

LONDON PENSIONS FUND AUTHORITY



Annual Report 2003 - 04



Chairman's statement

Equity markets have recovered from the low point of March 2003 and, although the UK market has fallen back a little in recent months, we remain optimistic that equities will continue to outperform bonds over the long term ~ a fundamental principle of our funding strategy.

This is particularly relevant for the triennial valuation exercise now underway which will set employer contribution rates from next year going forward. These rates will need to rise as investment returns are not expected to reach the levels we enjoyed throughout the nineties and as retirement periods lengthen.

Yes, we are living longer, on average, and the next generation are expected to live even longer. This inevitably means that the cost of paying pensions will rise for the employer unless other factors change e.g. higher employee contribution rates or reduced benefits. Decisions taken in the valuation process will seek to ensure the sustainability of the Scheme over the long term. That is less important for those of you who are pensioners ~ your benefits are guaranteed ~ but it is essential to new joiners, many of whom will have a 40 to 60 year time horizon.

The Government continues to consult on changes to the Scheme, and a major paper on the future is expected in the Autumn with proposals for modernisation. We will continue to do all we can to preserve the fundamental benefits of our scheme notwithstanding the fact that all around us private sector organisations are closing down their final salary schemes.

During the last year new investments have been made in property, private equity, PFI schemes, and alternatives investigated that will add value to the fund. Systems have been reviewed and improved, audit reports are good, and service

providers renewed after open tender procedures. We continue to win more agency work for London boroughs, giving a healthy growth to LPFA operations. We are talking to other major pension funds about partnership working, sharing ideas and developing best practice in an effective and cost efficient manner. We are still winning industry-wide awards which reflect LPFA's prominence in the market.

Our own governance procedures have been reviewed and are being strengthened across-the-board from equalities, through human resources and performance appraisal, to environmental and risk management in a responsible way ~ all you would expect from a leading public sector pension fund.

I am very grateful for the commitment and effort made by our staff and thank them sincerely for a job well done in 2003-04.

On Board membership, Kumar Murshid resigned in March and Keith Toms' appointment came to an end in July. I welcome Michael Ward and Danny Connellan who have been appointed to the Board from 1st August.

I am grateful to the whole Board for their support over the past year, and I am particularly grateful to Keith for his dedicated input over three years.

I hope to be able to introduce our new members at the Fund Member Forum on 17th September and to welcoming many of you at the QE II Centre.



Neil Newton
LPFA Chairman

Neil Newton, Chairman

July 2004

Introductory comment

The style and presentation of the annual report and accounts has changed this year. There is no longer a single public document but four separate publications which combine to form the equivalent to previous years.

The first is this Annual Report which replaces the Autumn newsletter to fund members with a review of the year's activities, and brief summaries of performance against targets, investment activity, and the financial and accounting information

Each of the last three summarises the key elements of

the Performance Report, the Investment Report, and the Financial Report ~ the last being the formal statutory accounts of the Authority which are produced in accordance with statutory requirements and CIPFA guidance.

The purpose of these changes is to enable us to target specific audiences and interested parties with each document or combinations of all four. For you, the fund member and our principal audience, this report represents our accountability in a less formal and hopefully more readable format.

**Copies of the Performance, Investment and Financial Reports are available from
Dexter House or on LPFA's corporate website.**



The **aims** of the LPFA include the provision of quality services at optimum cost, to strengthen LPFA's standing through growth and contribution to public debate, and to strive for social and environmental best practice.

We work to meet those aims by adhering to organisational and individual staff **values**, and by delivering **strategic objectives**, set for a three year period, through a series of **key actions** in each year.

This somewhat theoretical statement is followed in practice, and during 2003-04, LPFA continued to make a significant and valued contribution to industry-wide developments relating to fund investment and management, scheme administration, professional guidance on best practice, partnership working, and active responsible investment activity. The report that follows highlights the key achievements and performance of the Authority and its staff.

Effectiveness and efficiency

An Annual Efficiency and Quality Plan was produced for implementation in 2004-05 as a benchmark for measuring improvements in the efficiency and quality of the services we provide. As an integral part of that process, we have designed a national index of Pensions Performance Indicators which is with the ODPM for consideration - scores shown are indicative using 2003-04 as an example.

LPFA Performance Index	Score
1 Investment costs as a % of fund value	9
2 Investment returns: Total Fund	0
3 Funding level: Total Fund as a %	10
4 % of members satisfied with the service	8
5 Complaints as a % of workload	7
6 Administration costs as % of Fund value	9
7 Administration cost per Fund member	4
8 Staff/Fund member ratio expressed as 1: X	6
9 Cases completed on time – top 10 cases only	8
10 Average elapsed time – top 10 cases	0
Total score	61

N.B. The scoring system uses benchmarks drawn from industry best practice.

