Public Document Pack

To: Councillor Malik, Convener; Councillor Reynolds, Vice Convener; and Councillors Allard, Bell, Cooke, Councillor Barney Crockett, the Lord Provost, Councillor Alan Donnelly, the Depute Provost; Councillors Delaney and MacGregor (Pensions Committee); and Councillor McKelvie (Chairperson), Ms M Lawrence (Vice-Chairperson); Councillors Allan and Cowe; and Mr I Black, Mr L Knox, Mr K Masson and Mr A Walker (Pension Board).

Town House,
ABERDEEN, 6 September 2018

PENSIONS COMMITTEE AND PENSION BOARD

The Members of the **PENSIONS COMMITTEE AND PENSION BOARD** are requested to meet in **Committee Room 2 - Town House on FRIDAY, 14 SEPTEMBER 2018 at 10.30 am.**

FRASER BELL
CHIEF OFFICER - GOVERNANCE

B U S I N E S S

DETERMINATION OF URGENT BUSINESS

1 There are no items of urgent business at this time

DETERMINATION OF EXEMPT BUSINESS

2 Members are requested to determine that any exempt business be considered with the press and public excluded

DECLARATIONS OF INTEREST

3 Members are requested to intimate any declarations of interest (Pages 3 - 4)

MINUTES OF PREVIOUS MEETINGS

4 Minute of Previous Meeting of 22 June 2018 (Pages 5 - 12)

COMMITTEE PLANNER

5 Committee Business Planner (Pages 13 - 16)

FINANCE, PERFORMANCE, RISK AND SERVICE WIDE ISSUES

6 External Audit Annual Audit Report 2017/2018 - report by External Audit (Pages 17 - 58)

7 Consideration and Signing of Audited Annual Report and Accounts - PC/SEPT18/ACC (Pages 59 - 186)

8 Budget Forecast and Annual Spend - PC/SEPT18/BUD (Pages 187 - 192)

GENERAL BUSINESS

9 Strategy - PC/SEPT18/STRAT (Pages 193 - 244)

EXEMPT BUSINESS - NOT FOR PUBLICATION

10 Asset and Investment Manager Performance Report - PC/SEPT18/AIMPR (Pages 245 - 270)

Members, as a reminder, a training session / presentation will be held following the meeting.

Website Address: www.aberdeencity.gov.uk

Should you require any further information about this agenda, please contact Stephanie Dunsmuir, tel 01224 522503 or email sdunsmuir@aberdeencity.gov.uk

You must consider at the earliest stage possible whether you have an interest to declare in relation to any matter which is to be considered. You should consider whether reports for meetings raise any issue of declaration of interest. Your declaration of interest must be made under the standing item on the agenda, however if you do identify the need for a declaration of interest only when a particular matter is being discussed then you must declare the interest as soon as you realise it is necessary. The following wording may be helpful for you in making your declaration.

I declare an interest in item (x) for the following reasons ....
For example, I know the applicant / I am a member of the Board of X / I am employed by…
and I will therefore withdraw from the meeting room during any discussion and voting on that item.

OR

I have considered whether I require to declare an interest in item (x) for the following reasons .... however, having applied the objective test, I consider that my interest is so remote / insignificant that it does not require me to remove myself from consideration of the item.

OR

I declare an interest in item (x) for the following reasons .... however I consider that a specific exclusion applies as my interest is as a member of xxxx, which is

- (a) a devolved public body as defined in Schedule 3 to the Act;
- (b) a public body established by enactment or in pursuance of statutory powers or by the authority of statute or a statutory scheme;
- (c) a body with whom there is in force an agreement which has been made in pursuance of Section 19 of the Enterprise and New Towns (Scotland) Act 1990 by Scottish Enterprise or Highlands and Islands Enterprise for the discharge by that body of any of the functions of Scottish Enterprise or, as the case may be, Highlands and Islands Enterprise; or
- (d) a body being a company:-
  - i. established wholly or mainly for the purpose of providing services to the Councillor's local authority; and
  - ii. which has entered into a contractual arrangement with that local authority for the supply of goods and/or services to that local authority.

