

ITEM No ...9.....

**REPORT TO: PENSION SUB-COMMITTEE OF THE POLICY & RESOURCES COMMITTEE
& PENSION BOARD – 21 JUNE 2021**

**REPORT ON: LOCAL GOVERNMENT PENSION SCHEME ADVISORY BOARD
(SCOTLAND) – ANNUAL REPORT 2019-20**

REPORT BY: EXECUTIVE DIRECTOR OF CORPORATE SERVICES

REPORT NO: 202-2021

1 PURPOSE OF REPORT

The purpose of this report is to provide information on the Scheme Advisory Board's activities over the financial year to 31st March 2020.

2 RECOMMENDATION

The Committee is asked to note the contents of this report.

3 FINANCIAL IMPLICATIONS

There is no financial impact.

4 BACKGROUND

The Scottish Local Government Pension Scheme Advisory Board (SAB) was established under the Public Service Pensions Act 2013 to provide advice to Scottish Government Ministers on the desirability of changes to the design of the scheme and the implication of other policy issues.

The SAB also provides advice to the Scheme Managers or the Scheme's Pension Boards in relation to the effective and efficient administration and management of the scheme.

The Scheme Advisory Board is responsible for:

- Providing advice on request about the desirability of changes to the design of the scheme; policy issues and changes to scheme regulations
- Discussing and commenting on the potential implications of future valuation outcomes
- Making recommendations on adjustments to the Scheme in the event that costs breach the employer cost cap
- Providing advice to the Scheme Managers or the Scheme's Pension Boards in relation to the effective and efficient administration and management of the Scheme.

5 POLICY IMPLICATIONS

This Report has been screened for any policy implications in respect of Sustainability, Strategic Environmental Assessment, Anti-Poverty, Equality Impact Assessment and Risk Management.

There are none.

6 CONSULTATION

The Chief Executive and Head of Democratic and Legal Services have been consulted in the preparation of this report.

7 BACKGROUND PAPERS

None

ROBERT EMMOTT

EXECUTIVE DIRECTOR OF CORPORATE SERVICES

14 JUNE 2021

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Annual Report 2019-20

Opening Remarks from the Chair

On behalf of the Local Government Pension Scheme Advisory Board, I am delighted to be able to present the fifth SAB Annual Report. The aim of this Annual Report is to provide a primary source of information about the work of the Board over the last financial year, 2019-20 for LGPS members, employers, and other stakeholders.

This report summarises the financial position of funds across Scotland, and each local Pensions Committee has made decisions to invest their funds bearing in mind their own fiduciary duty. Although the positions of individual funds vary, overall across Scotland the LGPS is fully funded and sustainable, which is very welcome.

I hope you find this report useful. The Board welcomes feedback on the information provided and how this can be developed for future reports. More information can be found about the Board's work at our website: <https://lgpsab.scot/>

Cllr Jim Goodfellow
Chair of SAB (Outgoing)

Introduction

The Scottish Local Government Pension Scheme Advisory Board (SAB) was established under the Public Service Pensions Act 2013 to provide advice to Scottish Government Ministers on the desirability of changes to the design of the scheme and the implication of other policy issues.

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- Providing advice on request about the desirability of changes to the design of the scheme; policy issues and changes to scheme regulations.
- Discussing and commenting on the potential implications of future valuation outcomes.
- Making recommendations on adjustments to the Scheme, in the event that costs breach the employer cost cap.
- Providing advice to the Scheme Managers or the Scheme's Pension Boards in relation to the effective and efficient administration and management of the Scheme.

Structure and People

The SAB is a bipartite Board comprising equal representation from employers and employee representatives. It meets four times a year and considers Scotland-wide issues relating to the governance of the scheme.

In the past, these have included Fiduciary Duty, "pensions choice", scheme governance, reviews of pension regulations, Guaranteed Minimum Pensions, and the Audit Scotland review of funds.

Current issues include investment cost transparency, cessation valuations for admitted bodies, scheme valuation and quality of individual fund valuations, fund structures and board member training.

The partnership approach is also reflected in our administration arrangements with Joint Chairing on a rotational basis between the two sets of representatives and a Joint Secretariat sourced from existing resources within the Employers and Trade Union organisations.

