), and the City of Edinburgh Council. In addition to the compensation noted above, the company was also charged £1,010 (2018: £5,116) for services provided by key management personnel employed by LPFE Limited during the year.

13. Financial Risk Management

The company's financial instruments consist mainly of deposits with banks and accounts receivable and payable. Financial instruments do not include VAT, taxation, social security and deferred tax.

The company did not enter into any transactions that would be classed as derivative financial instruments during the period.

The totals for each category of financial instruments, measured in accordance with IAS 39 and detailed in the accounting policies, are as follows:

	2019	2018
	£	£
Financial assets		
Cash and cash equivalents	126,624	83,209
Trade and other receivables	160,139	34,200
Total financial assets	286,763	117,409
Financial liabilities		
Trade and other payables	118,837	15,197
Total financial liabilities	118,837	15,197

Financial risk management policies

The company aims to manage its overall capital structure to ensure it continues to operate as a going concern. The company's capital structure represents the equity attributable to the shareholders of the company together with cash equivalents.

The Board is charged with the overall responsibility of establishing and monitoring the company's risk management policies and processes in order to identify, analyse and monitor the risks that are faced by the company. The company does not enter into or trade financial instruments for speculative purposes.

The main risks that the company is exposed to through its financial instruments are credit risk, liquidity risk and market risk. These are managed as follows:

a. Credit risk

Exposure to credit risk relating to financial assets arises from the potential non-performance by counterparties of contractual obligations that could lead to a financial loss to the company.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance sheet date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the statement of financial position and notes to the financial statements. As at 31 March 2019 none of the company's financial assets were past due or impaired.

Credit risk is managed and reviewed regularly by senior management. It mainly arises from amounts owed by customers. Given the financial stature of its customers the credit risk faced by the company is considered to be very small.

13. Financial Risk Management (continued)

b. Liquidity Risk

Liquidity risk arises from the possibility that the company might encounter difficulty in settling its debts or otherwise meeting its financial obligations as they fall due. The company manages this risk through the following mechanisms:

- preparing forward-looking cash flow analysis in relation to its operational, investing and financing activities; and
- ensuring that adequate unutilised borrowing facilities are maintained.

The tables below reflect an undiscounted contractual maturity analysis for financial liabilities.

Financial liability and financial asset maturity analysis

	Within 1 Year 2019 £	1 to 5 Years 2019 £	Total 2019 £
Financial liabilities due for payment			
Trade and other payables	(118,837)	-	(118,837)
Total expected outflows	(118,837)	-	(118,837)
Financial assets — cash flows realisable			
Cash and cash equivalents	126,624	-	126,624
Trade and other receivables	160,139	-	160,139
Total anticipated inflows	286,763	-	286,763
Net inflow of financial instruments	167,926	-	167,926

Cash flows realised from financial assets reflect management's expectation as to the timing of realisation. Actual timing may therefore differ from that disclosed. The timing of cash flows as presented in the table (to settle financial liabilities) reflects the earliest contractual settlement dates.

The company has been granted a £250,000 unsecured revolving loan facility by its parent, The City of Edinburgh Council. The ceiling of the facility has been set at a level to ensure sufficient cash is available to meet the company's short-term cash flow needs, should there be a delay in customers settling invoices for services provided.

13. Financial Risk Management (continued)

c. Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the company's financial position. The company has no direct exposure to movements in foreign exchange or equity prices, and has very little exposure to interest rate movements, due to the low level of borrowing. The company monitors this risk but the directors are of the opinion that it is very unlikely to have a significant effect on the company's financial position.

14. Movements in financing (assets)/liabilities arising from financing activities

	Share capital	Current loans & borrowings	Total
At 1 April 2017	50,000	16,000	66,000
Cash flows			
Financing loans from group companies withdrawn	-	(16,000)	(16,000)
Issue of share capital	10,000	-	10,000
At 31 March 2018	60,000	-	60,000

	Share capital	Current loans & borrowings	Total
At 1 April 2018 and 31 March 2019	60,000	-	60,000

Scott-Moncrieff Audit Services
Exchange Place 3
Semple Street
Edinburgh
EH3 8BL

Dear Sirs

Lothian Pension Fund and Scottish Homes Pension Fund

This representation letter is provided in connection with your audit of the Lothian Pension Fund and Scottish Homes Pension Fund Annual Report and Accounts for the year ended 31 March 2019 for the purpose of expressing an opinion as to whether the financial statements show a true and fair view of the financial transactions of the Funds during the year to 31 March 2019 and of the amount and disposition at that date of its assets and liabilities (other than liabilities to pay pensions and benefits after the end of the period) in accordance with Part VII of the Local Government (Scotland) Act 1973 and International Financial Reporting Standards as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 and making a statement about contributions.