OR

I declare an interest in item (x) for the following reasons……and although the body is covered by a specific exclusion, the matter before the Committee is one that is quasi-judicial / regulatory in nature where the body I am a member of:

- is applying for a licence, a consent or an approval
- is making an objection or representation
- has a material interest concerning a licence consent or approval
- is the subject of a statutory order of a regulatory nature made or proposed to be made by the local authority…. and I will therefore withdraw from the meeting room during any discussion and voting on that item.

This page is intentionally left blank

PENSIONS COMMITTEE AND PENSION BOARD

ABERDEEN, 22 June 2018. Minute of Meeting of the PENSIONS COMMITTEE AND PENSION BOARD. Present:- Councillor Malik, Convener; Councillor Reynolds, Vice-Convener; Councillor Barney Crockett, the Lord Provost; Councillor Alan Donnelly, the Depute Provost; and Councillors Allard, Bell, Cooke and MacGregor (Pensions Committee); and Councillor McKelvie, Chairperson; and Mr S Clunes, Mr K Masson and Mr A Walker (Pension Board).

The agenda and reports associated with this minute can be found here.

Please note that if any changes are made to this minute at the point of approval, these will be outlined in the subsequent minute and this document will not be retrospectively altered.

DETERMINATION OF EXEMPT BUSINESS

1. The Committee was requested to determine that the following items of business, which contained exempt information as described in Schedule 7(A) of the Local Government (Scotland) Act 1973, be taken in private – item 12 (Asset and Investment Manager Performance Report).

The Committee resolved:-
in terms of Section 50(A)(4) of the Local Government (Scotland) Act 1973, to exclude the press and public from the meeting during consideration of item 12, so as to avoid disclosure of exempt information of the class described in paragraph 6.

The Board resolved:-
to note the decision of the Committee.

DECLARATIONS OF INTEREST

2. There were no declarations of interest.

MINUTE OF PREVIOUS MEETING

3. The Committee had before it the minute of its previous meeting of 16 March 2018.

The Committee resolved:-
to approve the minute as a correct record.

The Board resolved:-
to note the decision of the Committee.

COMMITTEE BUSINESS PLANNER

4. The Committee had before it the committee business planner, as prepared by the Chief Officer – Governance.

The Committee resolved:-
to note the business planner.

The Board resolved:-
to note the decision of the Committee.

INTERNAL AUDIT ANNUAL REPORT AND INTERNAL FINANCIAL CONTROL STATEMENT 2017/18 - IA/18/013

5. The Committee had before it a report by Internal Audit which set out the Internal Audit Annual Report for the North East Scotland Pension Fund for 2017/18. The Committee heard from Colin Harvey, Senior Auditor, in respect of the report.

The report recommended:-
that Committee –
(a) note the Annual Report for 2017/18;
(b) note that the Chief Internal Auditor has confirmed the organisational independence of Internal Audit;
(c) note that there has been no limitation to the scope of Internal Audit work during 2017/18; and
(d) note the progress that management has made with implementing recommendations agreed in Internal Audit reports.

The Committee resolved:-
to approve the recommendations.

The Board resolved:-
to note the decision of the Committee.

INTERNAL AUDIT REPORT AC1827 - PENSIONS SYSTEM

6. The Committee had before it a report by Internal Audit which presented the planned Internal Audit report on the Pensions System. The Committee heard from Colin Harvey, Senior Auditor, in respect of the report.

Members asked questions of officers in connection with the report, in respect of the recommendation to Committee in December 2017 to enter a new contract with the current supplier of the Pensions System, and the follow-up report presented to Committee in March 2018 to advise of the potential risk involved due to the supplier having the option to increase the support and maintenance fee by RPI plus 5% annually. Mr Harvey advised that Internal Audit had been involved in extensive discussions with officers as to whether the information should have been included in the December report, however as the decision in respect of the contract had not been taken until March, and the risk had been notified to Committee in March, the recommendation that the Committee should be provided with the full estimated cost of the proposed contract and alternative options had been implemented.

The report recommended:-
that Committee review, discuss and comment on the issues raised within the report and attached appendix.

The Committee resolved:-
to approve the recommendation.

The Board resolved:-
to note the decision of the Committee.

