

Pension Fund Unaudited Annual Report and Accounts **2022/23**



SHETLAND
ISLANDS COUNCIL

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Management Structure

Administering Authority

Shetland Islands Council
Town Hall
Lerwick
Shetland
ZE1 0HB

Fund Custodian

The Northern Trust Company

Investment Advisor

Isio

Investment Managers

Blackrock
Schroders
KBI Global Investors Limited
Newton Investment Management Limited
Baillie Gifford
Permira

Fund Actuary

Hymans Robertson LLP

Banker

Bank of Scotland

AVC Providers

Prudential
Equitable Life (closed to new members)

Independent Auditor

Audit Scotland

Website

www.shetlandpensionfund.org

Management Commentary

Welcome to Shetland Islands Council Pension Fund's (the 'Pension Fund') Annual Report and Accounts for the year ended 31 March 2023. The purpose of the Management Commentary is to present an overview of the Pension Fund's performance during the financial year 2022/23 and to help readers understand the Pension Fund's financial position at 31 March 2023. In addition, it outlines the main uncertainties facing the Pension Fund for the financial year 2022/23 and beyond.

Background

The Shetland Islands Council Pension Fund is part of the Local Government Pension Scheme (LGPS). It is administered by Shetland Islands Council for the purposes of providing pensions and other benefits for current members, deferred members, retired members and dependants of a range of Scheduled and Admitted bodies within Shetland.

The Pension Fund is governed by the Superannuation Act 1972 and is administered in accordance with the following legislation:

- the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended);
- the Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014 (as amended);
- the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015.
- The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016

Teachers are not included as they are members of the Scottish Teachers' Pension Scheme.

Membership

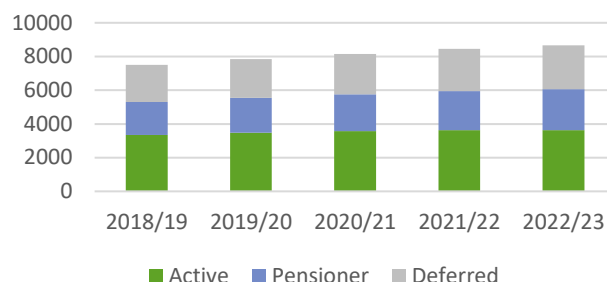
Membership of the Pension Fund comprises:

Active members	are employees who currently contribute to the LGPS.
Retired members	are in receipt of a pension, including spouses or dependants in receipt of a pension in respect of a former member.

Deferred members

are former active members who have elected to retain their rights in the LGPS until they become payable.

Pension Fund Membership



Employers with active members at 31 March 2023

Scheduled Bodies:

- Shetland Islands Council
- Orkney & Shetland Valuation Joint Board

Admitted Bodies:

- Lerwick Port Authority
- Shetland Recreational Trust
- Shetland Amenity Trust
- Shetland Seafood Quality Control
- Shetland Charitable Trust
- Shetland Arts Development Agency
- Shetland Care Attendant Scheme (previously Crossroads)
- Shetland UHI

During the year, one Admitted Body (Shetland – Highlands & Islands Enterprise (HIE)) who had no active members and was closed to new members, ceased participation in the Fund on 31 October 2022. Remaining deferred and pensioner members of Shetland HIE transferred to Highland Council Pension Fund.

Impact of COVID-19 and moving forward

Pension administration backlogs from COVID-19 continued to impact the Pension Fund's activities during 2022/23. Administratively, the Pension Section is near completion of recruiting to its vacant posts. This will ensure the Pension Fund continues to meet its requirements moving forward and

deliver an exceptional service to all members, employers and other stakeholders.

Pension Fund Committee and Pension Board meetings continued to take place during the year, with hybrid arrangements were increasingly used to facilitate attendance. Committee and Board Members, other Members, officers and external advisors were able to attend meetings in person or remotely, as necessary. These arrangements enabled routine business to be conducted through the year without any significant or adverse impact on the governance of the Council's activities.

Looking ahead to 2023/24, challenges still remain. The rising cost of living, increasing interest rates and global unrest presents some uncertainties. However, the Pension Fund will continue to move forward and adapt to these changing situations.

Pension Fund Purpose and Objectives

The Pension Fund's primary purpose is to provide for scheme members' pension and lump sum benefits on their retirement, or for their dependants on death before or after retirement. The Pension Fund receives contributions from employees and employers which are invested in order to pay out defined benefits, in line with LGPS regulations. In order to achieve this, the Pension Fund seeks to:

- secure and maintain sufficient resources to meet all liabilities as they fall due,
- mitigate the risk of failing to meet these liabilities, through an Investment Strategy specifically tailored to the Pension Fund's requirements,
- maximise investment returns within acceptable and reasonable parameters,
- provide stability in the level of employers' contribution rates, and,
- become fully funded by 2027. This means that the Pension Fund would be able to pay all liabilities due at that time and at any time in the future.

The Pension Fund's Investment Strategy is therefore central to achieving these objectives.

Investment Portfolio Review

During 2021/22, the Pension Fund reviewed its investment strategy to ensure it remains well placed to achieve the objectives set out above. The review

with assistance from investment consultants Isio concluded on 9 February 2022, when the Pension Fund Committee approved a new Investment Strategy.
<https://coins.shetland.gov.uk/agenda.asp?meetingid=7151>

The new investment strategy after conducting tender exercises awarded three new investment mandates in, global equities, private credit and infrastructure equity. The new investment strategy retains a focus on growth, through an increased allocation to equity investments, while providing an element of stability, diversification and inflation-proofing to the investment portfolio with new allocations to private credit and infrastructure equity. Investments in diversified growth and alternative credit assets will end, in order to facilitate the reorganisation of Pension Fund assets in line with the new Investment Strategy.

During 2022/23 the reorganisation of the strategy saw the alternative credit fund end with the corresponding cash invested in new mandates. Investments were also made with new fund managers in global equities and in a private credit fund.

The reorganisation of the Pension Fund's investments into the new strategy will take place gradually over a couple of years, as investment opportunities arise within the new asset classes.

Investment Portfolio

The Pension Fund's current investment portfolio has a value of £652m as at 31 March 2023, compared to £656m at the start of the year. The composition of the current investment portfolio is shown below, along with a brief description of the investment class and the specific external fund manager who manages those investments on the Pension Fund's behalf.

Equities

Equities are the main investment asset class, and currently account for 78% of the Pension Fund's investment portfolio. Equity investments are shareholdings in companies which fund managers buy and sell. Income is generated in the form of dividend payments or capital gains when shares are sold.

The Fund spreads equity investment risk by investing with three fund managers, a passive equity fund manager and two active equity fund managers. Passive equity investment tracks a specific market index (such as the FTSE 100), and the proportion and value of shares held mirrors the same index, so if the markets rise or fall so too does the value of the investment. Active equity investment involves the identification of companies that fund managers think will outperform other companies within an index, and buying shares that are expected to deliver the best dividends or increase in value.

Property

The Fund invests in property assets throughout the UK, with investments in a range of different sectors such as retail units, shopping centres, industrial units, student accommodation and offices. Investments are made into a variety of property unit trusts and funds, which spreads the investment over a greater number of properties.

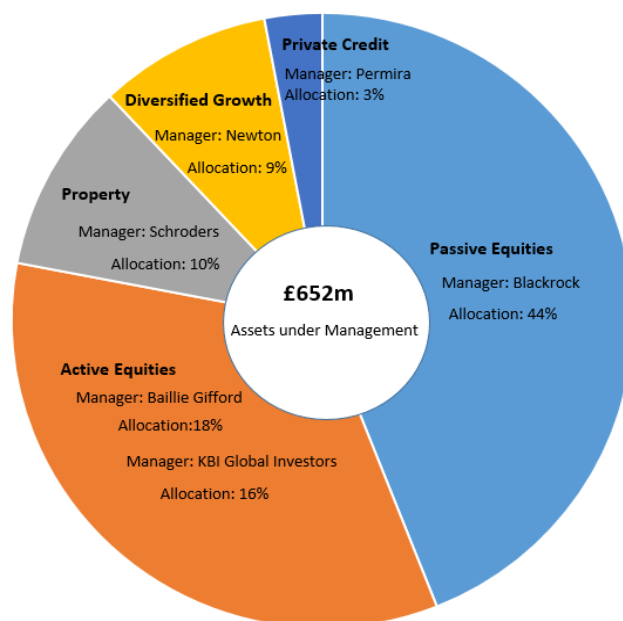
Diversified Growth

The diversified growth fund seeks to achieve similar returns to an equity investment but without the same risk of volatility. The growth fund does this by investing across a wide range of assets. The Fund's investments are a combination of traditional assets such as government bonds, listed equities and corporate bonds along with other asset classes such as emerging market debt, commodities, gold and infrastructure.

Private Credit

This is a new asset class for the Pension Fund with just an initial investment to date. Private credit involves a fund manager giving loans to small medium sized private companies. Income is received as interest and is charged on the loans. The loans are structured with security over assets and rank very high against other company debt.

Pension Fund Investment Portfolio: Current Allocation

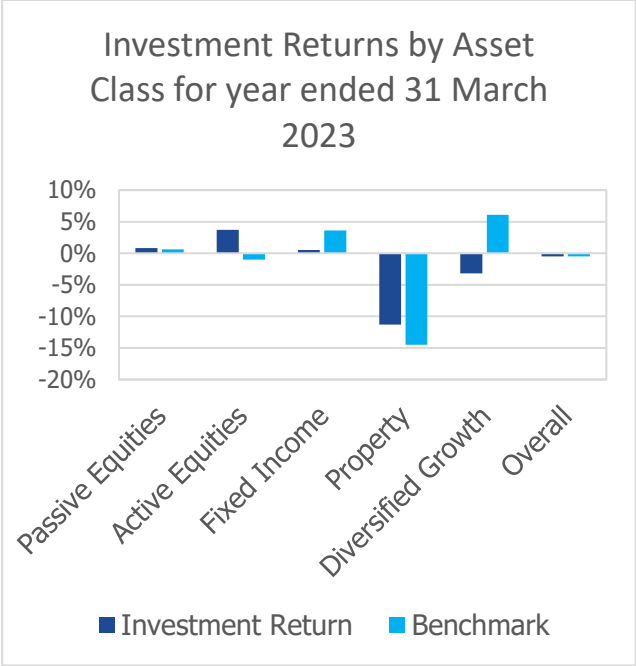
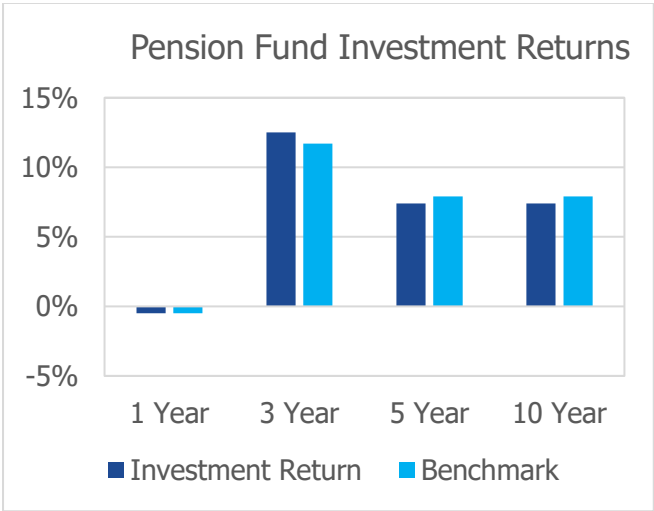


The investment portfolio struggled over the first half of the financial year, as all of the main investment markets fell in value. The ongoing conflict in Ukraine not only created global concern but was a contributing factor in the increase in global energy and food costs. This saw a steep rise in inflation and then in interest rates as central banks tried to combat inflation.

