

LONDON PENSIONS FUND AUTHORITY

a review of the year  
for our members



# Annual Report

2004-05

## Chairman's message

In my statement last year, I referred to some recovery in equity markets and the fundamental principle of our funding strategy being that equities would outperform bonds over time. As anticipated, this proved to be a major issue over the past year as the results of the valuation unfolded.

Much of the year has been devoted to developing a funding strategy for employers, incorporating increases in contribution rates over a phased period of years and expectations of higher investment returns going forward. These are important factors in seeking to maintain the future of the fund and a return to full funding.

The increases in costs to most employers are significant and reflect a common experience in private sector pension funds. We have worked hard to communicate and explain these results, and are holding a special forum for employers on 20<sup>th</sup> July to explain changes in investment strategy.

The Board held a very productive away-day at the end of the year to enable a full and open discussion on developing our investment strategy to meet liabilities in line with the funding strategy. A public tender process is now underway to appoint managers for new mandates, and I shall report progress at the Forum.

The Government's proposed modernisation of the Scheme stalled in the New Year during the consultation period, and planned changes in the regulations are subject to further discussions. As I write, new proposals are emerging from Government and more news on that as progress is made.

We continue to review the efficiency and quality of our services to make

improvements. Agency work for London boroughs is an integral element of that and I am pleased to report that we retained the contract with Bexley following a tender process. Discussions continue with TfL on plans for working together.

On Board membership, I can report that the Mayor has agreed new arrangements to maintain continuity on the Board. My own appointment as Chairman has been extended to July 2007 and Michael Ward has been appointed as Deputy Chairman for the same period.

Those members nominated by the four political parties represented on the GLA have been re-appointed until July 2006 after the London borough elections, and thereafter their appointments will be made on a four year cycle. The appointments for other members will be subject to public advertisement in the autumn and have been extended pro tem until 31<sup>st</sup> December 2005.

The greater continuity and certainty that these appointments give is crucial in the implementation of major decisions being taken at the current time and I look forward to working with the Board for the remainder of my chairmanship.

I should conclude with a reference to the recent bombing incidents in London on 7<sup>th</sup> July. I am happy to report that, although many of our staff were affected, none were injured physically in the incidents and service at Dexter House was maintained over a difficult period.

I am grateful for the commitment and effort that staff continue to put in to the successful operation of the LPFA and thank them sincerely for the excellent work they have achieved in 2004-05.

Neil Newton July 2005  
Chairman

## Highlights 2004-05

- ~ On-time processing rises to 98.8%, satisfaction levels up and the numbers of complaints down.
- ~ Annual Benefit Statements issued to all scheme members.
- ~ "Right First Time" initiative makes headway
- ~ Funding Strategy Statement published and triennial valuation completed.
- ~ Government proposals to modernise scheme under discussion and being monitored.
- ~ Major review of investment strategy undertaken and changes in progress.
- ~ Active and responsible investment policy published.
- ~ Bexley agency contract held against competition.
- ~ Equality standard Level 3 completed in parallel with Level 4 planning.
- ~ Investors in People accreditation won for a further three years.
- ~ LGC Finance Award - 'Quality of service' and the Professional Pensions UK Pensions Awards - 'Public Sector Scheme of the Year'.

## Governance

Governance, in the public service context, is the leadership, direction and control of public service organisations to ensure that they achieve their agreed aims and objectives, and in so doing, serve the public's best interests. Good governance is a crucial element of effective public services. It leads to good management, good performance, good stewardship of public money, good citizen engagement and, ultimately, to good outcomes. Good governance encompasses both what is achieved and how things are done.

A new LPFA corporate governance framework was agreed during the year modelled on guidance issued by the Chartered Institute of Public Finance and Accountancy but adjusted to reflect best local government practice where applicable and the requirements placed on pension funds to demonstrate effective scheme governance.

The five pillars of LPFA's framework are accountability, structures and processes, reporting and internal controls, public policy statements and standards of behaviour. Details of LPFA's performance against the framework can be found in the Governance Report 2004-05.

During 2005-06 LPFA will conduct its first corporate governance 'self assessment' in a similar way to other local authorities who are required to undergo a comprehensive performance assessment under the best value regime. The self assessment will take into account the guidance issued by the Independent Commission for Good Governance in Public Services published in January 2005.