NESPF DRAFT ANNUAL REPORT AND ANNUAL ACCOUNTS 2017-18 - PC/JUN18/AR

7. The Committee had before it a report by the Director of Resources which presented the unaudited Annual Report and Accounts for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund for consideration.

The Committee heard from Laura Colliss, Pensions Manager, in respect of the report. In relation to questions from the Committee about Section 12 (Corporate, Environment and Social Governance) and the NESPF voting, it was suggested that a report containing information on the activities of the Local Authority Pension Fund Forum (LAPFF) would be welcomed, and that an invitation could be extended to the Pensions & Investment Research Consultants Ltd (PIRC) to attend a future meeting.

The report recommended:-
that the Committee review and consider the unaudited Annual Report and Accounts for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund.

The Committee resolved:-
(i) to request that officers consider inviting representatives from PIRC to attend a future meeting; and
(ii) to approve the recommendation.

<u>The Board resolved</u>:-
to note the decision of the Committee.

STRATEGY - PC/JUN18/STRAT

8. With reference to article 14 of the minute of its previous meeting, the Committee had before it a report by the Director of Resources which provided an update on any changes to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund strategies and sought approval for amendments to the Scheme policy documents.

The report contained information and updates on an enhanced administration to payroll module which provided a more streamlined and secure process of passing pensioner data from the administration to payroll system; the Local Government Pension Scheme (Scotland) Regulations 2018 which were expected to come into force from 1 June 2018; the consultation on the LGPS Structure Review; breaches of law; pension fund staff training; and the 2018 Administration Forum to be held on 4 July 2018 at the Beach Ballroom.

The report also highlighted revisions which had been made to the following Scheme policies:-
- Governance Policy
- Communication Policy
- Myners Compliance Statement
- Training Policy
- Reporting Breaches of Law Policy
- Record Keeping Requirements Policy; and
- the new Data Protection Policy

The report recommended:-
That Committee review and approve the Scheme policy document updates as set out in the report at section 3.9.1.

<u>The Committee resolved</u>:-
(i) to request that officers prepare a report for a future meeting of the Committee in respect of engagement and the work of the LAPFF;
(ii) to note that officers would update the Committee on the discussion in respect of the LGPS Structure Review;
(iii) to note that officers would provide information outwith the meeting on the guidance given to participating employers in 2015 to help them to put together their discretions policy following the change of regulations; and
(iv) to approve the recommendations.

The Board resolved:-
to note the decision of the Committee.

NESPF BUSINESS PLAN

9. The Committee had before it the North East Scotland Pension Fund Pension Service Business Plan for 2018 to 2021, which set out officers' plan to build on current strengths and internal capabilities to drive transformation through the Service.

The report advised that the plan would be subject to regular reviews and updates in line with the development of the Local Government Pension Scheme and Aberdeen City Council as the administering authority for the Pension Fund.

The Committee resolved:-
to note the report.

The Board resolved:-
to note the decision of the Committee.

TRAINING PLAN 2018/19 - PC/JUN18/TRA

10. The Committee had before it a report by the Director of Resources which provided details of the training plan for 2018/19 for the Pensions Committee and Pension Board of the North East Scotland Pension Fund, and sought approval for travel to the various training sessions.

The report advised that training would be delivered over two set periods during 2018/19, alongside any external industry delivered training which became available.

It was noted that a training session would be held in London in early 2019 to include presentations from the Fund's fund managers.

There would also be external training opportunities including:-
- Scottish Funds Investment Governance Group – in Edinburgh (date and agenda to be confirmed)
- LGC Investment Seminar Scotland – in Edinburgh, 23-24 October 2018
- Local Authority Pension Fund Forum – location and dates to be confirmed, held quarterly with an annual conference.

The report recommended:-

that Committee:
(a) agree the proposed training scheduled as set out in items 3.4 to 3.8 in the report;
(b) approve the travel of members to the training session in London;
(c) approve the travel of members to external training opportunities; and
(d) approve the travel of members to attend LAPFF meetings.

The Committee resolved:-
to approve the recommendations.

The Board resolved:-
to note the decision of the Committee.

In accordance with the decision recorded under article 1 of this minute, the following items were considered with the press and public excluded.