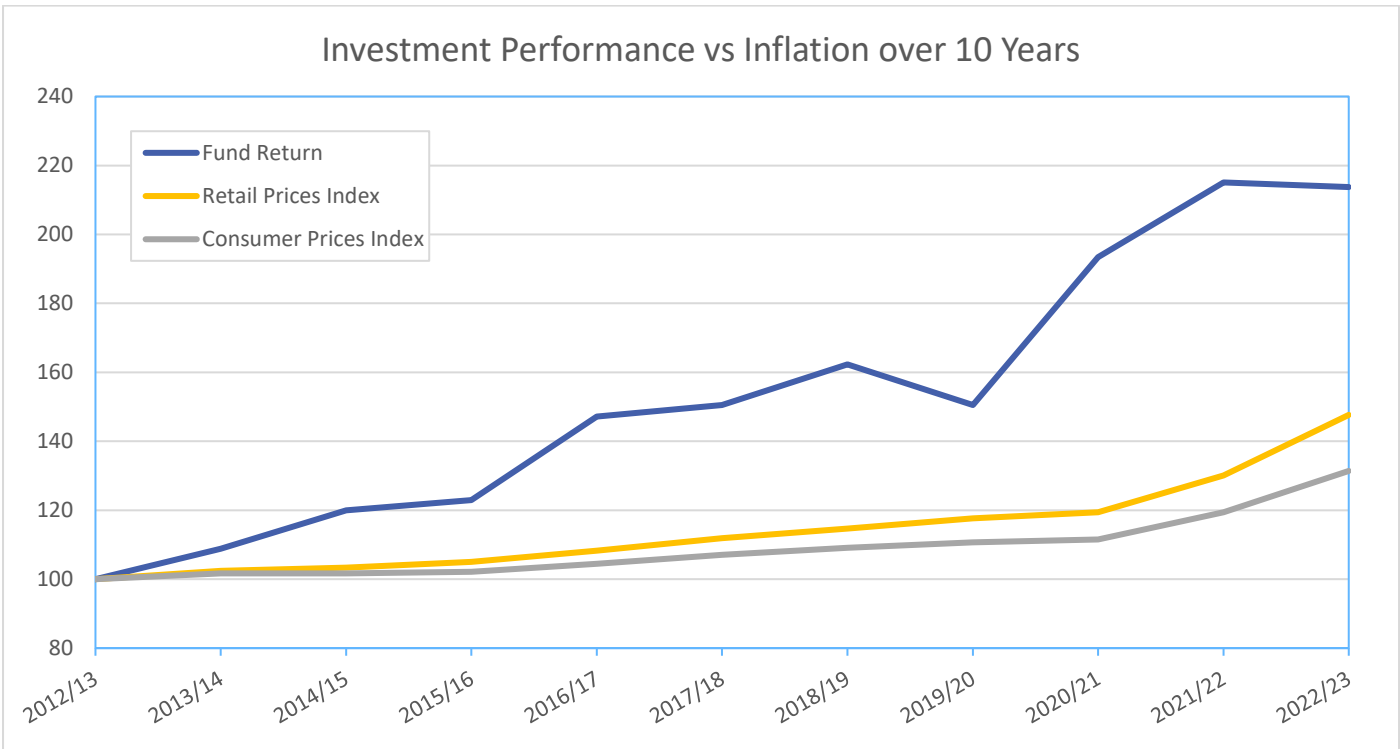
During the second half of the financial year the markets recovered as it was believed that inflation was nearing its peak and future interest rate rises would not be as severe as predicted. Market volatility was again seen near the end of the financial year with anxiety in the banking sector as two US banks and a Swiss bank failed and were bought over.

Further detail about the performance of the current investment portfolio can be found in the annual investment performance report.
<http://coins.shetland.gov.uk/submissiondocument.s.asp?submissionid=28939>

The Pension Fund’s current short, medium and longer term investment returns are summarised as follows:



The chart below shows the Fund’s investment performance over the last ten years versus inflation. Over the longer term, the Fund’s assets have grown positively in value on an annualised basis, outstripping inflation. However, actual returns vary on an annual basis reflecting the volatile nature of the Fund’s investment portfolio.



Investment arrangements and policies

The Pension Fund has a range of arrangements and policies in place to ensure the Council, as the administering authority, fulfils its fiduciary duty to maximise the Funds’ investment returns balanced against an appropriate level of risk.

The Fund utilises the service of fund managers, who have delegated powers for the acquisition and realisation of investments. As part of their internal investment decision-making processes, fund managers are expected to consider all factors, including the social, environmental and ethical policies of companies in which they may invest, to

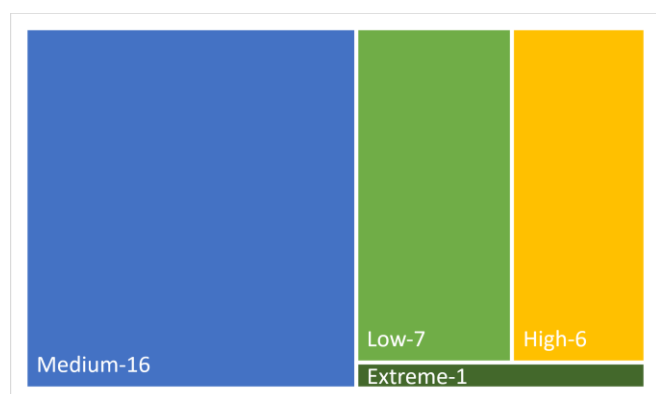
the extent that these may materially affect the long-term prospects of such companies.

All the fund managers have signed up to the United Nations Principles on Responsible Investment Management. The principles reflect the view that environmental, social and corporate governance (ESG) issues can affect the performance of investment portfolios and must be given appropriate consideration by investors if they are to fulfil their fiduciary (or equivalent) duty.

The focus of the Pension Fund's **Investment Strategy** is to achieve a 100% funding level whereby the Pension Fund's incoming contributions equal the benefits payable, by 2027. Beyond this point in time, the Pension Fund anticipates that benefit payments will not exceed the level of contributions made by employers and employees into the Pension Fund. The recently approved Investment Strategy advocates investment in growth oriented equities, balanced with diversification in investments such as property, infrastructure and private credit asset categories in order to reduce the exposure to risk and volatility within acceptable parameters.

Risk

The Pension Fund maintains a risk register which is updated regularly. The latest iteration of the risk register, published in May 2023, contained a total of 30 risks, summarised by risk level in the following heat map:



<https://coins.shetland.gov.uk/Agenda.asp?meetingid=7760>

The highest rated risk (extreme) to the Pension Fund is:

- adverse movement in bond yields, which could result in greater liabilities than anticipated.

The Pension Fund Committee and Pension Board are made aware of any changes, so that action can be taken to mitigate the risks.

Funding Strategy Statement

The regulations covering management of the LGPS Pension Funds require the administering authority to prepare, maintain and publish a written Funding Strategy Statement. A revised Funding Strategy Statement was adopted in March 2021, as part of the triennial valuation process. The Funding Strategy Statement will be reviewed again as part of the 2023 triennial valuation process. Details of the Funding Strategy Statement are found in Note 17: Funding Arrangements, on page 37.

The Funding Strategy Statement can be found here: <http://coins.shetland.gov.uk/submissiondocuments.asp?submissionid=26265>

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 employee contribution rates as possible; and
- to take a prudent longer-term view of funding those liabilities.

The most recent actuarial valuation was carried out as at 31 March 2020. It showed that the Pension Fund was valued at £461m and 92% funded, with a deficit of £38m. The triennial valuation includes setting the employer contribution rates for the next three years. The primary employer contribution rate across the whole fund is 22.3%, with additional secondary rates that adjust the final contribution rates payable by individual employers, depending on their specific circumstances with regards to membership and associated assets and liabilities.

The 31 March 2023 triennial valuation process is in the process of being carried out. This will set the Employers' rates for 2024/25, 2025/26 and 2026/27.

Statement of Investment Principles

The Pension Fund Committee and the Pension Board meetings on 31 August 2022 approved the current Shetland Islands Council Pension Fund Statement of Investment Principles. This statement includes administration details, the objective of the Pension Fund, types of investments, balance between different types of investment, risk, expected return on investments, realisation of investments, responsible investments, securities lending and

compliance. The current portfolio of investments does not align with the specific allocations set out in the Statement of Investment Principles. This is because investments have been made on the basis of market conditions, which has resulted in a variation to the fixed allocation set out in the Statement of Investment Principles. The Pension Fund is currently reviewing its Investment Strategy following the latest formal valuation which will result in changes to the allocation of asset categories within the investment portfolio. The Statement of Investment Principles was updated in August 2022 to reflect a permissible range of asset allocations rather than a fixed percentage.

The new statement of Investment Principles as approved by the pension fund committee on 31 August 2022, can be found here: <https://coins.shetland.gov.uk/submissiondocuments.asp?submissionid=28075>

The Pension Fund also complies with the six Myners Principles, which were contained in Appendix B to the Statement of Investment Principles.

Competition and Markets Authority Compliance

As a result of the coming into force of the Occupational Pension Schemes (Governance and Registration)(Amendment) Regulations 2022, compliance with part 7 of the Investment Consultancy and Fiduciary Management Market Investigation Order 2019 is now confirmed through the Annual Accounts. Shetland Islands Council pension fund committee assessed the Pension funds advisors at their meeting on 31 August 2022, recording a satisfaction score of 92.4%. An updated statement of Investment principles was approved by the committee and board at this time. The council as the administering authority of the Shetland Islands council Pension fund has complied with part 7 of the investment Consultancy and Fiduciary Management Market Investigation Order 2019.

Performance Management

The Annual Accounts satisfy the requirements of Regulation 55 (1) of the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended), to prepare a Pension Fund Annual Report for the financial year from 1 April 2022 to 31 March 2023. In addition, quarterly Management Accounts are presented to the Pension Fund Committee, which

shows the year to date position and the projected year-end outturn.

Primary Financial Statements

The Annual Accounts summarise the Pension Fund's transactions for the year and its year-end position at 31 March 2023. The Annual Accounts are prepared in accordance with the International Accounting Standards Board (IASB) Framework for the Preparation and Presentation of Financial Statements (the IASB) Framework as interpreted by the Code of Practice on Local Authority Accounting in the United Kingdom (the Code).

The two primary statements, the Pension Fund Account and Net Assets Statement, as at 31 March 2023, include a description of their purpose. Accompanying the two primary statements are notes to the accounts, which set out the accounting policies adopted by the Pension Fund and provide more detailed analysis of the figures disclosed in the Primary Financial Statements.

The primary financial statements and notes to the accounts, including the accounting policies, form the relevant Annual Accounts for the purpose of the auditor's certificate and opinion.

Financial Performance 2022/23

The Pension Fund accounts present the full economic cost of providing Pension Fund services for 2022/23 and this shows a net income of £0.5m. This differs from the draft outturn position, shown

below. The draft outturn report will be presented to the Pension Fund Committee and the Pension Board on 26 June 2023:

Description	2022/23 Annual Budget £000	2022/23 Draft Outturn £000	2022/23 Variance £000
Total Expenditure	19,543	22,737	3,194
Total Income	(26,193)	(31,710)	(5,517)
Net Income	(6,650)	(8,973)	(2,323)

The main difference between the draft outturn and the final accounts is that the Pension Fund Account includes the value of the growth of the Fund and income automatically reinvested into the Fund. This income is not included in the table above.