On the ground, satisfaction levels rose slightly in the year and the numbers of new complaints dropped to 50. This reflects a recovery in on-time processing to 98% 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 did not do so well on more general enquiries.

In many cases, it is not just completing the task, it is making sure there are no mistakes which then get picked up in checking and delay the response. We have therefore introduced a new initiative called "Right First Time" which will look at all aspects of our work to speed up responses and improve quality.



Peter Scales
Chief Executive

Environmental Policy ~ Objectives 2004

- *Minimise consumption and waste and prevent pollution*
- *Ensure that environmental topics are integrated into our business activities*
- *Ensure that staff, contractors and partner organisations are aware of this Environmental Policy and encourage them to incorporate similar principles*
- *Individually, and in partnership with employing authorities, LPFA's landlord and other organisations, promote environmental information and raise awareness in stakeholders*
- *Encourage and support innovation and the use of sustainable resources*
- *Comply with all relevant environmental legislation, regulations and applicable codes of practice*
- *Maintain a rolling annual action plan, monitored quarterly and progress reported to the Senior Management quarterly, and to Board annually*

This policy will be reviewed every six months and reported to Senior Management

We reviewed our Environmental Policy and environmental management system using external help. An action plan is in process for 2004-05 and the new policy will form part of our corporate responsibility framework.

Investing the fund

New asset allocation targets were set way back in 2002 involving heavier weightings of equities overseas and some switching to alternative assets which would spread our investments more widely, without undue risk and with the prospect of higher returns. Switches within equity portfolios were made in 2002-03 but the weak equity markets delayed the move to alternative assets.

Asset Allocation - at 31st March 2004				
	Active sub Fund %	Pens sub Fund %	Total Fund %	2003 %
Fixed Interest	10.2	16.8	13.5	13.9
Index-linked	1.9	66.0	33.9	40.3
UK Equities	38.1	6.8	22.5	19.4
Overseas Equities	43.2	6.7	25.0	22.1
Alternative Assets	5.8	-	2.9	-
Cash	0.8	3.7	2.2	4.3
	100.0	100.0	100.0	100.0

Progress has been made in 2003-04 with new investments in property unit trusts and manager structures in place for private equity investments. A small investment was also made into a Private Finance Initiative (PFI) Fund which will help fund public sector developments (e.g. schools).

The move to alternative investments has yet to have any significant impact on investment returns.

Performance summary			
	31st March 2004	3 years	10 years
Active sub-fund	23.6%	-3.4%	4.6%
Benchmark	23.9%	-2.3%	6.0%
Pensioner sub-fund	7.6%	5.2%	7.6%
Benchmark	8.4%	4.9%	7.4%
Total Fund	14.7%	0.9%	6.0%
WM All Funds (average return)	22.6%	-0.3%	6.9%
RPI	2.6%	2.3%	2.6%

Performance in 2003-04 was influenced by sharp movements in global equity and bond markets and virtually wiped out the losses incurred in 2002-03. The 3 year and 10 year figures show a smoother picture and a more healthy comparison to RPI.

Regulations were introduced by ODPM requiring a Funding Strategy Statement (FSS) to be published by March 2005 supported by detailed guidance issued by CIPFA. The FSS is for agreement with employers and will set out how future pensions are to be financed, actuarial assumptions, contribution rates and investment strategies. These components are not new but the published statement of them as an agreed strategy will support the future sustainability of the pension fund.

These developments will progress during 2004-05 as the valuation exercise takes place. The result of the valuation will also inform a full review of investment strategy to meet the future liabilities of the Fund.

Responsible investing embraces active voting of shares with regard to social, environmental and ethical issues. LPFA's policy in this respect has been developing in line with Treasury policy and now incorporates industry-wide standards of best practice.

Largest Equity holdings 2004

Vodafone	£29m
BP	£26m
HSBC Holdings	£20m
Glaxo Smithkline	£18m
HBOS	£16m
Pfizer	£15m
Astrazeneca	£14m
Royal Bank of Scotland	£14m
Barclays	£12m
Shell Transport & Trading	£11m

Collaboration with other pension funds enables responsible and active engagement. LPFA is a member of the National Association of Pension Funds (NAPF), the Local Authority Pension Fund Forum and the Institutional Investors Group on Climate Change.



Growing the business

The growth in scheme membership that we have experienced in past years has slowed recently with some significant employers switching to the Civil Service scheme.