ASSET AND INVESTMENT MANAGER PERFORMANCE REPORT - PC/JUN18/AIMPR

11. With reference to article 16 of the minute of its previous meeting, the Committee had before it a report by the Director of Resources which provided a review of the investment activity of the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund for the three month period ending 31 March 2018.

The Committee heard from Mr Graham Buntain, Investment Manager, in respect of the detail contained in the report. With reference to the discussion at the previous meeting about the Corporate Social Responsibility Policy and the responsibilities around good social and environmental practice, Mr Buntain advised that although officers had hoped to bring information before Committee at the meeting, discussions were ongoing to try to find a suitable provider who could produce consolidated metrics. Mr Buntain further advised that two of the long-standing fund managers with Aberdeen Property Investors and Blackrock had stepped down.

The report recommended:-
that the Committee note the report.

The Committee resolved:-
(i) to request that officers write to the fund managers to acknowledge their efforts on behalf of the Fund; and
(ii) to approve the recommendation.

The Board resolved:-
to note the decision of the Committee.

- **COUNCILLOR M. TAUQEER MALIK, Convener**

This page is intentionally left blank

	A	B	C	D	E	F	G	H	I
1	**PENSIONS COMMITTEE BUSINESS PLANNER** The Business Planner details the reports which have been instructed by the Committee as well as reports which the Functions expect to be submitting for the calendar year.								
2	**Report Title**	**Minute Reference/Committee Decision or Purpose of Report**	**Update**	**Report Author**	**Chief Officer**	**Directorate**	**Terms of Reference**	**Delayed or Recommended for removal or transfer, enter either D, R, or T**	**Explanation if delayed, removed or transferred**
3			**14 September 2018**						
4	Strategy	Regular update on any changes to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund strategies	On agenda	Mairi Suttie	Finance	Resources	1.2		
5	Asset and Investment Manager Performance Report	To provide a review of the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund for the latest three month period	On agenda	Graham Buntain	Finance	Resources	5.1		
6	Budget Forecast & Annual Spend	Update on budget and annual spend to date	On agenda	Michael Scroggie	Finance	Resources	1.3		
7	Corporate Governance including Local Authority Pension Fund Forum	To provide an update on the Corporate Governance activities (including the LAPFF as requested by Committee on 22/06/18) of the Pension Fund	Included within Asset and Investment Manager Performance Report	Graham Buntain	Finance	Resources	4.1		
8	NESPF Annual Report & Accounts	To present the annual accounts and report on the NESPF	On agenda	Laura Colliss	Finance	Resources	3.1		
9	External Audit Annual Audit Report	To report on the 17/18 External Audit of the NESPF	On agenda	Rachel Browne	External Audit	External Audit	2.1		
10			**30 November 2018**						
11	Strategy	Regular update on any changes to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund strategies		Mairi Suttie	Finance	Resources	1.2		
12	Funding Strategy Statement	To provide an update on the funding strategy statement		Claire Mullen	Finance	Resources	1.2		
13	Asset and Investment Manager Performance Report	To provide a review of the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund for the latest three month period		Graham Buntain	Finance	Resources	5.1		
14	Investment Strategy Update	To provide an update on the Fund's investment strategy and set out any recommendations in respect of the NESPF		Graham Buntain	Finance	Resources	1.2		
15	Update on Annual Benefit Statements	To present the final outcome in respect of the provision of the annual benefit statements to the Fund's active and deferred members		Mairi Suttie	Finance	Resources	Purpose 1		
16	Local Government in Scotland: Financial Overview 2017/18 - LG Pension Funds Supplement	To present the LG Pension Funds Supplement	May not be available for November meeting - may need to be reported in March 2019	Rachel Browne	External Audit	External Audit	2.2		
17	Corporate Governance	To provide an update on the Corporate Governance activities (including the LAPFF) of the Pension Fund		Graham Buntain	Finance	Resources	4.1		