Expenditure was higher than budgeted due to a greater number of lump sums paid out during the year than had been estimated. More people than anticipated retired during 2022/23 resulting in an increase in benefits payable. Income was greater than anticipated mainly due to income distributions on investment loans from a new fund manager which was not anticipated. Contributions received were higher as were transfers in, due to a higher number of transfers than projected.

Budgets set for lump sums, transfers in and out, death benefits and AVC in and out are based on five-year averages. It is difficult to estimate these items accurately as there is a huge amount of personal choice or life events involved in what is received and paid out, and therefore these transactions cannot be fully predicted. Expenditure, such as lump sums and transfers are based on a number of variables and will be different for each individual transaction.

Administration Strategy

The Pension Fund's Pension Administration Strategy highlights the duties of, and sets the performance for, both the Fund and all of the participating employers.

Employers must provide accurate information to the Pension Fund in a timely manner, to ensure that information provided to Fund members is also

accurate and timely. The information received from employers to the Pension Fund, such as new starters, leavers, retirements and deaths was delivered in a timely manner during 2022/23.

All employer's contributions in 2022/23 were received by the 19th of the month following deduction.

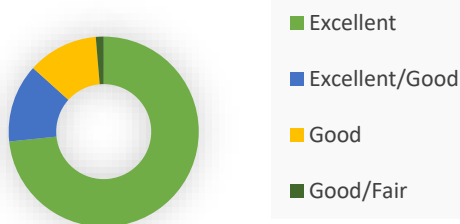
Administration Performance

Shetland Islands Council, as administering authority, is also committed to providing a high quality service to both members and employers and to ensure members receive their correct pension benefit entitlement.

To ensure excellent customer care is provided, retiring members and employers participating in the Fund are invited to complete a customer satisfaction survey.

Eight employer surveys were returned which indicated 75% of respondents rated the service received as excellent and 25% rated the service as good.

Member Satisfaction Survey



The chart opposite summarise the latest member satisfaction survey results, a total of 75 surveys were received. As well as administering employer contributions, retirements and pension payments, the Pension Section also processes the pensioners' payroll.

The table below shows the summarised budget and spend for the Pension Fund's administration costs for 2022/23:

Administration Expenses	2022/23 Annual Budget £000	2022/23 Draft Outturn £000	2022/23 Variance £000
Staff Time Allocations	383	320	63
Supplies, Services & Systems	108	109	(1)
Printing & Publications	3	3	0
Total	494	432	62

Staff Time Allocations were underspent due to a vacancy.

The Pension Administration KPI's for 2022/23 are:

Key Performance Indicator	Target	31 March 2023			31 March 2022		
		Number	Number within target	% within target	Number	Number within target	% within target
New starts	2 months from date of joining scheme	614	614	100%	649	649	100%
Leavers	2 months from leaving scheme	403	399	99%	255	226	89%
Transfer in quotes	2 months from date of transfer quotation	52	52	100%	50	48	96%
Transfer out quotes	3 months from date of request	42	42	100%	20	20	100%
Notifying members of benefits on retirement	1 month from date of retirement	157	157	100%	157	157	100%
Retirement estimates	2 months from date of request	98	94	96%	174	173	99%
Calculation of dependants benefits	2 months from notification	31	31	100%	30	30	100%
Annual Benefits statement - to all active and deferred members	by 31 August each year	5,788	5,788	100%	5,887	5,887	100%
Contributions from employers	by 19th of month following deduction	120	120	100%	108	107	99%

Monitoring Arrangements

The Pension Fund Committee and Pension Board receive regular updates on performance and the Committee papers and minutes are available via the Council's committee management system website: <http://www.shetland.gov.uk/coins/>.

Reports are prepared on a quarterly basis for the Pension Fund Committee and Pension Board that give an overview of the position of the Pension Fund's external investments and present a summary of each Fund Manager's performance for the quarter and over a three-year period.

In line with the Pension Fund's governance arrangements to monitor and review Fund Managers, the Pension Fund Committee and Pension Board invite Fund Managers to attend the quarterly meetings to give presentations on their mandates and investment performance. During COVID it was not possible to invite fund managers to give presentations but as 2022/23 progressed we were able to restart these presentations, and Schroders gave a presentation at the August meeting to the Pension Fund Committee and Pension board.

The Fund Managers supply a quarterly audited performance review report and monthly valuation report.

Membership of the Pension Board consists of trade union representatives and employer representatives, drawn from Shetland Islands Council and scheduled or admitted bodies in membership of the Pension Fund.

Remuneration Report

There is no requirement for a remuneration report for the Pension Fund, as the Pension Fund does not directly employ any staff.

All staff are employed by Shetland Islands Council and its costs are reimbursed by the Pension Fund. The Councillors who are members of the Pension Fund Committee and Pension Board are also remunerated by Shetland Islands Council. They do not receive any additional allowance for being members of the Pension Fund Committee or Pension Board. Trade union, and admitted and scheduled bodies members similarly do not receive any additional allowance for their role.

Details of Senior Councillors and Senior Employees remuneration can be found in the annual accounts of Shetland Islands Council, which are available on the Council's website.

Looking Ahead

Impact of COVID-19 in 2022/23

As alluded to earlier in this commentary, COVID-19 has necessitated changes to way the various teams involved in pensions administration, governance and investment have had to work. Staff have demonstrated a great deal of flexibility and resilience despite the disruption experienced, and have continued to deliver high quality services which reflected in the latest satisfaction survey scores. As restrictions have been lifted, staff returned to work in offices on a more regular basis, as the wider Council prepares to embrace an element of remote or home working as part of a new normal. Any new arrangements will fit around the continued provision of high quality services.

Consultation on the Future of Scottish LGPS Funds

The consultation about the structure of the Scottish LGPS, commissioned by the Scottish Scheme Advisory Board (SAB) during 2018/19 is still ongoing. The results of the initial consultation were 68% in favour of status quo or collaboration, 2% for pooling and 30% for merger. Since the initial results were reported, the SAB have commissioned further work to explore the benefits of a fully-merged model. The SAB after consulting with Scottish Government Ministers have now paused its work on the structure review until the outcome of the England and Wales review of pooling, and the proposed merger of Lothian and Falkirk Funds becomes clearer.

2023/24 Budget

The 2023/24 budget for the Pension Fund was approved on 8 March 2023. The budget anticipates the Pension Fund generating income of £28.3m and incurring total expenditure of £22m, resulting in net income of £6.3m. A range of assumptions and historical trends are used to inform the development of the budget for the Pension Fund. Due to the level of individual choice involved in choosing when to retire, the budget represents the most reasonable estimates of income and expenditure at that time, but it is not an exact science and is therefore liable to change throughout the year.

.....
Emma Macdonald
Leader of the Council
Chair of the Pension Fund Committee
26 June 2023

.....
Maggie Sandison
Chief Executive
26 June 2023



.....
Paul Fraser, CPFA
Executive Manager - Finance
26 June 2023

Annual Governance Statement

Introduction

This Annual Governance Statement explains how the Council, as the Administering Authority for the Shetland Islands Council Pension Fund, has complied with the principles of the CIPFA/SOLACE Framework 'Delivering Good Governance in Local Government' for the year ended 31 March 2023. It sets out the Council's governance arrangements and systems of internal control, and concludes on their effectiveness. The arrangements put in place by the Council apply equally to the activities of the Pension Fund

Scope of responsibility

Shetland Islands Council is responsible for ensuring that its business is conducted in accordance with the law and that public money is safeguarded, properly accounted for and used economically, efficiently and effectively. The Council has a statutory duty to make arrangements to secure Best Value under the Local Government in Scotland Act 2003.

In discharging these overall responsibilities, the Council is responsible for establishing proper arrangements for the governance of its affairs, including the stewardship of resources at its disposal and arrangements for the management of risk.

The Council reviewed and updated its Code of Corporate Governance in August 2018 which sets out seven fundamental elements that govern how the Council conducts its business. The Code of Corporate Governance is consistent with the CIPFA/SOLACE Framework 'Delivering Good Governance in Local Government', which was published in 2016.

The Council has a system of internal controls in place designed to manage risk to a reasonable level. Internal controls cannot completely eliminate the risk of failure to achieve strategic priorities and outcomes, but they can provide a reasonable level of assurance.

The system of internal controls is regularly reviewed to identify and prioritise the risks to the achievement of the Council's strategic priorities and outcomes, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The Purpose of the Governance Framework

The governance framework consists of the systems, processes, culture and values by which the Council is directed and controlled. It enables the Council, and therefore the Pension Fund, to monitor the achievement of its strategic priorities and to consider whether those priorities have led to the delivery of appropriate, cost-effective services.

The Governance Framework

The governance framework adopted by the Council is consistent with the seven core principles of the CIPFA/SOLACE framework illustrated below:

A	<i>Behaving with integrity, demonstrating a strong commitment to ethical values and respecting the rule of law.</i>
B	<i>Ensuring openness and comprehensive stakeholder engagement.</i>
C	<i>Defining outcomes in terms of sustainable economic, social and environmental benefits</i>
D	<i>Defining the interventions necessary to optimise achievement of intended outcomes.</i>
E	<i>Developing the entity's capacity, including the capability of its leadership and the individuals within it.</i>
F	<i>Managing risks and performance through robust internal control and strong public financial management.</i>
G	<i>Implementing good practices in transparency, reporting and audit to deliver effective accountability</i>

The governance framework has been in place for the year ended 31 March 2023 and up to the date of approval of the annual accounts.

The key elements of the Council's governance framework include:

- the **legal powers, duties and functions** of the Council, and roles and responsibilities of the people who take decisions on behalf of the community;

- **Scheme of Administration and Delegations**, which detail the functions that the Council has asked officers to carry out on its behalf, and the conditions they must comply with in doing so;
- **Standing Orders**, which set out the rules around how committees are run and decisions are made;
- **Financial Regulations**, setting out how the Council manages its financial affairs in accordance with good practice and statute;
- **Contract Standing Orders**, which set out the principles and rules about contracting with other parties;
- the Council's **Performance Management Framework**, which sets out how the Council sets its objectives, monitors and reports on its performance against those objectives and identifies areas for improvement;
- **Compliance** with CIPFA codes of practice and the CIPFA Statement on *the Role of the CFO in the Local Government Pension Scheme*.
- A **comprehensive programme of internal audit reviews** across different service areas, which provides assurance about the effectiveness of the system of internal controls and identifies areas of improvement.

The Council's suite of governance documents, including the Scheme of Administration and Delegation, Financial Regulations, Contract Standing Orders and Code of Corporate Governance can be found on the Council's [website](#).

In addition to complying with the governance framework approved by the Council, LGPS regulations require each Administering Authority to publish a Governance Compliance Statement that sets out how their governance arrangements comply with best practice issued by the Scottish Ministers. The Pension Fund's Governance Compliance Statement can be found on page 14. Where compliance does not meet the required standard, there is a requirement for Administering Authorities to set out any reasons for non-compliance in their Governance Compliance Statement.

Review of Effectiveness

The Pension Fund is responsible for ensuring the governance framework and systems of internal control remains effective. The Pension Fund conducts an annual review of the effectiveness of the overall governance framework. The review is informed by evidence from different sources:

- Internal management;
- Internal audit reviews;
- External audit reports; and

- Investment Fund Managers and the Custodian.

i) Internal management

Administration of the Pension Fund is directly within the remit of the Director of Corporate Services and assurance has been sought from the Director in relation to the effectiveness of internal financial controls. This assurance provides the opportunity to highlight any weaknesses or areas of concern that should be considered. For 2022/23, no areas of weakness or concern were identified.