Looking back to 1994, the table shows a significant increase in contributors which has served to reduce the maturity of the fund. Looking back 10 more years to 1984, just prior to GLC abolition, total numbers were the same as in 1994 but many more contributors relative to pensioners as you might expect.

Fund membership	1984	1994	2004
Contributors	35,200	16,914	21,460
Deferred	5,050	13,954	19,895
Pensioners	23,400	32,862	32,217
Total	63,650	63,730	73,572

Discussions have been held with West Midlands Pensions Fund to investigate partnership arrangements which would serve our mutual interests in developing the efficiency and quality of the administration. A number of ideas have emerged (e.g. on annual benefits statements), exchange visits have been organised, and practical initiatives are being taken forward in 2004-05.

In a similar vein, we have been working with Transport for London as the only other funded pension scheme in the Greater London Authority family to identify joint working possibilities which not only save money but establish a stronger capability for providing pensions within the GLA.

In the wider London market, following our success in winning the contract at Brent at the end of 2002-03, we have taken on more agency work winning Hammersmith and Fulham, adding pensioner payroll for Westminster and Hackney and the Bexley contract was extended to 2005. The temporary support arrangements at Ealing were successfully concluded in March for hand-over to the new external administrator.

Ensuring effective management of this agency work is high on the Board's agenda and a full review of the pricing and costing of this work was completed in the year. The new structure has a more commercial focus for fixed cost recovery and has been audited by the District Auditor.

Scheme modernisation

The ODPM has been consulting local authorities on a number of issues underlying the administration of the scheme as part of an exercise they call "Stocktake". In effect, this has taken different aspects of the scheme and tested improvements or changes to modernise its operation.

In April 2004, revised regulations came into force following a period of consultation introducing detailed changes covering entitlement periods, aggregation of membership and the operation of the Internal Dispute Resolution Procedure.

Phil Goodwin, Director of Pensions Operations was named *Pensions Manager of the Year at the Pensions Management Magazine Awards in October 2003.* *The LPFA also won an award for best Investment Strategy using specialist managers. LPFA were named as Best Pension Fund - UK at the Investment & Pensions Europe Magazine Awards in November 2003.*



LPFA has played its part in the discussions and consultation processes that have taken place over the past year to ensure existing rights are protected. Members and employers have been kept informed of these changes and consulted where appropriate.

Further changes (e.g. '85 year rule') are in discussion for April 2005 and the ODPM intend to issue a substantive consultation paper on structural changes to modernise the scheme in the Autumn. This will involve a lengthy process of consultation and changes are not likely to take effect before April 2007.

Integrating equalities

The planned integration of equalities into all aspects of LPFA's operations has been given a high priority by the Board within an objective to achieve Level 5 of the Local Government Equality Standard by December 2005. Level 2 was achieved in 2003-04 and there is a substantial amount of review work underway to take this forward.

The Local Government Equality Standard will:

- Provide a systematic framework for the mainstreaming of equalities
- Help LPFA to meet its obligations under the law
- Encourage the development of anti-discrimination practice.
- Provide a basis for tackling forms of institutionalised discrimination.
- Provide a framework for improving performance over time.

LPFA will be able to assess progress based on five levels:

- Level 1: Commitment to a Comprehensive Equality Policy
- Level 2: Assessment and Consultation
- Level 3: Setting equality objectives and targets
- Level 4: Information systems and monitoring against targets
- Level 5: Achieving and reviewing outcomes

Initial action has been focused on setting up a Corporate Equality Plan and a steering group to oversee progress chaired by Andrew Cornwell. Further more fundamental work is in hand for 2004 to conduct impact needs and requirement assessments for individual functions and to establish effective consultation procedures.

One initiative in this respect has been to offer accommodation in Dexter House to the Mayor of London's Older People's Resource Facility. This not only enables LPFA to contribute to the mayor's strategies but to gain access to a communications network for older people in London.

Effective communication remains a key issue for LPFA, whether through web sites, e-mail or more traditional paper copy and we try to keep our scheme members and employers informed and engaged in LPFA developments.

Developing the workforce

Good internal communication is essential to developing an informed and motivated workforce. A new performance management and appraisal process for staff went live in April 2003 and with some minor modifications mid-year has proved a great success. This not only gives staff the opportunity to discuss their performance in a structured way, but also to identify their training needs.

To aid that process, the organisation of human resource functions has been redefined following external review and linked more closely with staff training and development. New recruitment procedures were put in place and a computerised personnel database (CIPHR) was introduced to aid management.