## LPFA Board members appointments

Neil Newton, Chairman	1 <sup>st</sup> July 2001 to 31 <sup>st</sup> July 2007
Michael Ward as Deputy Chairman from August 2005	1 <sup>st</sup> August 2004 to 31 <sup>st</sup> July 2007
Niaz Alam	1 <sup>st</sup> July 2001 to 31 <sup>st</sup> December 2005
Ray Ambrose	2 <sup>nd</sup> Jan 2002 to 31 <sup>st</sup> December 2005
Councillor Pamela Batty (Conservative)	1 <sup>st</sup> July 1998 to 31 <sup>st</sup> July 2006
Councillor Danny Connellan (Labour)	1 <sup>st</sup> August 2004 to 31 <sup>st</sup> July 2006
Andrew Cornwell	1 <sup>st</sup> July 2001 to 31 <sup>st</sup> July 2006
Councillor Serge Lourie (Liberal Democrat)	30 <sup>th</sup> October 1989 to 31 <sup>st</sup> July 2006
Dr Ann Robinson	1 <sup>st</sup> July 2001 to 31 <sup>st</sup> December 2005
Bill Roots	1 <sup>st</sup> July 2001 to 31 <sup>st</sup> December 2005
Jenny Rosser MBE	1 <sup>st</sup> July 2001 to 31 <sup>st</sup> December 2005

## Effectiveness and efficiency

LPFA continues to review the costs of services it buys and the unit costs of its administration. Commercial costing methods focussed cost control and the pricing of new business to maximise a fair contribution to fixed costs. A three year rolling plan evaluating the scope for further efficiencies was produced during the year and, for the next financial year, we have set a target to reduce costs by the equivalent or 2½% p.a. over each of the next three years.

Building on the developments of performance indicators and the "Right First Time" initiative started last year, a rolling series of process and functional reviews took place to ensure services remain effective and improve. The changes in retirement benefit processing that emerged involved key staff in their implementation both in practice and developing the training programme.

LPFA systems rely on computer and related technology to drive efficiencies, and innovations in deliverable systems continue to be implemented. After an evaluation of options for general ledger and management accounting a new system, which was subject to thorough testing, was in place for the start of the 2005-06 financial year.

Satisfaction levels rose to 96% in the year and the numbers of complaints dropped to 35. This reflects the continuing recovery in on-time processing to 98.8% of all cases being completed within the Charter Standards. We aim to get above 99% ~ the levels achieved in past years ~ and did so on the main case types but only achieved 98% on the more general enquiries.

## Customer satisfaction

	2001-02	2002-03	2003-04	2004-05
Satisfaction levels %	90	91	92	96
Cases on time %	99	94	98	99
Number of complaints	40	82	50	35

Further details of LPFA's performance can be found in the Performance Report.

## Investing the fund

The triennial valuation together with proposals to strengthen future sustainability through the preparation and publication of a Funding Strategy Statement were a major influence on strategy over the year. Developments to underpin the Myners principles on trustee duties and accountability ran alongside the continued implementation of long term asset allocation targets.

Despite continuing volatility in the markets, we have continued to build up the allocation to alternative assets, mainly private equity and property. Investment with the private equity managers is slow and interim investments have been made into private equity investment trusts to gain exposure to this sector. Investment in property is now close to target through investment in property unit trusts, and we continue to investigate other assets which can add value without undue risk.

Investment returns continue to disappoint due in part to weightings in equities and manager styles, in relation to market returns. Longer term, investment performance is above inflation though we need greater margins to improve funding levels.

All these factors were taken into account in a fundamental review of investment strategy at the end of the year. As a result, a public tender process is now running to select managers for new investment mandates which set higher performance targets within a reasonable degree of risk. For the active sub-fund, there will be currency hedging and a switch from traditional bonds to target returns ~ more news on this later in the year.

LPFA enforced its role as an active and responsible investor by publishing a new policy statement as part of the investment principles, and setting clear responsibilities for the external investment managers. Collaboration with other funds and institutions remains a vital role for LPFA in seeking to influence best practice, and Peter Scales is now a member of the Marathon Club. The Club's overall purpose is to stimulate more long-term thinking on investment actions, and greater emphasis on being responsible and active owners of assets.

Further details of LPFA's investment activities can be found in the Investment Report 2004-05.