In relation to the effectiveness of the Council's arrangements with regard to its statutory officers, both the Executive Manager – Finance (Chief Financial Officer) and Executive Manager – Governance & Law (Monitoring Officer) are full members of the Council's Corporate Management Team and are in attendance at the Pension Fund Committee and Pension Board meetings to provide advice as required.

The Council's Committee structure supports the organisational and management structure of the Council, incorporating a culture of accountability that has been developed throughout. The Pension Fund Committee oversees the business of the Pension Fund and the Administering Authority is supported by the Pension Board. The Audit Committee remains responsible for ensuring the effectiveness of the internal audit function and considering all reports prepared by the external auditor, which provides further assurance to the Pension Fund.

The Audit Committee's remit ensures that the work of the Council, from both a control and performance perspective, is scrutinised robustly. As well as an annual audit plan, the Committee can request one-off reviews to investigate particular issues if necessary. The role of Chief Internal Auditor is fulfilled by the Head of Audit and Inspection at Glasgow City Council, under an arrangement with Audit Glasgow that provides internal audit services to the Council.

ii) Internal audit reviews

The Council provides internal audit arrangements to the Pension Fund both as a tool of management and with direct reporting to the Council's Audit Committee. The Internal Audit function operates in accordance with the Public Sector Internal Audit Standards (PSIAS) and the CIPFA Statement on the *Role of the Chief Internal Auditor*. Internal audit works to an approved annual internal audit plan, based on an approved audit strategy which takes into account the audit universe and an annual assessment of known and potential risks. During the year, an internal audit review of the

administration of monthly payroll payments to pensioners concluded that reasonable assurance could be placed upon the internal controls in place.

iii) External audit reports

External auditors assess the design and implementation of internal controls in operation within the Council as part of their annual audit work.

The Local Government Pension Scheme (LGPS) regulations require LGPS Administering Authorities to assess their own governance arrangements against the standards set out in the guidance. Where compliance does not meet the published standard, there is a requirement for administering authorities to set out any reasons for non-compliance in their governance compliance statement.

iv) Investment fund managers and the Custodian

The Custodian for the Pension Fund is the Northern Trust Company, who provide a global custody service. The custodian holds for safekeeping the Pension Fund's investment assets such as electronic certificates. The custodian also provides secure settlement of any global transactions that a Fund Manager may undertake, ensuring that all money and legal rights transfer to the appropriate customer as per the transaction in the correct timeframe. The custodian also provides other services such as reclaiming tax, short term cash investment, securities lending, collection of dividends and valuation reports.

All Fund Managers must be registered with, and comply with the Financial Conduct Authority. At the outset of any investment, the mandate details are agreed by the fund management and the Pension Fund, and documented in an Investment Management Agreement or an Application Form depending on the type of investment. These initial documents cover all aspects of the operation of the mandate, such as investment objectives and restrictions, custody and banking, fees and charges, reporting and communication and dealing arrangements. Any changes to the mandate must be agreed by both the fund management company and the Pension Fund.

Significant governance issues

The system of governance aims to provide reasonable, *but not absolute*, assurance that assets are safeguarded, transactions are authorised and properly recorded, material errors or irregularities are either prevented or detected within a timely period and significant risks impacting on the achievement of the

Pension Fund's objectives have been mitigated to an acceptable level. A review of the effectiveness of the governance framework has not identified any significant governance issues or control weaknesses in the Pension Fund's governance arrangements.

Impact of COVID-19

COVID-19 continued to impact many of the Pension Fund's activities during 2022/23. At all times, activity has been managed in accordance with the Scottish Government's *COVID-19: Scotland's Strategic Framework* document, which summarised the restrictions and guidance in place through the period.









Pension Fund Committee and Pension Board meetings continued to take place during the year, with hybrid arrangements being used to facilitate attendance. Committee and Board Members were able to attend meetings in person at the Town Hall or remotely as necessary. These arrangements enabled routine business to be conducted through the year without any significant or adverse impact on the governance of the Council's activities.




Conclusion

Overall, it is our opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the governance arrangements and systems of internal control that operate across the Council and, by extension, the Pension Fund throughout 2022/23. We consider that the governance arrangements and internal control environment allows the us to identify any significant risks which may impact on the achievement of the Pension Fund's principal objectives, and to take action (or actions) to avoid or mitigate the impact of any such risks.

Governance Compliance Statement 2022/23

The Local Government Pension Scheme (Scotland) Regulations 2018 require each Administering Authority to publish a Governance Compliance Statement that sets out how their governance arrangements comply with best practice issued by the Scottish Ministers. The table below contains a self-assessment of the Fund's compliance with these principles and highlights any actions required to implement improvements.

Principle	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.		The Pension Fund Committee has delegated responsibility for overseeing the management and administration of the LGPS and managing the investments of the Pension Fund.
Representatives of participating LGPS employers (scheduled and 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.		The Pension Board, which meets concurrently with the Pension Fund Committee, includes representatives from employers (Councillors), admitted bodies (a Board Member) and scheme members (Trade Unions).
Where a secondary committee or panel has been established, the structure ensures effective communication across both levels.		The Pension Fund Committee and Pension Board meet concurrently to aid easy and open communication.
Where a secondary committee or panel has been established, at least one seat on the main committee is allocated for a member from the secondary committee or panel.		The Pension Board is not a secondary committee, both the Pension Fund Committee and Pension Board meet concurrently and have access to the same agenda papers. There is therefore no need for a Pension Board member to be on the Committee.
Committee Membership and Representation		
<p>All key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include:</p> <p>i) employing authorities (including non-scheme employers, e.g., admitted bodies); and</p> <p>ii) scheme members (including deferred and pensioner scheme members);</p> <p>iii) where appropriate, independent professional observers; and expert advisors (on an ad-hoc basis).</p>	<p>i) </p> <p>ii) </p> <p>iii) </p>	<p>i) Representation on both Pension Fund Committee and Pension Board.</p> <p>ii) Representation on the Pension Board.</p> <p>iii) Professional advisors (investment fund managers, investment advisors, actuary etc.) are regularly invited to attend Pension Committee and Board meetings.</p>
Where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers, meetings and training and are given opportunities to contribute to the decision-making process, with or without voting rights.		Pension Board members have the same access to information, papers and training as Pension Fund Committee members.
Selection and role of lay members		

Committee or board members are made fully aware of the status, role and function they are required to perform on either a main or secondary committee.		Committee and Board members induction training provided following the Scottish Local Government elections. Members of the Pension Fund Committee and Pension Board attended training events during the year relating to Fund administration and investment management.
At the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.		'Declarations of Interest' is a standing item on all agendas.
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.		The Terms of Reference for both Pension Fund Committee and Pension Board sets out this principle.

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Emma Macdonald
Leader of the Council
Chair of the Pension Fund Committee
26 June 2023

.....
Maggie Sandison
Chief Executive
Shetland Islands Council
26 June 2023

Statement of Responsibilities for the
Statement of Accounts

The administering authority’s
responsibilities

The Authority is required to:

- make arrangements for the proper administration of its Pension Fund and to ensure that the proper officer has the responsibility for the administration of those affairs (section 95 of the Local Government (Scotland) Act 1973). In this authority, that officer is the Executive Manager – Finance;
- manage its affairs to secure economic, efficient and effective use of resources and to 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); and
- approve the Annual Accounts for signature.

I certify that the Unaudited Annual Accounts have been approved for signature by the Pension Fund Committee at its meeting on 26 June 2023.

Signed on behalf of Shetland Islands Council.

.....
Emma Macdonald
Leader of the Council
Chair of the Pension Fund Committee
26 June 2023

The Executive Manager – Finance’s
responsibilities

The Executive Manager - Finance is responsible for the preparation of the Pension Fund Statement of Accounts in accordance with proper practices as required by legislation and as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom (the Accounting Code).

In preparing the Annual Accounts, the Executive Manager - Finance has:

- selected suitable accounting policies and then applied them consistently;
- made judgements and estimates that were reasonable and prudent;
- complied with legislation; and
- complied with the local authority Accounting Code (in so far as it is compatible with legislation).

The Executive Manager - Finance has also:

- kept proper accounting records which were up to date; and
- taken reasonable steps for the prevention and detection of fraud and other irregularities.

I certify the Annual Accounts give a true and fair view of the financial position of the Pension Fund at the reporting date and the transactions of the Pension Fund for the year ended 31 March 2023.


.....
Paul Fraser, CPFA
Executive Manager - Finance
Shetland Islands Council
26 June 2023

Pension Fund Account for year ended 31 March 2023

The Pension Fund Account sets out all income and expenditure of the Pension Fund.

2021/22 £000	Notes	2022/23 £000	2022/23 £000
	Dealings with members, employers and others directly involved in the scheme		
(20,662)	Contributions 6	(23,024)	
(1,879)	Transfers in from other pension funds 7	(2,346)	
0	Other income	(4)	
(22,541)	Total Additions		(25,374)
16,544	Benefits payable 8	17,543	
87	Payments to and on account of leavers 9	2,188	
4	Other payments	9	
16,635	Total Withdrawals		19,740
(5,906)	Net (additions)/withdrawals from dealings with members		(5,634)
2,411	Management expenses 10		2,997
(3,495)	Net additions including Fund Management Expenses		(2,637)
	Return on investments		
(3,959)	Investment income 12		(6,336)
(62,543)	(Profits) and losses on disposal of investments and changes in market value of investments 15b		8,454
(66,502)	Net return on investments		2,118
(69,997)	Net (increase)/decrease in the net assets available for benefits during the year		(519)
(589,951)	Opening net assets of the scheme		(659,948)
(659,948)	Closing net assets of the scheme		(660,467)

Net Assets Statement as at 31 March 2023

The Net Assets Statement sets out the value, as at the Statement date, of all assets and current liabilities of the Pension Fund. The net assets of the Pension Fund (assets less current liabilities) represent the funds available to provide for pension benefits at the statement date.

The financial statements summarise the transactions of the Pension Fund during the year and its net assets at the year-end. It should be noted, however, that they do not take account of the obligations to pay pensions and benefits that fall due after the end of the year. The actuarial position of the Pension Fund, which does take account of such obligations, is discussed in the Actuarial Statement. 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.

As at 31 March 2022 £000		Notes	As at 31 March 2023 £000
	Investment Assets		
655,772	Investment Assets	13	652,306
655,772	Total Investment Assets		652,306
	Non current Assets		
123	Long-term debtors	19a	116
123	Total Non Current Assets		116
	Current Assets		
1,755	Debtors	19	1,925
4,232	Bank current accounts	19	8,451
5,987	Total Current Assets		10,376
	Current Liabilities		
(542)	Sundry creditors	21	(697)
(1,392)	Benefits payable	21	(1,634)
(1,934)	Total Current Liabilities		(2,331)
659,948	Net assets of the scheme available to fund benefits at the reporting year end		660,467



Paul Fraser, CPFA
Executive Manager - Finance
Shetland Islands Council
26 June 2023

Notes to the Accounts

Note 1: Description of Pension Fund

The Shetland Islands Council Pension Fund is part of the Local Government Pension Scheme and is administered by Shetland Islands Council. The Council is the reporting entity for this Pension Fund.

General

The Pension Fund is governed by the Superannuation Act 1972 and by the Public Service Pensions Act 2013. The Pension Fund is administered in accordance with the following secondary legislation:

- the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended);
- the Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014 (as amended); and
- the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014.
- The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.

It is a contributory defined benefit pension scheme administered by Shetland Islands Council to provide pensions and other benefits for pensionable employees of scheduled bodies,

Shetland Islands Council, Orkney and Shetland Valuation Joint Board and admitted bodies within Shetland. Teachers are not included as they are members of the Scottish Teachers' Pension Scheme.

The Pension Fund is overseen by the Pension Fund Committee and Pension Board.