	A	B	C	D	E	F	G	H	I
2	**Report Title**	**Minute Reference/Committee Decision or Purpose of Report**	**Update**	**Report Author**	**Chief Officer**	**Directorate**	**Terms of Reference**	**Delayed or Recommended for removal or transfer, enter either D, R, or T**	**Explanation if delayed, removed or transferred**
18	Budget Forecast & Annual Spend	Update on budget and annual spend to date		Michael Scroggie	Finance	Resources	1.3		
19			**15 March 2019**						
20	Strategy	Regular update on any changes to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund strategies		Mairi Suttie	Finance	Resources	1.2		
21	Budget Forecast & Projected Spend	Update on budget and annual spend to date		Michael Scroggie	Finance	Resources	1.3		
22	Investment Strategy Update	To provide an update on the Fund's investment strategy and set out any recommendations in respect of the NESPF		Graham Buntain	Finance	Resources	1.2		
23	Asset and Investment Manager Performance Report	To provide a review of the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund for the latest three month period		Graham Buntain	Finance	Resources	5.1		
24	Governance Arrangements (Internal Audit)	To present the outcome of the audit to Committee		David Hughes	Governance	Governance	2.2		
25	Corporate Governance	To provide an update on the Corporate Governance activities (including LAPFF) of the Pension Fund		Graham Buntain	Finance	Resources	4.1		
26	Internal Audit Plan 2019/20	To present the internal audit plan 2019/20		David Hughes	Governance	Governance	2.1		
27	External Audit Annual Audit Plan 2018/19	To present the external audit plan 2018/19		Rachel Browne	External Audit	External Audit	2.1		
28	Governance Review	To provide an annual review of governance arrangements		Mairi Suttie	Finance	Resources	4.1 and 4.2		
29	Statement of Accounts	To provide high level information and key dates in relation to the 2018/19 Statement of Accounts		Laura Colliss	Finance	Resources	1.3		
30			**April 2019 Onwards**						
31	Internal Audit Annual Report	To present the annual report to Committee	Apr-19	David Hughes	Governance	Governance	2.1		
32	Annual Committee Effectiveness Report	To present the annual effectiveness report for the Committee.	Jun-19	Steph Dunsmuir	Governance	Governance	GD 7.4		
33	External Audit Annual Audit Report 2018/19	To present the external audit annual audit report	Sep-19	Rachel Browne	External Audit	External Audit	2.1		
34		**AD HOC REPORTS (CYCLE DEPENDENT ON REQUIREMENT TO REPORT)**							

	A	B	C	D	E	F	G	H	I
2	**Report Title**	**Minute Reference/Committee Decision or Purpose of Report**	**Update**	**Report Author**	**Chief Officer**	**Directorate**	**Terms of Reference**	**Delayed or Recommended for removal or transfer, enter either D, R, or T**	**Explanation if delayed, removed or transferred**
35	Request for admitted body status	To consider applications for admission to the Local Government pension scheme administered by Aberdeen City Council		Claire Mullen	Finance	Resources	5.2		

This page is intentionally left blank

4th Floor
102 West Port
Edinburgh EH3 9DN

T: 0131 625 1500
E: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk

AUDIT SCOTLAND

North East Scotland Pension Funds
Pensions Committee

5 September 2018

North East Scotland Pension Fund
Audit of 2017/18 annual accounts

Independent auditor's report

1. Our audit work on the 2017/18 annual accounts is now substantially complete. We anticipate being able to issue unqualified audit opinions in the independent auditor's report on 14 September 2018 (the proposed report is attached at **Appendix A**).

Annual audit report

2. Under International Standards on Auditing in the UK, we report specific matters arising from the audit of the financial statements to those charged with governance of a body in sufficient time to enable appropriate action. We present for the Pension Fund Sub Committee consideration our draft annual report on the 2017/18 audit. The section headed "Significant findings from the audit in accordance with ISA 260" sets out the issues identified in respect of the annual accounts.

3. The report also sets out conclusions from our consideration of the four audit dimensions that frame the wider scope of public audit as set out in the Code of Audit Practice.

4. This report will be issued in final form after the annual accounts have been certified.

Unadjusted misstatements

5. We also report to those charged with governance all unadjusted misstatements which we have identified during our audit, other than those of a trivial nature and request that these misstatements be corrected.