Current SAB Members (as at April 2021)

Chair – Cllr Jim Goodfellow, East Lothian Council (Vice Chair 2019-20)
Vice Chair – Andy Thompson, GMB (Chair 2019-20)

Members representing Scheme Member interests:

Simon Watson, UNISON; Stephen Smellie, UNISON; Dr Davena Rankin, UNISON; Brian Robertson, Unite the Union; Wendy Dunsmore, Unite the Union; Andy Thompson, GMB; Annette Drylie, GMB.

Members representing COSLA, Scheduled and Admitted Bodies:

Cllr Alastair Rankin, City of Edinburgh Council (COSLA); Cllr Jim Goodfellow, East Lothian Council (COSLA); Cllr David Parker, Scottish Borders Council (COSLA); Cllr Simon Mountford, Scottish Borders Council (COSLA); Cllr Frank Anderson, West Lothian Council (COSLA); Brian Strathie, Scottish Water (Scheduled and Admitted Bodies); Lynne Robertson, Inspire (Scheduled and Admitted Bodies) (from January 2020).

During 2019-20 Cllr Richard Thompson, Aberdeenshire Council, was replaced by Cllr Frank Anderson, West Lothian Council

Joint Secretary – Employers Jonathan Sharma, COSLA Kathy Cameron, COSLA (until March 2020)
Joint Secretary – Trade Unions Simon Watson, UNISON

There are a number of observers and advisers who support the SAB in the deployment of Board business. These include representatives from, and on behalf of, the Scottish Government, formal COSLA officials, pension scheme managers and representatives from professional associations.

Communications

The SAB has developed a bespoke website to act as a unique source of information and advice to all stakeholders. The site includes the minutes of SAB meetings along with other governance documentation, guidance documents and details of the Board's membership. The content of the website will develop as the work of the Board continues.

Similar information is also published on the local government pages of the Scottish Public Pensions Agency (SPPA) website - www.sppa.gov.uk.

A short bulletin is also published after each meeting covering the key decisions. This bulletin is circulated to key stakeholders and is available on the SAB website – lgpsab.scot

SPPA links and useful resources for local government employers to each Fund:
<https://pensions.gov.scot/local-government/about-local-government-pensions/useful-links>

Links to local government employer websites: <https://www.cosla.gov.uk/>

Links to Funds: <https://lgpsab.scot/related-websites/>

Financial report

The regulations underpinning the 2013 Act allow the SAB to collect a levy to support its work. In the first year of operation, the SAB adopted a straight proportion of the levy raised by our equivalent SAB in England and Wales equating to £40,000. The SAB secretariat and support function is used from existing resources within both employer and trade union organisations to minimise the financial impact of our work on the public purse. During the business year 2019-20, the SAB retained the bulk of the funds in anticipation of the forthcoming structure review procurement and to meet anticipated costs of the UK online fee transparency portal, to be met by the Scottish SAB. Further detail is contained in the Review of the Year below. A regular financial report is considered by the SAB at each meeting and any monies not used are held over for the following financial year.

Review of the Year 2019-20

1. The SAB kicked off the year by receiving the final report from the Pensions Institute, who had been commissioned to consult on a review of the Structure of the Scottish LGPS.

2. Respondents were asked to evaluate the scheme against the criteria of investment costs, governance, operating risks and ability to invest in infrastructure. The suggested actions from the

research were to evaluate the case for merger; to examine how the Scottish Government could help boosting the supply of Scottish infrastructure investments; to challenge investment costs by making reporting using Institutional Disclosure Working Group templates mandatory; and to examine measures to ease the ability of multi-fund employers to consolidate into a single fund.

3. The SAB Chair wrote to the Cabinet Secretary with the outcome of this research, and in reply the SAB was asked to take forward work into the details of mergers and pooling and later included co-operation between funds. A detailed specification was prepared by a SAB working group and approved, before COVID struck and much of the work programme was severely disrupted.

4. The Autumn also saw the “Section 13” report by the Government Actuaries Department (GAD) on Fund valuations. It found that the valuations were compliant, and in aggregate that the funds were fully funded. It did highlight a recommendation that a standardised way of funds reporting, which would allow some cross-comparison, would be desirable.