Membership

Membership of the LGPS is automatic, but employees are free to choose to opt out of the Scheme and make their own personal pension arrangements outside the Scheme.

Organisations participating in the Shetland Islands Council Pension Fund include:

- Scheduled bodies, which are local authorities and similar statutory bodies whose staff are automatically entitled to be members of the Pension Fund; and
- Admitted bodies, which are other organisations that participate in the Pension Fund under an admission agreement between the Pension Fund and the relevant organisation. Admitted bodies include voluntary, charitable and similar bodies or private contractors undertaking a local authority function following outsourcing to the private sector.

There are 10 employer organisations with active members within Shetland Islands Council Pension Fund including the Council itself; a summary of membership is shown below.

31 March 2022	Shetland Islands Council Pension Fund	31 March 2023
10	Number of employers with active members	10
	Number of employees in scheme:	
3,267	Shetland Islands Council	3,275
367	Other employers	350
3,634	Total	3,625
	Number of pensioners/dependants	
2,128	Shetland Islands Council	2,217
193	Other employers	212
2,321	Total	2,429
	Deferred pensioners	
2,044	Shetland Islands Council	2,146
459	Other employers	462
2,503	Total	2,608
8,458	Scheme Total	8,662

Funding

Benefits are funded by contributions and investment earnings. Contributions are made by active members of the Pension Fund in accordance with the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended) and range from 5.5% to 12% of pensionable pay for the financial year ended 31 March 2023. Employee contributions are topped

up by employers' contributions, which are set, based on triennial actuarial funding valuations. The actuarial valuation as at 31 March 2020 set these employers' contribution rates, which range from 17.2% to 36.0% of pensionable pay.

Benefits

Pension benefits under the LGPS are calculated as per the table below:

Service pre 1 April 2009	Service post 31 March 2009	Service Post 31 March 2015
Each year worked is worth 1/80 x final FTE pensionable salary	Each year worked is worth 1/60 x final FTE pensionable salary	Each year worked is worth 1/49 x actual pensionable salary
Automatic lump sum of 3 x salary	No automatic lump sum	No automatic lump sum
In addition, part of annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up	Part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up	Part of the annual pension can be exchanged for a one-off tax-free cash payment. A lump sum of £12 is paid for each £1 of pension given up

There are a range of other benefits provided under the scheme including early retirement, ill health retirement and death benefits. For more details, please refer to <https://pensions.gov.scot/local-government> or

contact Shetland Islands Council Pension Section on 01595 744644. Benefits are index-linked in line with the consumer price index.

Note 2: Basis of Preparation

The Statement of Accounts summarises the Pension Fund's transactions for the 2022/23 financial year and its position at year-end as at 31 March 2023. The accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2022/23, which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

The accounts summarise the transactions of the Pension Fund and report on the net assets available to pay pension benefits. The accounts do not take account of obligations to pay pensions and benefits that fall due after the end of the financial year. The actuarial present value of promised retirement benefits, valued on an International Accounting Standard IAS 26 basis, is disclosed at Note 18.

The accounts have been prepared on a going concern basis.

Note 3: Accounting Standards Issued and Adopted in year

a) Standards, amendments and interpretations effective in the current year.

In the current year, the Pension Fund has applied a number of amendments to IFRS Standards and Interpretations that are effective for an annual reporting period that begins on 1 January 2022. Their adoption has not had any material impact on the disclosures or on the amounts reported in these financial statements:

- Annual Improvements to IFRS Standards 2018 – 2020;
- Amendments to IAS 16 (Property Plant and Equipment) – amendments to Proceeds before Intended Use.

b) Standards, amendments and interpretations early adopted this year

There are no new standards, amendments or interpretations early adopted this year.

Note 4: Accounting Standards Issued not Adopted

At the date of authorisation of these financial statements, the Pension Fund has not applied the following new and revised IFRS Standards that have been issued but are not yet effective:

- Amendments to IAS 8 (Accounting Policies, Changes in Accounting Estimates and Errors) – definition of Accounting Estimates – applicable for periods beginning on or after 1 April 2023;
- Amendments to IAS 1 (Presentation of Financial Statements) and IFRS Practice Statement 2 – disclosure of Accounting Policies – applicable for periods beginning on or after 1 April 2023.

The Pension Fund does not expect that the adoption of the Standards listed above will have a material impact on the financial statements in future periods.

Note 5: Assumptions Made about the Future and Other Major Sources of Estimation Uncertainty

The Statement of Accounts contains estimated figures that are based on assumptions made by the Council about the future, or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because balances cannot be determined with certainty, actual results could be materially different from assumptions and estimates.

The table below highlights the approximate impact that a small change in the assumptions used would have on the liabilities of the fund:

Item	Uncertainties - Estimate	Effect if actual results differ from assumptions
Actuarial present value of promised retirement benefits	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 pension fund assets. An actuary to the Fund is appointed to provide the fund with expert advice about the assumptions to be applied.	The effects on the net pension liability of changes in individual assumptions can be measured. For instance, 0.1% decrease in the real discount rate assumption would result in a decrease in the pension liability of £11m. A 0.1% increase in salary increase rate would increase the value of liabilities by approximately £1m, and a 0.1% increase in pension increase rate would increase the liability by approximately £10m.

Note 6: Contributions Receivable

By category:

31 March 2022 £000		31 March 2023 £000
(15,821)	Employers - normal	(18,001)
(138)	Employers - augmentation	0
(4,703)	Members - normal	(5,023)
(20,662)	Total	(23,024)

By authority:

31 March 2022 £000		31 March 2023 £000
(18,047)	Administering authority	(19,828)
(174)	Scheduled bodies	(213)
(2,441)	Admitted bodies	(2,983)
(20,662)	Total	(23,024)

Note 7: Transfers in from Other Pension Funds

The total transfers received during the year are as follows:

31 March 2022 £000		31 March 2023 £000
(1,879)	Individual transfers in	(2,346)
(1,879)	Total	(2,346)

The Pension Fund received 75 transfers in during 2022/23 with an average value of £31,285, compared to 72 transfers in during 2021/22 with an average value of £26,102.

Note 8: Benefits Payable

By category:

31 March 2022 £000		31 March 2023 £000
12,898	Pensions	13,655
3,253	Commutation and lump sum retirement benefits	3,337
393	Lump sum death benefits	551
16,544	Total	17,543

By authority:

31 March 2022 £000		31 March 2023 £000
14,675	Administering authority	15,766
121	Scheduled bodies	124
1,748	Admitted bodies	1,653
16,544	Total	17,543

Note 9: Payments to and on Account of Leavers

31 March 2022 £000		31 March 2023 £000
18	Refunds to members leaving service	35
26	Individual transfers	1,039
43	Group transfers	1,114
87	Total	2,188

Note 10: Management Expenses

31 March 2022 £000		31 March 2023 £000
510	Administration Expenses	434
45	Oversight and Governance Expenses	43
	Investment Management expenses	
1,784	Management Fees	2,443
40	Performance Fees	42
32	Custody Fees	35
2,411	Total	2,997

Note 10a – Investment Management Expenses

2022/23	Total £000	Management fees £000	Performance related fees £000
Managed Funds	713	699	14
Diversified growth funds	531	527	4
Fixed income unit trusts	137	137	0
Private Credit	188	187	1
Unit linked insurance policies	33	15	18
Pooled Property Unit Trusts	745	741	4
Property Debt	73	72	1
Unitised Liquidity Fund	57	57	0
Cash Deposits	8	8	0
	2,485	2,443	42
Custody fees	35		
Total	2,520		

2021/22	Total £000	Management fees £000	Performance related fees £000
Managed Funds	684	675	9
Diversified growth funds	635	629	6
Fixed income unit trusts	162	159	3
Unit linked insurance policies	34	15	19
Pooled Property Unit Trusts	270	266	4
Property Debt	24	24	0
Unitised Liquidity Fund	15	15	0
Cash Deposits	1	1	0
	1,825	1,784	41
Custody fees	32		
Total	1,857		

Note 11: External Audit Costs

31 March 2022 £000		31 March 2023 £000
29	Payable in respect of external audit	35
29	Total	35

Note 12: Investment Income

31 March 2022 £000		31 March 2023 £000
0	Private equity income	(1,982)
(3,167)	Pooled investment vehicles	(3,489)
(4)	Interest on cash deposits	(201)
(788)	Other	(664)
(3,959)	Total	(6,336)

Note 13: Investments

Fair Value As at 31 March 2022 £000		Fair Value As at 31 March 2023 £000
233,198	Managed Funds	280,410
301,945	Unit Linked Insurance Policies	283,434
45,070	Fixed income unit trusts	0
0	Private Credit	19,907
65,403	Pooled property unit trusts	57,726
3,690	Unitised Liquidity Fund	4,472
5,933	Property Debt	5,602
130	Cash deposits	634
10	Property income due	11
153	Diversified growth income due	99
240	Fixed income due	0
0	Cash income due	11
655,772	Total investment assets	652,306

Note 13a - Reconciliation of movements in investments

	Market Value at 1 April 2022 £000	Purchases during the year £000	Sales during the year £000	Change in market value during the year £000	Market Value at 31 March 2023 £000
Investment Assets:					
Pooled funds - managed funds	233,198	117,000	(70,000)	212	280,410
- unit linked insurance policies	301,945	0	(19,220)	709	283,434
Fixed income unit trusts	45,070	1,278	(46,682)	334	0
Private Credit	0	20,065	16	(174)	19,907
Pooled property unit trusts	65,403	4,970	(3,425)	(9,222)	57,726
Unitised Liquidity Fund	3,690	2,938	(2,191)	35	4,472
Property Debt	5,933	538	(522)	(347)	5,602
Total Pooled Investment Vehicles	655,239	146,789	(142,024)	(8,453)	651,551
Other investment balances:					
Diversified Growth income due	153				99
Fixed income due	240				0
Property income due	10				11
Cash income due	130				645
Net investment assets	655,772				652,306

	Market Value at 1 April 2021 £000	Purchases during the year £000	Sales during the year £000	Change in market value during the year £000	Market Value at 31 March 2022 £000
Investment Assets:					
Pooled funds - managed funds	216,957	0	0	16,241	233,198
- unit linked insurance policies	267,242	0	(2,850)	37,553	301,945
Fixed income unit trusts	44,701	1,001	0	(632)	45,070
Pooled property unit trusts	53,871	5,369	(3,215)	9,378	65,403
Unitised Liquidity Fund	4,238	0	(549)	1	3,690
Property Debt	2,719	3,233	(21)	2	5,933
Total Pooled Investment	589,728	9,603	(6,635)	62,543	655,239
Other investment balances:					
Diversified Growth income due	150				153
Fixed income due	268				240
Property income due	12				10
Cash income due	60				130
Net investment assets	590,218				655,772

Indirect costs are incurred through the bid-offer spread on investments within pooled investment vehicles. The amount of indirect costs is not separately provided to the Scheme. There are no direct transaction costs.

Note 13b - Analysis by Fund Manager

Market Value 31 March 2022			Market Value 31 March 2023	
£000	%		£000	%
301,958	46	BlackRock	283,447	44
75,154	11	Schroders	67,928	10
95,351	15	Newton Asset Management	61,064	9
137,999	21	KBI	102,774	16
45,310	7	M & G Investments	4	0
0	0	Baillie Gifford	116,678	18
0	0	Permira	20,411	3
655,772	100	Total investment assets	652,306	100

The following investments represent more than 5% of the net assets of the scheme:

Market Value 31 March 2022			Market Value 31 March 2023	
£000	%		£000	%
112,905	17	Aquila Life UK equity index	104,546	16
45,070	7	M & G Alpha Opp Fd AGBP	0	0
137,999	21	KBI 1 Dividend Plus	102,770	18
95,198	15	Newton Real Rtrn X ACC NAV	60,963	16
189,041	29	Aquila Life World EX UK Fund Series 1	178,887	9
0	0	Baillie Gifford Global Alpha Fund	116,676	27

Note 14: Fair Value Hierarchy

Asset and liability valuations have been classified into three levels according to the quality and reliability of information used to determine their fair values. Transfers between levels are recognised in the accounts in the year in which they occur.