6. There is one unadjusted misstatement:

- A termination fee of £0.212 million was registered with the company liquidator of an employer who left the fund but the final payment, received after the year end, was only £0.086 million. The fund therefore incurred a loss of £0.126 million. The current assets in the NESPF Net Assets Statement are overstated by £0.126 million and the impairment of this debt is understated by the same amount in the NESPF Fund Account.

7. Management have taken the decision not to adjust for this misstatement as it is not considered to be material.

Fraud, subsequent events and compliance with laws and regulations

8. In presenting this report to the Pensions Committee we seek confirmation from those charged with governance of any instances of any actual, suspected or alleged fraud; any subsequent

events that have occurred since the date of the financial statements; or material non-compliance with laws and regulations affecting the entity that should be brought to our attention.

Representations from Section 95 Officer

9. As part of the completion of our audit, we are seeking written representations from the Section 95 Officer on aspects of the annual accounts, including the judgements and estimates made.

10. A draft letter of representation is attached at **Appendix B**. This should be signed and returned to us by the Section 95 Officer with the signed annual accounts prior to the independent auditor's report being certified.

APPENDIX A: Proposed Independent Auditor's Report

Independent auditor's report to the members of Aberdeen City Council as administering authority for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund and to the Accounts Commission

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 120 of the Code of Audit Practice approved by the Accounts Commission, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Report on the audit of the financial statements

Opinion on financial statements

I certify that I have audited the financial statements in the annual report of the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund (the funds) for the year ended 31 March 2018 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Fund Accounts, the Net Assets Statements and Notes to the Pension Fund Accounts, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 (the 2017/18 Code).

In my opinion the accompanying financial statements:

- give a true and fair view in accordance with applicable law and the 2017/18 Code of the financial transactions of the funds during the year ended 31 March 2018 and of the amount and disposition at that date of their assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2017/18 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Basis for opinion

I conducted my audit in accordance with applicable law and International Standards on Auditing (UK) (ISAs (UK)). My responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of my report. I am independent of the funds in accordance with the ethical requirements that are relevant to my audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standard, and I have fulfilled my other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Conclusions relating to going concern basis of accounting

I have nothing to report in respect of the following matters in relation to which the ISAs (UK) require me to report to you where:

- the use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Chief Officer – Finance has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the funds' ability to continue to

adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Responsibilities of the Chief Officer – Finance and Aberdeen City Council Pensions Committee for the financial statements

As explained more fully in the Statement of Responsibilities, the Chief Officer – Finance is responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Chief Officer – Finance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Chief Officer – Finance is responsible for assessing the funds' ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless deemed inappropriate.

The Aberdeen City Council Pensions Committee is responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit of the financial statements

My objectives are to achieve reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of the auditor's responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website www.frc.org.uk/auditorsresponsibilities. This description forms part of my auditor's report.

Other information in the annual report

The Chief Officer – Finance is responsible for the other information in the annual report. The other information comprises the information other than the financial statements and my auditor's report thereon. My opinion on the financial statements does not cover the other information and I do not express any form of assurance conclusion thereon except on matters prescribed by the Accounts Commission to the extent explicitly stated later in this report.

In connection with my audit of the financial statements, my responsibility is to read all the other information in the annual report and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit or otherwise appears to be materially misstated. If I identify such material inconsistencies or apparent material misstatements, I am required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

Report on other requirements

Opinions on matters prescribed by the Accounts Commission

In my opinion, based on the work undertaken in the course of the audit:

- the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with statutory guidance issued under the Local Government in Scotland Act 2003;

- the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016); and
- the information given in the Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations 2014.

Matters on which I am required to report by exception

I am required by the Accounts Commission to report to you if, in my opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- I have not received all the information and explanations I require for my audit.

I have nothing to report in respect of these matters.

Gillian Woolman MA FCA CPFA
Audit Director
Audit Scotland
4th Floor
102 West Port
Edinburgh
EH3 9DN

14 September 2018

APPENDIX B: Letter of Representation (ISA 580)

Gillian Woolman
Audit Director
Audit Scotland
4th Floor
102 West Port
Edinburgh
EH3 9DN

Dear Gillian

North East Scotland Pension Funds
Annual Accounts 2017/18

1. This representation letter is provided about your audit of the annual accounts of North East Scotland Pension Funds for the year ended 31 March 2018 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view in accordance with the financial reporting framework, and for expressing other opinions on the management commentary, annual governance statement and governance compliance statement.