The business planning process of LPFA has become more participative during the year with the introduction of team business plans. These involve staff in delivering the strategy alongside core activities and feed into the planning process for future years.

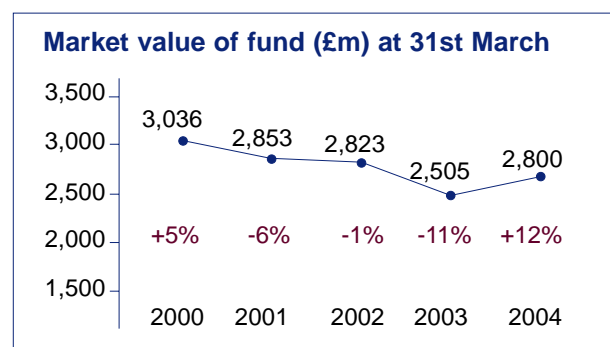
An 'awayday' to consider future strategy was held in June 2003 involving Board Members and senior management. A similar exercise is planned for 2004 to involve all managers.

"The Mayor of London's Older People's Resource Facility based in the LPFA's premises is proving to be a great success at providing practical support to older people's organisations across London with the work they carry out. All of the staff at the LPFA were very welcoming when we first moved into their premises at Dexter House earlier this year. We hope this arrangement continues in this positive way, and that the Greater London Authority (GLA), and LPFA can build on their relationship in the future."

GLA officers: Charlotte Smith, Anna Roberts

Finance and accounting

The **pension fund accounts** show a recovery in asset values at the year end to £2.8 billion, the same level as in March 2002.



Net fund revenue income, excluding changes in the market value of investments, continues to be positive.

Pension Fund Accounts		
2002-03 £'000	2003-04 £'000	
Income		
101,800	Contributions receivable	108,210
30,580	Transfers in	32,856
132,380		141,066
Expenditure		
154,554	Benefits payable	160,353
18,891	Leavers	38,426
4,075	Administration expenses	4,040
177,520		202,819
(45,140)	Net expenditure	(61,753)
Returns on Investment		
68,836	Investment income	65,930
(338,966)	Change in market value	294,165
(2,890)	Investment expenses	(2,884)
(273,020)	Net Return on Investments	357,211
(318,160)	Net increase in the Fund	295,458
2,823,027	Net assets 1st April	2,504,867
2,504,867	Net assets 31st March	2,800,325

The **combined accounts** show details of the operating costs and how they have been financed in part from the pension fund and recovered as charges for agency services.

The financing of unfunded benefits (e.g. added years) and other residual liabilities (e.g. injury claims) inherited from the GLC and ILEA is from levies on London boroughs of £24m and £9m recoverable from other bodies.

Combined Accounts		
2002-03 £'000	2003-04 £'000	
Operational expenditure		
98	Board Members	97
3,468	Staff	3,984
1,199	Premises	1,236
708	Information technology	691
701	Office costs	652
300	Other fees and expenses	432
	Residual liabilities and unfunded benefits	33,992
34,128		
40,602	Cost of activities	41,084
Financed by:		
4,075	Charge to pension fund	4,040
1,791	Charges for services	2,313
8,808	Recoverable benefits	9,108
1,989	Investment income	1,929
23,883	Levy on London boroughs	23,883
40,546		41,273
170	FRS17 adjustment *	216
(114)	(Surplus) / deficit in year	(405)

* FRS17 is a financial reporting standard requiring accounting adjustments in relation to the cost of employer pension liabilities.

There are two independent reports included in the accounts, from the auditor and the actuary:

For the Audit Commission, the District Auditor's report on the financial statements is based on his review and assessment of the conclusions drawn from audit evidence obtained in the course of the audit. The opinion is unqualified.

The Actuary's report is based on the last full valuation in March 2001. The interim valuation, (December 2002) did not require any adjustment to contribution rates. The next full valuation, as at 31st March 2004, is currently in progress.

Ways to contact LPFA

If you are a pensioner:

A local rate telephone number **0845 30 30 335** is available.

e-mail: payroll@lpfa.org.uk

If you are a contributor to the Fund or a deferred pensioner:

The telephone number for contributors and deferred members is **020 7369 6118**.

e-mail: enquiries@lpfa.org.uk

Other contact numbers

Facsimile: 020 7369 6111

Textphone: 020 7369 6119

LPFA websites

Access to your pension records is available via LPFA's secure member website:

www.yourpension.org.uk

Details about the LPFA, services provided, corporate publications and events can be found on the corporate website at:

www.lpfa.org.uk/corporate

This Report is also available in large print and on audio cassette.

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