Level 1

Assets and liabilities 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, quoted fixed securities, quoted index linked securities and unit trusts.

Level 2

Assets and liabilities 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.

Level 3

Assets and liabilities 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.

The following table provides an analysis of the financial assets of the pension fund, grouped into Levels 1 and 2 and 3, based on the level at which the fair value is observable.

As at 31 March 2022 £000	Fair value through profit and loss	As at 31 March 2023 £000
4,223	Level 1	5,117
580,213	Level 2	571,874
71,336	Level 3	75,315
655,772	Net Investment assets	652,306

Basis of Valuation

The basis of valuation for each class of investment asset 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 that represent the highest and best price available at the reporting date.

Description of Asset	Valuation hierarchy	Basis of valuation	Observable / unobservable inputs	Key sensitivities affecting valuations
Cash and cash equivalents	Level 1	Carrying value is deemed to be fair value because of the short term nature of these financial instruments	Not required	Not required
Unquoted pooled fund investments	Level 2	Average of brokers prices	Evaluated price feeds	Not required
Pooled property funds where regular trading takes place	Level 2	Closing bid price where bid and offer prices are published Closing single price where single price published	NAV-based pricing set on a forward pricing basis	Not required
Pooled property funds where regular trading does not take place	Level 3	Valued by investment managers on a fair value basis each year using PRAG guidance	NAV-based pricing set on a forward pricing basis	Valuations are affected by any changes to the value of the financial instrument being hedged against
Other unquoted and private equities	Level 3	Comparable valuation of similar companies in accordance with international Private Equity and Venture Capital Valuation Guidelines 2018 and the IPEV Board's Special valuation guidance (March 2020)	-EBITDA multiple - Revenue multiple -Discount for lack of marketability - Control premium	Valuations are affected by any changes to the value of the financial instrument being hedged against

Sensitivity of assets valued at level 3

In order to give a clearer picture of the impact on the Fund's results or financial position of potential changes and assumptions, a sensitivity analysis is shown below. This sensitivity is based on assumptions and conditions prevailing at the year-end and should be used with caution. The effects provided are not necessarily indicative of the actual effects that would be experienced because the Fund's actual exposure are constantly changing.

	Assessed valuation range (+/-)	Value at 31 March 2023 £000	Value on increase £000	Value on decrease £000
Property	15.5%	55,408	63,996	46,820
Private Credit	9.6%	19,907	21,818	17,996
		75,315	85,814	64,816

For there year ending 31 March 2023 the value of level 3 assets was £75m (2021/22: £71m)

Note 14a – Reconciliation of fair value measurements within Level 3

	Market value at 1 April 2022 £000	Transfers into Level 3 £000	Transfers out of Level 3 £000	Purchases during the year £000	Sales during the year £000	Unrealised gains/ (losses) £000	Realised gain £000	Market value at 31 March 2023 £000
Pooled Property	71,336	-	(7,581)	5,508	(3,989)	(9,909)	43	55,408
Private Credit	-	-	-	20,065	16	(174)		19,907
	71,336	-	(7,581)	25,573	(3,973)	(10,083)	43	75,315

The transfer from level 3 to level 2 at March 2023 is due to confirmation from the fund manager they had incorrectly classified this item last year.

Note 15: Financial Instruments

Note 15a - Classification of financial instruments

Accounting policies describe how different asset classes of financial instruments are measured, and how income and expenses, including gains and losses, are recognised.

The following table analyses the carrying amounts of financial assets and liabilities (excluding cash) by category and net assets statement heading. No financial assets were reclassified during the accounting period.

As at 31 March 2022				As at 31 March 2023		
Fair value through profit and loss £000	Receivables £000	Financial liabilities £000		Fair value through profit and loss £000	Receivables £000	Financial liabilities £000
			Financial assets			
			Pooled funds			
233,438			- managed funds	280,410		
301,945			- unit linked insurance policies	283,434		
45,070			Fixed income unit trusts	0		
0			Private Credit	19,907		
65,403			Pooled property unit trusts	57,726		
3,690			Unitised liquidity funds	4,472		
5,933			Property debt	5,602		
153			Diversified growth	99		
130	4,232		Cash	634	8,451	
10			Property income due	11		
0			Cash income due	11		
	1,755		Debtors		1,925	
655,772	5,987	0	Total Financial assets	652,306	10,376	0
			Financial liabilities			
0	0	(1,934)	Creditors	0	0	(2,331)
0	0	(1,934)	Total Financial liabilities	0	0	(2,331)
655,772	5,987	(1,934)	Total	652,306	10,376	(2,331)

Note 15b - Net gains and losses on financial instruments

As at 31 March 2022 £000	Financial assets	As at 31 March 2023 £000
(62,543)	Fair value through profit and loss	8,454
(62,543)	Total	8,454

Note 15c - Value of financial instruments

As at 31 March 2022		Financial assets	As at 31 March 2023	
Book value £000	Market value £000		Book value £000	Market value £000
367,475	655,772	Fair value through profit and loss	411,437	652,306
367,475	655,772	Total	411,437	652,306

Note 16: Nature and Extent of Risks Arising from Financial Instruments

Risk and risk management

The Pension Fund's primary long-term risk is that its assets will fall short of its liabilities (i.e. promised benefits payable to members). Therefore, the aim of investment risk management is to minimise the risk of an overall reduction in the value of the Pension Fund and to maximise the opportunity for gains across the whole Pension Fund portfolio. The Pension Fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) and credit risk to an acceptable level. In addition, the Pension Fund manages its liquidity risk to ensure there is sufficient liquidity to meet the Pension Fund's forecast cash flows. The Pension Fund manages these investment risks as part of its overall Pension Fund risk management programme.

Responsibility for the Pension Fund's risk management strategy rests with the Council. Risk management policies are established to identify and analyse the risks faced by the Council's pension operations. Policies are reviewed regularly to reflect changes in activity and market conditions.

Market risk

Market risk is the risk of loss from fluctuations in equity, bond and property prices, interest and foreign exchange rates and credit spreads. The Pension Fund is exposed to market risk from its investment activities, particularly through its equity holdings. The level of risk exposure depends on market condition, expectations of future price and yield movements and the asset mix.

The objective of the Pension Fund's risk management strategy is to identify, manage and control market risk exposure within acceptable parameters, whilst optimising the return on risk.

In general, excessive volatility in market risk is managed through the diversification of the portfolio in terms of geographical and industrial sectors and individual securities. To mitigate market risk, the Pension Fund and its investment advisors undertake appropriate monitoring of market conditions and benchmark analysis.

Other price risk

Other price risk represents the risk that the value of a financial instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate risk or foreign exchange risk), whether those changes are caused by factors specific to the individual instrument, or its issuer,

or factors affecting all such instruments in the market.

The Pension Fund's investment managers mitigate this price risk through diversification and the selection of investments, which is monitored by the Council, as the administering authority, and the Fund Managers to ensure it is within limits specified in the Pension Fund investment strategy.

Other Pension Fund price risk - sensitivity analysis

In agreement with the Pension Fund's performance analyst and following analysis of historical data and expected investment return during the financial year, the Pension Fund has determined that the following movements in market price risk are deemed reasonably possible for the financial year 2022/23 reporting period:

Asset Type	Potential market movements (+/-)
UK Equities	18.2%
Global Equities	19.0%
Property	15.5%
Cash	0.3%
Diversified Growth	8.9%
Alternative Credit	9.4%
Private Credit	9.6%

The potential price changes disclosed above are determined based on the observed historical volatility of asset class returns. 'Riskier' assets such as equities will display greater potential volatility than bonds as an example, so the overall outcome will depend largely on Pension Funds' asset allocations. The potential volatilities are consistent with a one standard deviation movement in the change in value of the assets over the latest three years. This can then be applied to the period end asset mix.

Had the market price of the Pension Fund investments increased/decreased in line with the above, the change in the net assets available to pay benefits in the market price would have been as shown in the following table (the prior year comparator is shown below).

Asset Type	Value as at 31 March 2023 £000	Percentage Change %	Value on Increase £000	Value on Decrease £000
Cash and cash equivalents	5,117	0.30%	5,132	5,102
Investment portfolio assets:			0	0
UK Equities	104,546	18.2%	123,573	85,519
Global Equities (ex UK)	398,334	19.0%	474,017	322,651
Property	63,339	15.5%	73,157	53,521
Diversified Growth	61,063	8.9%	66,498	55,628
Alternative Credit	0	9.0%	0	0
Private Credit	19,907	9.6%	21,818	17,996
Total assets	652,306		764,195	540,417

Asset Type (Restated)	Value as at 31 March 2022 £000	Percentage Change %	Value on Increase £000	Value on Decrease £000
Cash and cash equivalents	130	0.30%	130	130
Investment portfolio assets:				
UK Equities	112,905	19.9%	135,373	90,437
Global Equities (ex UK)	327,040	20.1%	392,775	261,305
Property	75,036	15.0%	86,291	63,781
Diversified Growth	95,351	9.1%	104,028	86,674
Alternative Credit	45,310	9.0%	49,388	41,232
Total assets	655,772		767,985	543,559

Interest rate risk

The Pension Fund invests in financial assets for the primary purpose of obtaining a return on investments.

These investments are subject to interest rate risks, which represent the risk that the value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Pension Fund has a diversified portfolio, managed by different Fund Managers who have the flexibility to hold cash and cash-equivalent balances in order to make investments at short notice. These balances are exposed to interest rate risk, however Fund Managers are expected to maintain such balances at a minimal level, whilst retaining the agility to invest in line with their respective investment mandates.

The Pension Fund's direct exposure to interest rate movements are set out below:

As at 31 March 2022 £000		As at 31 March 2023 £000
	Asset type	
130	Cash and cash equivalents	5,117
4,232	Cash balances	8,451
45,070	Fixed income unit trusts	0
49,432	Total	13,568

Interest rate risk sensitivity analysis

The Pension Fund recognises that interest rates can vary and can affect both income to the Pension Fund and the value of the net assets available to pay benefits. A 110 basis point (BPS) movement in interest rates is viewed as a reasonable level of risk sensitivity for the Pension Fund under current interest rate circumstances. The Pension Fund's performance analyst has also agreed that the long-term average rates are expected to move less than 110 basis points (hence 100 basis points used in the examples below) from one year to the next and experience suggests that such movements are possible.

The analysis that follows assumes the total Fund volatility takes into account the expected interactions between the different asset classes shown, based on the underlying volatilities and correlations of the assets, in line with mean variance portfolio theory.

Asset Type	Carrying amount as at 31 March 2023 £000	Change in year in the net assets available to pay benefits	
		+100 BPS £000	-100 BPS £000
Cash and cash equivalents	5,117	51	(51)
Cash balances	8,451	85	(85)
Fixed income unit trusts	0	0	0
Total change in assets available	13,568	136	(136)

Asset Type	Carrying amount as at 31 March 2022 £000	Change in year in the net assets available to pay benefits	
		+100 BPS £000	-100 BPS £000
Cash and cash equivalents	130	1	(1)
Cash balances	4,232	42	(42)
Fixed income unit trusts	45,070	451	(451)
Total change in assets available	49,432	494	(494)

Currency risk

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Pension Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Pension Fund (£ sterling).