5. In the new year, the ground-breaking online cost transparency system went live. This is the first step in a project which will allow fund managers to upload their cost transparency reports and Funds to analyse and compare these.

6. COVID disrupted the March 2020 meeting of the SAB, and so there were only three in the year, but many pieces of work were subsequently picked up and taken forward.

7. More detailed updates on key issues are included later in the Report.

Financial Overview

Audit Scotland published an annual Financial Overview of Local Government in Scotland 2019/20 on the SLGPS within its main report. This describes the scheme and governance arrangements together with an analysis of the financial position. Its conclusions were as follows:

Investment returns for each fund were between -1.9% and -8.3% in 2019/20. In the majority of funds, the overall investment returns still outperformed their individual annual benchmarks to 31 March 2020. A number of pension fund auditors drew attention to the levels of greater uncertainty attached to ‘level 3’ investments, by including an ‘emphasis of matter’ paragraph in their auditors’ reports. These valuations included material valuation uncertainty disclosures this year due to Covid-19.

The reports can be found on Audit Scotland’s website, link below:

<https://www.audit-scotland.gov.uk/report/local-government-in-scotland-financial-overview-201819>

<https://www.audit-scotland.gov.uk/report/scottish-government-annual-audit-plan-and-interim-audit-report-201920>

Triennial valuations of Scottish Local Government Pension Funds are due to be completed in March 2021. This will identify the funding level in each scheme and inform future funding and investment strategies as well as determining the level of employer and employee contribution rates from 2021/22 onwards.

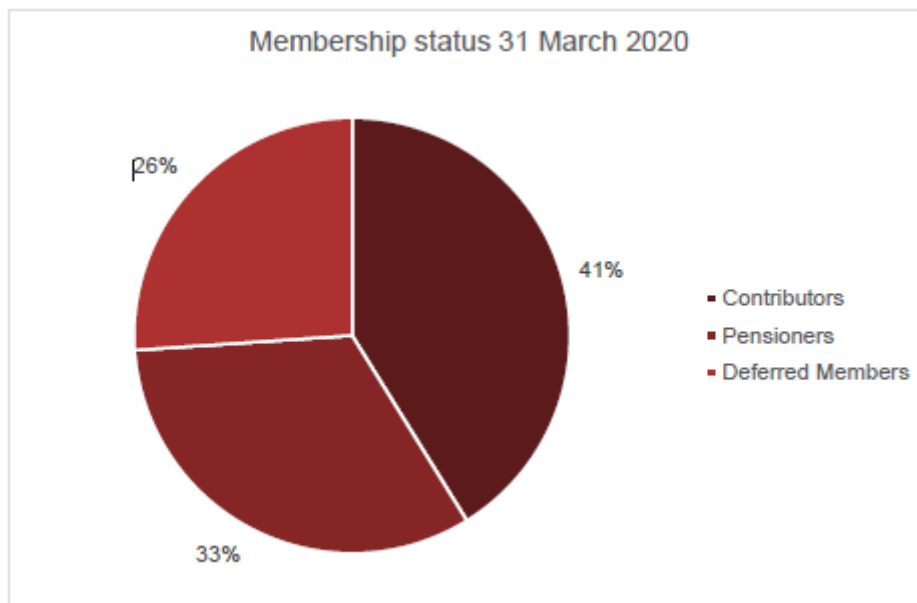
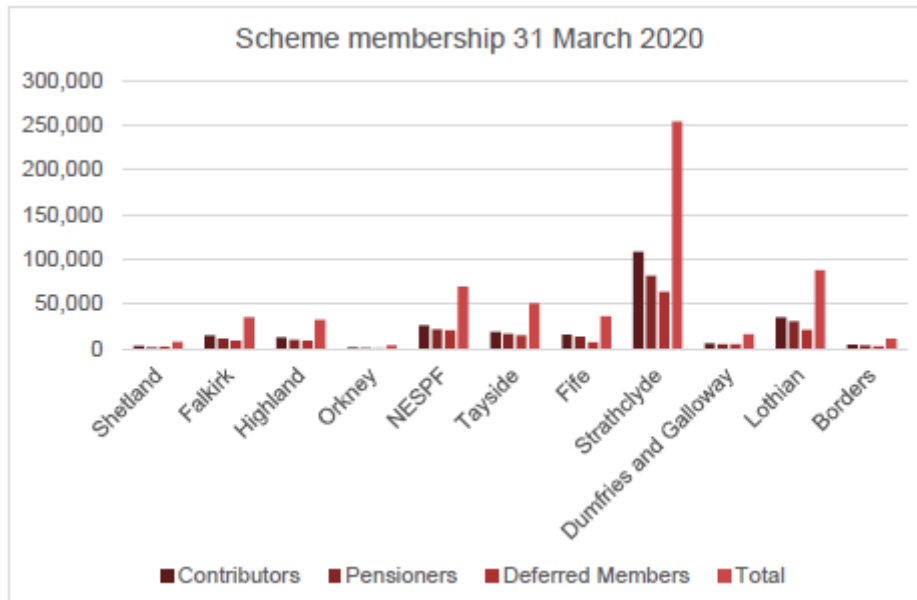
LGPS Funds Accounts and Net Assets as at 31 March 2020 are available at <http://scotlgpsab.webdigi.co.uk/docs/Appendix12020.pdf>