2. I confirm to the best of my knowledge and belief, and having made appropriate enquiries of relevant officers, the following representations given to you in connection with your audit of North East Scotland Pension Funds annual accounts for the year ended 31 March 2018.

General

3. North East Scotland Pension Funds and I have fulfilled our statutory responsibilities for the preparation of the 2017/18 annual accounts. All the accounting records, documentation and other matters which I am aware are relevant to the preparation of the annual accounts have been made available to you for the purposes of your audit. All transactions undertaken by North East Scotland Pension Funds have been recorded in the accounting records and are properly reflected in the financial statements.

4. I confirm that the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the financial statements as a whole. I am not aware of any uncorrected misstatements other than those reported by you.

Financial Reporting Framework

5. The annual accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 (2017/18 accounting code), and in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Government in Scotland Act 2003 and The Local Authority Accounts (Scotland) Regulations 2014.

6. In accordance with the 2014 regulations, I have ensured that the financial statements give a true and fair view of the financial position of the North East Scotland Pension Funds at 31 March 2018 and the transactions for 2017/18.

Accounting Policies & Estimates

7. All significant accounting policies applied are as shown in the notes to the financial statements. The accounting policies are determined by the 2017/18 accounting code where applicable. Where the code does not specifically apply I have used judgement in developing and applying an accounting policy that results in information that is relevant and reliable. All accounting policies applied are appropriate to North East Scotland Pension Fund circumstances and have been consistently applied.

8. The significant assumptions used in making accounting estimates are reasonable and properly reflected in the financial statements. Judgements used in making estimates have been based on the latest available, reliable information. Estimates have been revised where there are changes in the circumstances on which the original estimate was based or as a result of new information or experience.

Going Concern Basis of Accounting

9. I have assessed North East Scotland Pension Funds ability to continue to use the going concern basis of accounting and have concluded that it is appropriate. I am not aware of any material uncertainties that may cast significant doubt on North East Scotland Pension Funds ability to continue as a going concern.

Assets

Investments

10. For the year ended 31 March 2018, the amounts included in the net assets statements reflect investments managed/held both internally and externally by appointed fund managers and the global custodian on behalf of the funds. Amounts have been calculated in accordance with approved bases of valuation and fairly represent the values at 31 March 2018. In making these assertions I am reliant on the opinions of the appointed fund managers. As far as we can reasonably ascertain, all assets are free from any lien, encumbrance or charge except as disclosed in the financial statements.

Banking and Cash Flow Arrangements

11. The pension funds maintain separate bank accounts and while these accounts form part of Aberdeen City Council's treasury management arrangements, the pension fund can demonstrate that there is no borrowing from the administering authority. Amounts due to the administering authority to cover daily cash flows such as payments through the council's systems are reimbursed on a regular basis.

Other Current Assets

12. On realisation in the ordinary course of the funds' business, the other current assets in the Net Assets Statements are expected, in my opinion, to produce at least the amounts at which they are stated. In particular adequate provision has, in my opinion, been made against all amounts owing which are known or may be expected to be irrecoverable.

Liabilities

13. All liabilities at 31 March 2018 of which I am aware have been recognised in the annual accounts.

14. Provisions have been recognised in the financial statements for all liabilities of uncertain timing or amount at 31 March 2018 of which I am aware where the conditions specified in the 2017/18 accounting code have been met. The amount recognised as a provision is the best estimate of the expenditure likely to be required to settle the obligation at 31 March 2018. Where the effect of the time value of money is material, the amount of the provision has been discounted to the present value of the expected payments.

15. Provisions recognised in previous years have been reviewed and adjusted, where appropriate, to reflect the best estimate at 31 March 2018 or to reflect material changes in the assumptions underlying the calculations of the cash flows.

16. The pension assumptions made by the actuary in the IAS 19 report for North East Scotland Pension Funds have been considered and I confirm that they are consistent with management's own view.

17. There are no plans or intentions that are likely to affect the carrying value or classification of the liabilities recognised in the financial statements.