The Pension Fund holds both monetary and non-monetary assets denominated in currencies other

than £ sterling. Fund Managers are expected to manage currency risk. Fund Managers also routinely report the performance of their respective portfolios to the Pension Fund, including the level of exposure to currency risk.

The following table summarises the Pension Fund's currency exposure as at 31 March 2023 and as at the previous period end.

As at 31 March 2022 £000		As at 31 March 2023 £000
327,040	Asset type Pooled Funds - overseas equities	398,334
45,310	Alternative credit - overseas	0
153	Diversified Growth Fund	153
372,503	Total	398,487

Currency risk - sensitivity analysis

Following analysis of data provided by the Pension Fund's performance analysts, the Pension Fund considers the likely volatility associated with foreign exchange rate movements to be 10%.

This analysis assumes that all other variables, in particular interest rates, remain constant. A 9.9% strengthening/weakening of the pound against the various currencies in which the Pension Fund holds investments would increase/decrease the net assets available to pay benefits as follows:

Asset Type	Carrying amount as at 31 March 2023 £000	Change to net assets available to pay benefits	
		+9.9% £000	-9.9% £000
Pooled Funds - overseas equities	398,334	437,769	358,899
Alternative credit - overseas	0	0	0
Diversified Growth Fund	153	168	138
Total change in assets available	398,487	437,937	359,037

Asset Type	Carrying amount as at 31 March 2022 £000	Change to net assets available to pay benefits	
		+10.0% £000	-10.0% £000
Pooled Funds - overseas equities	327,040	359,744	294,336
Alternative credit - overseas	45,310	49,841	40,779
Diversified Growth Fund	153	168	138
Total change in assets available	372,503	409,753	335,253

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 Pension Fund to incur a financial loss. The market values of investments generally reflect an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the Pension Fund's financial assets and liabilities.

In essence, the Pension Fund's entire investment portfolio is exposed to some form of credit risk. However, the selection of high quality counterparties, brokers and financial institutions

minimises credit risk that may occur through the failure to settle a transaction in a timely manner.

Deposits are not made with banks and financial institutions unless they meet the Council's credit criteria. The Council has also set limits on the value of these deposits, which can be placed with any bank or financial institution, apart from the bank the Council uses for its daily operations.

The Council believes it has managed its exposure to credit risk, and has had no experience of default or uncollectible deposits over the past five financial years.

The Pension Fund's cash holding under its treasury management arrangements at 31 March 2023 was £9.096m (31 March 2022: £4.362m). This was held with the following institutions:

As at 31 March 2022 £000		As at 31 March 2023 £000
	Fund manager deposits	
118	Schroders cash	117
12	BlackRock cash	13
0	Newton cash	2
0	Permira cash	504
0	Baillie Gifford cash	2
0	M&G cash	3
0	KBI cash	4
	Bank current accounts	
4,232	Bank of Scotland Plc	8,451
4,362	Total	9,096

Liquidity risk

Liquidity risk represents the risk that the Pension Fund will not be able to meet its financial obligations as they fall due. The Pension Fund takes steps to ensure that it has adequate cash resources to meet its commitments.

The Pension Fund has immediate access to all its cash holdings. The Pension Fund also has an overdraft facility to cover any unexpected short-term cash needs. The overdraft facility has not been used over the past five years and therefore the Pension Fund's exposure to liquidity risk is considered negligible.

The Pension Fund defines liquid assets as assets that can be converted to cash within three months. Illiquid assets are those assets that will take longer than three months to convert into cash. As at 31 March 2023, the value of illiquid assets was £63m, which represented 9.7% of the Pension Fund Investment assets (31 March 2022: £75m, which represented 11.4% of the Pension Fund assets).

Refinancing risk

The key risk is that the Pension Fund will be bound to replenish a significant proportion of its financial instruments at a time of unfavourable interest rates. The Pension Fund does not have any financial instruments that have a refinancing risk as part of its treasury management and investment strategies

Note 17: Funding Arrangements

In line with the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended), the Pension Fund's actuary undertakes a funding valuation every three years for the purpose of setting employer contribution rates for the forthcoming triennial period. The valuation for the current accounting period took place as at 31 March 2020.

The funding policy is set out in the Pension Fund's Funding Strategy Statement (FSS), dated March 2021.

The key elements of the funding policy are:

- to ensure the long-term solvency of the Pension Fund using a prudent long-term view. This will ensure that sufficient funds are available to meet all members'/ dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable where appropriate;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return. This will also minimise the costs to be borne by Council Tax payers;
- to reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and
- to use reasonable measures to reduce the risk to other employers and ultimately to the

Council Tax payer from an employer defaulting on its pension obligations.

Employee benefits are guaranteed and employee contributions are fixed, so employers need to pay the balance of the cost of delivering the benefits to members and dependants. The Funding Strategy Statement sets out how the Administering Authority has balanced the conflicting aims of affordability and stability of employer contributions and prudence in the funding basis with regard to employer liabilities.

Funding position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 32 of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2014 was at 31 March 2020. This valuation revealed that the Pension Fund's assets, which at 31 March 2020 were valued at £461m, were sufficient to meet 92% (£450m and 90% at 31 March 2017 valuation) of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2020 valuation was £38m (2017 valuation: £51m).

Copies of the 2020 Valuation Report and Funding Strategy Statement are available on request from Shetland Islands Council, the Administering Authority to the Pension Fund.

Principal actuarial assumptions and method used in the valuation

Full details of the method used are described in a valuation report from the actuaries, Hymans Robertson LLP, available on request from Shetland Islands Council, the Administering Authority to the Pension Fund, at 8 North Ness Business Park, Lerwick.

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

The assumptions are required to place value on the benefits earned to date and the benefits that will be earned in the future. To this end, the assumptions fall broadly into two categories; financial assumptions and demographic assumptions. Financial assumptions relate to the size of members' benefits, and information affecting these assumptions are discount rate, price inflation, which affects benefit increases, and salary increases. Demographic assumptions relate to longevity of current pensioners and future pensioners.

The common rate of contribution payable by each employing authority under regulation 32(4)(a) of the 2014 Regulations for the period 1 April 2021 to 31 March 2024 is 22.3% of pensionable pay, (i.e. the rate which all employers in the Pension Fund pay).

Individual employers' rates are adjusted under regulation 32(4) (b) from the common contribution rate. The contribution rates payable for the period 1 April 2021 to 31 March 2024 were set in accordance with the Pension Fund's funding policy as set out in its Funding Strategy Statement.

During this period, the employers' rate due by Shetland Islands Council is 20.8% per annum for 2021/22 then 22.0% for 2022/23 and 2023/24.

A market-related approach was taken when valuing the liabilities, for consistency with the valuation of the Fund assets at their 31 March 2020 market value.

The key financial assumptions adopted for the 2020 valuation were as follows:

Financial assumptions	% per annum
Discount rate	3.4%
Salary increase assumption	1.7%
Benefit increase assumption (CPI)	1.7%

Mortality assumptions

The key demographic assumption was the allowance made for longevity. The expectancy assumption was based on the Fund's Vita Curves alongside future improvements based on the CMI 2019 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.5% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

Mortality assumption at age 65	Males	Females
Current Pensioners	20.9 yrs	23.1 yrs
Future Pensioners	22.4 yrs	25.3 yrs

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 post-April 2009 service.

50:50 Option assumption

It is assumed that 1.0% of members (uniformly distributed across the age, service and salary range) will choose the 50:50 option. This is where members pay 50% of contributions in return for 50% of benefits. Employers still pay the full contribution.

Note 18: Actuarial Present Value of Promised Retirement Benefits

In addition to the Triennial Funding Valuation, the Actuary also undertakes a valuation of pension fund liabilities on an IAS19 basis every year using the same base data as the Valuation, rolled forward to the current financial year, taking account of changes in membership numbers and using updated assumptions. A statement prepared by the Actuary is attached as an **Appendix**.

Note 19: Current Assets

As at 31 March 2022 £000		As at 31 March 2023 £000
	Debtors:	
403	Contributions due - employees	414
1,346	Contributions due - employers	1,471
6	Sundry debtors	40
0	Prepayments	0
4,232	Bank current accounts	8,451
5,987	Total	10,376

Note 19a: Long Term Debtor

As at 31 March 2022 £000		As at 31 March 2023 £000
	Long Term Debtors	
123	Reimbursement of lifetime tax allowance	116
123	Total	116

Note 20: Unfunded Pension

As at 31 March 2022 £000		As at 31 March 2023 £000
728	Added years pension	714

Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998 [Section 31] allows local authorities and admitted bodies to pay additional pension on a voluntary basis. Additional pension in respect of added years' enhancement is awarded from the body or service where the employee retired and costs are paid directly by the employer and not the Pension Fund.

Note 21: Current Liabilities

As at 31 March 2022 £000		As at 31 March 2023 £000
(542)	Sundry creditors	(697)
(1,392)	Benefits payable	(1,634)
(1,934)	Total	(2,331)

Note 22: Contingent Liabilities

McCloud Judgement

The LGPS benefit structure has been reviewed following the Government's loss of the right to appeal two Court of Appeal judgements in December 2018, collectively referred to as the 'McCloud' judgement. The courts have ruled that the 'transitional protections' awarded to members who were within 10 years of normal retirement age in 2012 when the scheme was reformed on 1 April 2015 were unlawful on the grounds of age discrimination. On 1 October 2023, it is expected that the retrospective remedy to address these age inequalities will come into force.

In May 2020, the SPPA set out their expectations for how funds should allow for this uncertainty in the benefit structure as part of their 2020 valuations. The Fund Actuary included an allowance in the Fund's liabilities in line with SPPA's instructions.

GMP Indexation

On 23 March 2021 HMT responded to its consultation on the indexation of Guaranteed Minimum Pensions (GMPs) in Public Service Pension Schemes. In summary, HMT has discounted conversion (of GMP into main scheme benefits) as their long-term policy solution and instead will make full GMP indexation the permanent solution for public service pension schemes.

Initially members whose State Pension Age was between 5 April 2016 and 6 April 2021 had their GMP pensions fully uprated by their scheme in

line with CPI. The new policy has extended this to be the permanent solution for all members whose State Pension Age (SPA) is on or after 6 April 2021.

GMP Equalisation

Following a High Court ruling from 26 October 2016, all defined benefit pension schemes must equalise guaranteed minimum pension (GMP) for men and women. Further guidance is still awaited on how to deal with the sex inequalities which will persist for a minority of scheme members.

Survivors Benefits

Regulations have now been made which change the rules for calculating pre-April 15 survivor pensions in response to two court cases: namely Walker v Innospec and Goodwin v Department for Education. Principally, for deaths on or after 5 December 2005, the amendments place surviving same-sex civil partners, survivors of married same-sex couples and male survivors of female married members in a similar position to female survivors of male married members.

The Regulations were made on 29 April 2022 and came into force on 1 June 2022. As calculations still require to be performed, there is insufficient data available to estimate reliably the impact this will have on scheme liabilities however the impact is thought to be minimal.

Cost Cap Valuation

When the Local Government Pension Scheme was reformed in 2015, a mechanism, called the Cost Cap, was put in place to protect employers from significant increases in future pension costs. The mechanism is symmetrical in its design – following a Cost Cap valuation carried out by the Government Actuary's Department (GAD). If the cost changes and falls outside a two percent corridor above/below the rate, action must be taken to bring the cost back to the rate. This means if the scheme is calculated to have a lower/(higher) than intended cost to employers, then action will be taken: improvements/(reductions) in future benefit accrual and/or increases/(reductions) in employee contribution rates.