By a resolution of the board, passed today, I am directed to confirm to you, in respect of the financial statements of the Funds for the year ended 31 March 2019 the following:

1. We have fulfilled our responsibilities for preparing financial statements which give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 and for making accurate representations to you.
2. We have provided you with:
    - access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
    - additional information that you have requested from us for the purpose of the audit; and
    - unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
3. All transactions have been recorded in the accounting records and are reflected in the financial statements.
4. We acknowledge our responsibilities for the design and implementation of internal control in order to prevent and detect fraud and to prevent and detect error.
5. We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity and involves:
    - management;
    - employees who have significant roles in internal control; and
    - others where the fraud could have a material effect on the financial statements.

6. We are not aware of any allegations of fraud or suspected fraud with a potential effect on the financial statements which have been communicated to us by employees, former employees, regulators or other third parties.

7. We have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations, whose effects should be considered when preparing the financial statements.

8. We confirm that, in our opinion, the assumptions that have been used in determining fair values, whether such values are disclosed or applied in the financial statements, are reasonable and reflect our ability and intent to carry out specific courses of action, where this is relevant to the determination of those values.

9. In our opinion the significant assumptions used by us in making accounting estimates are reasonable.

10. Where required, the value at which assets and liabilities are recorded in the net assets statement is, in our opinion, the market value. We are responsible for the reasonableness of any significant assumptions underlying the valuation, including consideration of whether they appropriately reflect our intent and ability to carry out specific courses of action on behalf of the Funds. Any significant changes in those values since the accounting reference date have been disclosed to you.

11. We have disclosed to you the identity of the company's related parties and all related party relationships and transactions of which we are aware.

12. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of International Financial Reporting Standards as adopted by the European Union.

13. In particular, no trustee, shadow trustee, their connected persons or other officers had any indebtedness, agreement concerning indebtedness or disclosable interest in a transaction with the Funds at any time during the year.

14. The following have been properly recorded and, when appropriate, adequately disclosed in the financial statements:

    - losses arising from sale and purchase commitments;
    - agreements and options to buy back assets previously sold;
    - assets pledged as collateral.

15. We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

16. We have no plans to abandon activities or other plans or intentions that will result in any excess or obsolete stocks, and no stock is stated at an amount in excess of net realisable value.

17. The Funds have satisfactory title to all assets and there are no liens or encumbrances on the Funds' assets, other than as disclosed in the financial statements.

18. We have recorded or disclosed, as appropriate, all liabilities, both actual and contingent, and all guarantees that we have given to third parties.

19. All events subsequent to the date of the financial statements and for which International Financial Reporting Standards as adopted by the European Union require adjustment or disclosure have been adjusted or disclosed. Should any material events occur which may necessitate revision of the figures included in the financial statements or inclusion in the notes thereto, we will advise you accordingly.

20. The Funds have complied with all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance.

21. To the best of our knowledge and belief, the information disclosed in the financial statements in respect of parties which control the Funds is complete and accurate.

22. Except as disclosed in the financial statements, the results for the year were not materially affected by:

- any change in accounting policies;
- transactions of a type not usually undertaken by the Funds' group;
- circumstances of an exceptional or non-recurrent nature; or
- charges or credits relating to prior periods.

23. There is no pending or potential litigation against the Funds and there are no contingencies of a material amount for which provision has not been made in the financial statements.

24. We confirm that we have reviewed going concern considerations and are satisfied that it is appropriate for the financial statements to have been drawn up on the going concern basis. In reaching this opinion we have taken into account all relevant matters of which we are aware and have considered a future period of at least one year from the date on which the financial statements were approved.

Yours faithfully

John Burns
Chief Finance Officer (Section 95 Officer for the Pension Funds)