Scheme Membership

The tables below give a snapshot of the Local Government Pensions Scheme as at 31 March 2020, showing the total numbers for the scheme.

2020	Contributors	Pensioners	Deferred Members	Total
Shetland	3,472	2,077	2,293	7,842
Falkirk	15,186	11,183	9,027	35,396
Highland	12,820	10,547	9,018	32,385
Orkney	2,017	1,041	990	4,048

NESPF	26,275	22,156	20,986	69,417
Tayside	19,117	16,635	15,252	51,004
Fife	15,679	13,735	7,194	36,608
Strathclyde	108,492	81,470	63,796	253,758
Dumfries and Galloway	6,349	5,065	5,201	16,615
Lothian	35,655	30,840	21,406	87,901
Borders	4,573	3,856	2,909	11,338
	249,635	198,605	158,072	606,312



Transparency of Investments

With more than £46bn of assets, there is significant interest in how contributions are invested and in maximising the financial benefit for scheme members and employers.

The Board has focussed on transparency of investment fees and costs by adopting and promoting templates to report these, first developed by the Institutional Disclosure Working Group and now taken forward by the Cost Transparency Initiative (CTI). These represent a step forwards in having a common and comparable system of reporting investment costs.

The next step is enabling boards to compare costs, notwithstanding that there will always be local differences and minor variations. So, the SAB has supported the development of an online “portal” through which funds can require investment managers to report their fees and costs. This has been commissioned and was launched in March 2020. It provides basic data validation and average costs of investments for various asset classes. This is very much the start of developing a more granular system which will help shine a light on the totality of investment costs.

Pensions Funds have continued to promote the Transparency Code and have engaged with their asset managers to ensure the Code is adopted. Evidence is that the majority of fund managers are adopting the Code, while for others this is still work in progress.

For the 2019/2020 scheme year for Scotland, the status shown on the SAB Cost Transparency Compliance and Validation System was as follows:

	Complete	Due	Late
Grand Total	162	0	5

Therefore, 97% of templates expected to be uploaded for this period were complete.

Funds are continuing to notice a modest improvement in the granularity of costs being disclosed, with cost templates covering up to 31 March 2020 being provided. However, there remains more work to be done working with private markets, in particular in providing cost transparency. Funds are adopting the CTI templates and expect to be reporting on this basis in the 2020/21 financial period.

Cessation Issues

Smaller employers, typically outwith the public sector, are members of various LGPS funds in Scotland. They typically have weaker covenants than local authorities, and therefore are at higher risk and have to pay higher contributions. In addition, when they no longer have any active members, the employers are required to address any funding deficits. These arrangements vary by fund.

At the request of Scottish Ministers, the SAB convened a working group to explore guidance to address the differences in the treatment of different employers in different funds and ensure a fair, consistent and transparent approach to cessation issues.

The SAB is currently considering the outcome of the Cessation Working Group’s work and is advising SPPA accordingly (see Future work below).