The employer cost cap rate for LGPS (Scotland) is 15.2 percent. The results of the first valuation as at 2017 showed that the cost was 0.2 per cent above the cost cap rate. This shows the cost has remained within the two per cent corridor which means no changes to benefits or member contributions are needed.

Note 23: Additional Voluntary Contributions

As at 31 March 2022 £000		As at 31 March 2023 £000
7,271	Prudential	5,640
55	Equitable Life	52
7,326	Total	5,692

AVC contributions of £0.620m were paid directly to Prudential during the year (2021/22: £0.603m).

Prudential were unable to provide a year-end valuation, however they have provided an estimated statement which provides a reasonable indication of the transactions and funds under management.

The estimated balance provided at 31 March 2023 does not include the estimated terminal bonus which is not guaranteed.

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

Note 24: Related Party Transactions

Shetland Islands Council

The Shetland Islands Council Pension Fund is administered by Shetland Islands Council. Consequently, there is a strong relationship between the Council and the Pension Fund. The Council incurred costs of £0.442m (2021/22 £0.583m) in relation to the administration of the Fund and was subsequently reimbursed by the Fund for these expenses.

The investments of the Fund are overseen by the Council's Treasury Section: their costs are levied by staff time allocations. Costs incurred were £0.042m (2021/22 £0.041m) in relation to investment of the Fund and was subsequently reimbursed by the Fund for these expenses.

The Council incurred costs of £13.663m (2021/22 £12.892m) in relation to pensioner payments. Such payments are reimbursed by the Fund.

In addition the Council is the single largest employer of Pension Fund members, and contributed £15.459m to the Fund (2021/22 £13.922m).

Governance

Four members of the Pension Fund Committee receive pension benefits from the Shetland Islands Council Pension Fund.

Each member of the Pension Fund Committee and Pension Board is required to declare their interests at each meeting.

Key management personnel

Key management personnel for the Pension Fund include the Shetland Islands Council Councillors, who sit on the Pension Fund Committee and Pension Board. The membership is as follows:

Pension Fund Committee Membership
Emma Macdonald (Chair)
Davie Sandison
Moraig Lyall
John Fraser
Duncan Anderson
Gary Robinson
Dennis Leask
Catherine Hughson
Robbie McGregor
Liz Peterson
Robert Thomson
Pension Board Membership
Bryan Peterson
Tom Morton
Mark Robinson

Note 25: Changes in Actuarial Present Value of Promised Retirement Benefits

Actuarial Present Value of Promised Retirement Benefits	Vested Benefits £000	Total £000
Balance at 31 March 2023	549	549
Increase/Decrease in value during 2022/23	(280)	(280)
Balance at 31 March 2022	829	829
Decrease in value during 2021/22	(23)	(23)
Balance at 31 March 2021	852	852

Note 26: Critical Judgements in Applying Accounting Policies

Pension Fund liability

The Pension Fund liability is calculated every three years by the appointed actuary, with annual updates in the intervening years, if required. The methodology used is in line with accepted guidelines and in accordance with IAS 19. Assumptions underpinning the valuations are agreed with the actuary and are summarised in Note 17. This estimate is subject to significant variances based on changes to the underlying assumptions.

Note 27: Events after the Balance Sheet Date

The unaudited annual accounts were authorised for issue on 26 June 2023. Events taking place after this date are not reflected in the financial statements or notes. Where events taking place before this date provided information about conditions existing at 31 March 2023, the figures in the financial statements and notes have been adjusted in all material respects to reflect the impact of this information.

Note 28: Accounting Policies

The Pension Fund accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2022/23 which is based upon International

Reporting Standards (IFRS) as amended for the UK public sector.

The accounts summarise the transactions of the Fund and report on the net assets available to pay pension benefits. The accounts do not take account of any obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present value of the promised retirement benefits, valued on an International Accounting Standard (IAS) 19 basis is disclosed at Note 18 of these accounts.

Management has considered a range of factors that may influence the ability of the Pension Fund to continue as a going concern, including:

- the regulatory and legislative framework governing Pension Funds;
- the Council's governance arrangements;
- the Council's current and medium-term financial position, and
- the impact of COVID-19.

Management's assessment of the above factors has determined that it is still appropriate to prepare the Pension Fund's accounts on a going concern basis, as required by the Code of Practice on Local Authority Accounting 2022/23.

Pension Fund account - revenue recognition

A Contribution income

Normal contributions are accounted for on an accruals basis as follows:

- Employee contribution rates are set in accordance with LGPS regulations, using common percentage rates for all schemes that rise according to pensionable pay.
- Employer contributions are set at the percentage rate recommended by the fund actuary for the period to which they relate.

Employer deficit funding contributions are accounted for on the basis advised by the Fund actuary in the rates and adjustment certificate issued to the relevant employing body. Additional employer's contributions in

respect of ill-health and early retirements are accounted for in the year the event arose. Any amount due in year but unpaid will be classed as a current financial asset. Amounts not due until future years are classed as long-term financial assets.

B Transfers to and from other schemes

Transfers in and out relate to members who have either joined or left the Fund.

Individual transfers in/out are accounted for when received or paid. Transfers in from members wishing to use the proceeds of their additional voluntary contributions (see below) to purchase scheme benefits are accounted for on a receipts basis and are included in transfers in (Note 7).

Bulk (group) transfers are accounted for in accordance with the terms of the transfer agreement.

C Investment income

- **Interest income** is recognised in the Pension Fund account as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination.
- **Distributions from pooled funds** are recognised on 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.
- **Changes in the value of investments** (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during the year.

Pension Fund account - expense items

D 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, providing that payment has been approved.

E Management Expenses

The Pension Fund discloses its management expenses in line with CIPFA guidance *Accounting for Local Government Pension Scheme Management Expenses (2016)*, as shown below. All items of expenditure are charged to the Fund on an accruals basis as follows:

- Administrative Expenses – all staff costs relating to the pensions administration team are charged direct to the fund. Council recharges for management, accommodation and other overhead costs are also accounted for as administrative expenses of the fund.
- Oversight and governance – all costs associated with governance and oversight are separately identified, apportioned to this activity and charged as expenses to the fund.
- Investment management expenses – investment fees are charged directly to the Fund as part of management expenses and are not included in or netted off from the reported return on investments. Where fees are netted off returns by investment managers, these expenses are grossed up to increase the change in value of investments. Fees charged by external investment managers and custodians are set out 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. The costs of the Council's in-house fund management team are also charged to the fund as well as a proportion of the time spent by officers on investment management activity.

F Taxation

The Fund 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 fund expenses as it arises.

Net assets statement

G Financial assets

All investment assets are included in the financial statements 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. Any amounts due or payable in respect of trades entered into but not yet complete at 31 March each year are accounted for as financial instruments held at amortised cost and reflected in the reconciliation of movements in investments and derivatives in Note 13a. Any gains or losses on investment sales arising from changes in the fair value of the asset are recognised in the fund account.

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 IFRS 13 (see Note 13). 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).

H Cash and cash equivalents

Cash comprises cash in hand and demand deposits and includes amounts held by the Fund's external managers. All cash balances are short-term, highly liquid investments that are readily convertible to known amounts of cash and are subject to minimal risk of changes in value.

I Loans and receivables

Financial assets classed as amortised cost are carried in the net assets statement at the value of outstanding principal receivable at the year-end plus accrued interest.

J Financial Liabilities

A financial liability is recognised in the net asset statement on the date the fund becomes legally responsible for that liability. The fund recognises financial liabilities relating to investment trading at fair value and any gains and losses arising from changes in the fair value of the liability between contract date, the year-end date and the eventual settlement date are recognised in the fund account as part of the change in the value of investments.

K Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits is assessed on a triennial basis by the Fund actuary in accordance with the requirements of IAS 19 and relevant actuarial standards. As permitted under the Code, the Pension Fund has opted to disclose the actuarial present value of the promised retirement benefits by way of a note to the net assets statement (Note 18).

L Additional voluntary contributions

Shetland Islands Council Pension Fund provides an additional voluntary contributions (AVC) scheme for its members, the assets of which are invested separately from those of the Pension Fund. The Pension Fund has appointed Prudential and Equitable Life (closed to new members) as its AVC providers. AVCs are paid to the AVC provider 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.

AVCs are not included in the accounts in accordance with section 4(1) (b) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 but are disclosed as a note only (Note 23).

M Contingent Liabilities

A contingent liability arises where an event has taken place that gives the Pension Fund a possible obligation whose existence will only be confirmed by the occurrence or otherwise of uncertain future

events not wholly within the control of the Pension Fund. Contingent liabilities also arise in circumstances where a provision would otherwise be made but either it is not probable that an outflow of resources will be required or the amount of the obligation cannot be measured with sufficient reliability.

Contingent liabilities are not recognised in the Balance Sheet but disclosed in a note to the accounts.



Shetland Islands Council Pension Fund (“the Fund”) Actuarial Statement for 2022/23

This statement has been prepared in accordance with Regulation 55(1)(d) of the Local Government Pension Scheme (Scotland) Regulations 2018. 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 Statement (FSS), dated March 2021. In summary, the key funding principles are as follows:

- to ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable where appropriate;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return (NB this will also minimise the costs to be borne by Council Tax payers);
- to reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and
- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

The FSS sets out how the Administering Authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable. For employers whose covenant was considered by the Administering Authority to be sufficiently strong, contributions have been stabilised to have a sufficiently high likelihood of achieving the funding target over 20 years. Asset-liability modelling has been carried out which demonstrate that if these contribution rates are paid and future contribution changes are constrained as set out in the FSS, there is at least a 66% likelihood that the Fund will return to full funding over 20 years.

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 2018 was as at 31 March 2020. This valuation revealed that the Fund's assets, which at 31 March 2020 were valued at £461 million, were sufficient to meet 92% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2020 valuation was £38 million.

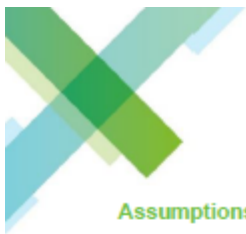
Each employer had contribution requirements set at the valuation, with the aim of achieving full funding within a time horizon and probability measure as per the FSS. Individual employers' contributions for the period 1 April 2021 to 31 March 2024 were set in accordance with the Fund's funding policy 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 2020 valuation report.

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 for the 2020 valuation were as follows:

Financial assumptions	31 March 2020
Discount rate	3.4%
Salary increase assumption	1.7%
Benefit increase assumption (CPI)	1.7%

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 2019 model with an allowance for smoothing of recent mortality experience and a long term rate of improvement of 1.5% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	20.9 years	23.1 years
Future Pensioners*	22.4 years	25.3 years

*Currently aged 45

Copies of the 2020 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2020

Markets were severely disrupted by COVID-19 at the 31 March 2020 funding valuation date, resulting in depressed asset values, but these recovered very strongly in 2020 and 2021. Markets have continued to be disrupted by the ongoing war in Ukraine and inflationary pressures, impacting on investment returns achieved by the Fund's assets. High levels of inflation in the UK (compared to recent experience), have resulted in a higher than expected LGPS benefit increase of 10.1% in April 2023. Despite this, the funding level of the Fund is likely to be higher than reported at the 31 March 2020 funding valuation due to the significant rise in interest rates which reduces the value placed on the Fund's liabilities.

The next actuarial valuation will be carried out as at 31 March 2023. The Funding Strategy Statement will also be reviewed at that time.

Steven Scott FFA

For and on behalf of Hymans Robertson LLP

18 May 2023

Hymans Robertson LLP is a limited liability partnership registered in England and Wales with registered number OC310282.

A list of members of Hymans Robertson LLP is available for inspection at One London Wall, London EC2Y 5EA, the firm's registered office.

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