### Asset allocation as at 31<sup>st</sup> March

	Active sub-Fund %	Target %	Pens sub-Fund %	Target %	Total Fund %	2004 %
Fixed interest	11	15	20	20	15	13.5
Index-linked	0	0	58	67	27	33.9
UK equities	35	35	9	6.5	23	22.5
Overseas equities	40	35	7	6.5	25	25
Alternative assets	10	15	0	0	5	2.9
Cash	4	0	6	0	5	2.2
	100	100	100	100	100	100

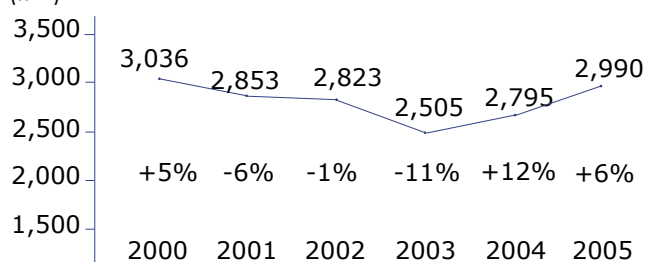
### Performance summary as at 31<sup>st</sup> March 2005

	1 Year	3 Years	10 Years
Active sub-Fund	10.7	0.6	5.6
Benchmark	11.9	2.3	7.0
Pensioner sub-Fund	6.1	6.6	8.0
Benchmark	6.3	6.3	7.9
Total Fund	8.5	3.6	6.7
WM All Funds (average return)	11.6	3.7	8.0
RPI (broadest measure)	3.2	3.0	2.6

### Largest equity holdings

	Mkt value £m
BP	£34.30
Vodafone	£25.50
Glaxosmithkline	£17.50
Barclays	£17.20
HSBC	£16.70
Lloyds TSB	£15.10
BHP Billiton	£14.50
Shell Transport	£13.20
Astrazeneca	£12.80
HBOS	£12.00

### Market value of Fund at 31<sup>st</sup> March 2005 (£m)



### Fund membership

	2001-02	2002-03	2003-04	2004-05
Contributors	22,444	21,862	21,460	21,473
Deferred pensioners	17,844	19,140	19,895	20,172
Pensioners	31,853	32,017	32,217	32,155
Total Fund membership	72,141	73,019	73,572	73,800

## Growing the business

Key partnerships with other pension administrators were planned to drive innovative administration options and the scope for joint initiatives with potential partners was investigated during the year. We have plans to embark on a joint web development with another administering authority and continue to have talks with other pension providers.

Winning and retaining key borough agency work remains a significant contribution to LPFA as an effective leading edge LGPS administrator. A new business implementation planning structure was completed and incorporated into the successful re-tender for LB Bexley pensions administration work and, ultimately, satisfactory revised contract negotiations were conducted with LB Hackney.

New services and products emerged from an inclusive development programme embracing new IT solutions to today's problems. A client 'needs and perceptions' survey was conducted with all agency clients and the reaction, generally, was positive. The corporate website was reviewed along with the communications strategy and a revised links page has been added. The Employer website was enhanced to allow online processing for retirements and this will be available to all participating employers by August 2006.

Fund membership numbers continue to remain fairly constant both in terms of the number of contributors and participating employers although the perceived high cost of final salary defined benefit schemes is causing some employers to review their options relating to occupational pensions scheme provision.

## Scheme modernisation

In a period in which the Government generally and ODPM for local government plan significant changes to the sustainability of pension schemes, LPFA was at the forefront of discussions and guidance on implementation.

ODPM issued a consultation paper in the Autumn of 2004 with plans to phase in substantial modifications to the local government scheme, to make it more relevant to today's workforce, simpler to understand and more sustainable into the future as a final salary pension scheme. Interim changes to the regulations were due to come into force in April 2005 but discussions with employer representatives broke down.

The ODPM have now revoked the changes with retrospective effect. We will keep members and employers informed of developments but if you are a contributor to the Fund you will find an insert within this Report explaining the effect of the changes.

## Integrating equalities

The drive to achieve the Local Government Equality Standard had a fundamental impact on LPFA in establishing comprehensive consultation procedures, improving equality of access to all services and operating employer best practice.

The programme of Impact Needs / Requirements Assessments (INRAs) against 21 functions and policies were, in the main, completed by January 2005. The INRA's evaluated performance in both employment and service delivery with regard to equalities.

Before any perceived inequalities could be addressed the Authority embarked on a period of consultation with specialist external organisations, e.g. Commission for Racial Equality, Employer's Forum on Disability, as well as a random 5% sample of the Fund membership, all pensioners living abroad, employers participating in the Fund, LPFA staff and Board members.

Some of this data is still being analysed but all teams have now set their equality targets for 2005-06 which they will monitor and report back on. These targets are published in the LPFA's Corporate Equality Plan which can be found on the corporate website or hard copies can be made available upon request.

During the year a 'preferred supplier' list was compiled. All approved suppliers and contractors must now have LPFA compatible policies relating to Equalities, Environmental issues and Health and Safety. We also ensure that supplier and contract opportunities are made available to smaller minority businesses.