Employment Tribunal (McCloud)

The SAB has been keenly aware of the December 2018 Court of Appeal ruling on transitional protections in the Judicial and firefighters pension scheme, which it found unlawfully discriminated against younger workers. However, the specific protection in the LGPS differs from the other public service pension schemes –the statutory underpin in the transitional regulations applies only to those within ten years of retirements on 31 March 2012. The UK Treasury is taking forward work on this, and the SAB will consider proposals from the SPPA in due course. Uncertainty around the implications of this judgement, and especially any costs involved, has also led to a delay in considering the valuation of the Scottish LGPS scheme and if the cost cap has been breached.

The latest position is covered in Future Work below.

Member Training

As part of taking forward the outcomes of its governance review, the SAB has sought updated information from Pension Boards on training for board members. It considered the training requirements and good practice for board members, and SAB members and agreed that links with Boards needed to be strengthened. A training programme has been developed in conjunction with SAB advisers and was brought forward during 2019/20. In more general terms, the SAB has considered what advice it needs to take forward its work and how best to utilise the skills and experience of its advisers.

Future Work

The Board plans to progress the areas set out above. This includes work to further scope work to assess options under the structure review; work to further develop transparency of investments; responsible investment transparency; to consider the outcome of the work of the Cessations Working Group and advise SPPA accordingly; and work on training for board members. The Board also expects to receive recommendations from the Government Actuary Department (GAD) on the 2016 Cost Cap Valuation, in the first half of 2021.

Financial Statement

Fund Account 2018/2019	Dealings with members, employers and others directly involved in the Scheme (£000s)	2019/2020
	Contributions and Benefits	
1,349,521	Contributions	1,440,450
32,919	Transfers in from other pension funds	53,950
705	Other income	729
1,383,145		1,495,129
-1,369,965	Benefits	-1,484,737
-84,326	Payments to and on account of leavers	-90,384
-14,991	Administration expenses	-6,545
-6,052	Oversight and Governance expenses	-1,303
-1,475,334		-1,582,969
-92,189	Net additions from dealings with members	-87,840
	Returns on investments	
776,422	Investment income	867,908
-18,390	Taxes on income	-14,521
2,542,920	Profits and losses on disposal of investments and changes in the market value of investments	-2,681,741
-222,230	Investment management expenses	-223,441
3,078,722	Net return on investments	-2,051,795
2,986,533	Net increase in the net assets available for benefits during the year	-2,139,635
45,433,470	Net Assets of the Fund as at 1 April (2019 restated)	48,420,003
48,420,003	Net Assets of the Fund as at 31 March	46,280,368
6.6%	Net return	-4.3%
7.0%	Return on investment (excluding expenses)	-3.9%

Net asset statement

2018/2019	Investment Assets (£000s)	2019/2020
2,267,418	Bonds/Gilts	1,967,008
16,628,442	Equities	10,341,162
15,939,590	PIVs3	19,297,581
894,810	Property PIVs	860,772
3,247,199	Property	3,294,756
4,895,285	Private equity	5,852,142
-1,358	Derivatives	7,998
1,251,778	Other	900,761
626,710	Other balances	1,273,200
2,559,777	Cash deposits	2,243,339
48,309,650		46,038,719
0	Investment Liabilities	0
7,786	Non-current assets	7,786
-47,125	Non-current liabilities	-47,125
406,198	Current Assets	406,198
-125,210	Current Liabilities	-125,210
48,551,299	Net assets of the fund available to fund benefits at the period end	46,280,368

Investments

Investment Assets (£000s)	2019	2020	2019	2020	change
Bonds/Gilts	2,267,418	1,967,008	4.7%	4.3%	-0.4%
Equities	16,628,442	10,341,162	34.4%	22.5%	-12.0%
PIVs	15,939,590	19,297,581	33.0%	41.9%	8.9%
Property PIVs	894,810	860,772	1.9%	1.9%	0.0%
Property	3,247,199	3,294,756	6.7%	7.2%	0.4%
Private equity	4,895,285	5,852,142	10.1%	12.7%	2.6%
Derivatives	-1,358	7,998	0.0%	0.0%	0.0%
Other	1,251,778	900,761	2.6%	2.0%	-0.6%
Other balances	626,710	1,273,200	1.3%	2.8%	1.5%
Cash deposits	2,559,777	2,243,339	5.3%	4.9%	-0.4%