All staff were involved in diversity training during the year and this will continue with a programme of long term activity ranging from regular team meetings discussing diversity to facilitated workshops on specific issues such as recruitment.

You, the Fund member, will be aware that we are a very 'customer focussed' organisation but we now aim to take that focus to the next level where we are not simply fair to everyone but also recognise and respect differences, and aim for an equal outcome for all.

Further details of LPFA's equality initiatives can be found in the Corporate Equality Plan.

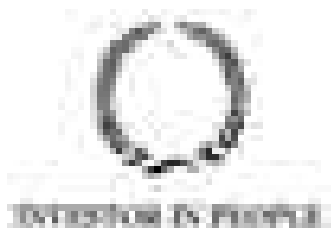
## Developing the workforce

The Authority was extremely pleased to retain its IiP accreditation for a further three years and this reflects the continuing development of the staff appraisal process and the strengthening of the human resource function to aid personal training and development.

Performance planning was improved greatly with new appraisal procedures and continued to strengthen an inclusive engagement process through all levels of the organisation. Recruitment processes were enhanced to deliver diversity targets and to meet equality shortfalls.

The 'away-day' concept for business planning was extended to managers this year and with an external facilitator produced useful input to the Performance Plan. Managers identified six priorities for improvement: internal communication, use of IT, business development, planning, clarity of structure and reputation management.

For the current year we aim to set training targets for individual posts, strengthen the feedback for future business planning via regular team meetings and further develop Board member training modules.



IiP accreditation was first awarded in 1996 and, following external assessment, was retained in 1999, 2001 and 2004.

## Workforce details

	2003-04	2004-05
Staff numbers	125	126
Staff turnover	8%	9%
Ave. number of days lost to sickness per person	10	9
Ethnicity		
White	76%	75%
Asian/Asian British	12%	11%
Black/Black British	8%	9%
Mixed	4%	4%
Chinese/Other	0%	1%

## Finance and accounting

The net assets of the pension fund increased by £195 million mainly resulting from a rise in the market value of investments. The total fund is now very close to the level achieved in March 2000 following the progressive falls in 2001 to 2003, the major reason for the funding problems now facing most defined benefit pension schemes. Fund income continues to exceed expenditure but with a maturing Fund membership profile this will revert in later years to a net outflow position.

Operational costs have risen by more than inflation due to higher staff costs reflecting increased activity on agency work and on the valuation. Residual liabilities in respect of added years and injury claims continue to decline steadily, and levies in the year were held or reduced by using spare balances.

Further detail of LPFA's financial activities can be found in the Financial Report 2004-05.

### Pension Fund Accounts

2003-04		2004-05
£'000		£'000
	Income	
107,091	Contributions receivable	115,069
32,856	Transfers in	67,426
139,947		182,495
	Expenditure	
159,920	Benefits payable	163,049
38,426	Leavers	51,497
4,040	Administration expenses	4,218
202,386		218,764
(62,439)	Net expenditure	(36,269)
	Returns on investment	
65,930	Investment income	72,083
293,965	Change in market value	162,842
(2,884)	Investment expenses	(3,853)
357,011	Net return on investments	231,072
294,572	Net increase in the Fund	194,803
2,500,145	Net assets 1 <sup>st</sup> April	2,794,717
2,794,717	Net assets 31 <sup>st</sup> March	2,989,520

## Operational Accounts

2003-04			2004-05	
£'000			£'000	
		Operational expenditure		
97		Board Members	103	
3,984		Staff	4,316	
1,236		Premises	1,283	
691		Information technology	695	
652		Office costs	671	
432		Other fees and expenses	423	
7,092		Cost of activities	7,491	
		Financed by:		
4,040		Charge to pension fund	4,218	
2,263		Agency contracts	2,365	
528		Funded from levy	524	
50		Other charges	52	
6,881			7,159	
(216)		FRS17 adjustment *	(332)	
(5)		(Surplus) deficit in year	0	

\* FRS 17 is financial reporting standard requiring accounting adjustments in relation to the cost of employer pension liabilities.

## Residual Accounts

2003-04			2004-05		
£'000			£'000		
Greater London	Inner London		Greater London	Inner London	
8,630	14,853	Net expenditure	8,346	14,680	
8,983	14,900	Less met from levies	7,453	14,900	
(353)	(47)	Net use of balances	893	(220)	
2,522	1,188	Balances as at 31 <sup>st</sup> March	1,629	1,409	

London Pensions Fund Authority  
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## Contacts

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