Contingent liabilities

18. There are no significant contingent liabilities, other than those disclosed in Note 29 to the financial statements, arising either under formal agreement or through formal undertakings requiring disclosure in the accounts. All known contingent liabilities have been fully and properly disclosed, including any outstanding legal claims which have not been provided under the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 and IAS 37

Fraud

19. I have provided you with all information in relation to:

- my assessment of the risk that the financial statements may be materially misstated because of fraud
- any allegations of fraud or suspected fraud affecting the financial statements
- fraud or suspected fraud that I am aware of involving management, employees who have a significant role in internal control, or others that could have a material effect on the financial statements.

Laws and Regulations

20. I have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements.

Related Party Transactions

21. All material transactions with related parties have been disclosed in the financial statements in accordance with the 2017/18 accounting code. I have made available to you the identity of all the North East Scotland Pension Funds' related parties and all the related party relationships and transactions of which I am aware.

Management commentary

22. I confirm that the Management Commentary has been prepared in accordance with the statutory guidance and the information is consistent with the financial statements.

Corporate Governance

23. I confirm that the North East Scotland Pension Funds has undertaken a review of the system of internal control during 2017/18 to establish the extent to which it complies with proper practices set out in the Delivering Good Governance in Local Government: Framework 2016. I have disclosed to you all deficiencies in internal control identified from this review or of which I am otherwise aware.

24. I confirm that the Annual Governance Statement has been prepared in accordance with the Delivering Good Governance in Local Government: Framework 2016 and the information is consistent with the financial statements. There have been no changes in the corporate governance arrangements or issues identified, since 31 March 2018, which require to be reflected.

Events Subsequent to the Date of the Balance Sheet

25. All events subsequent to 31 March 2018 for which the 2017/18 accounting code requires adjustment or disclosure have been adjusted or disclosed.

Yours sincerely

Jonathon Belford, CPFA
Chief Officer - Finance

This page is intentionally left blank

North East Scotland Pension Fund DRAFT

2017/18 Annual Audit Report

To Members of the Aberdeen City Council Pensions Committee and the Controller of Audit

14 September 2018

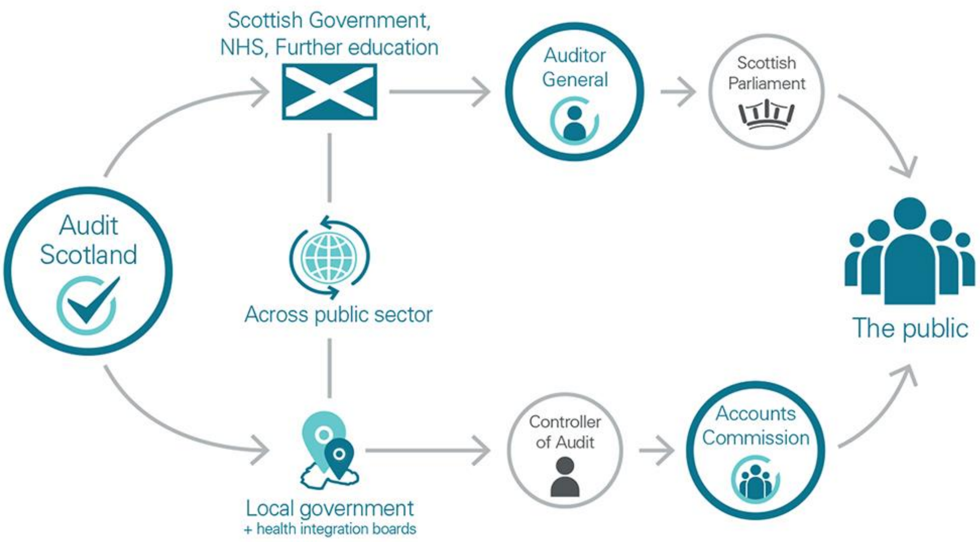
Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.

- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.

- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money

- reporting our findings and conclusions in public

- identifying risks, making clear and relevant recommendations.

Contents

Key messages

2017/18 annual report and accounts

1 In our opinion the North East Scotland Pension Fund's financial statements give a true and fair view and were properly prepared.

2 The management commentary, annual governance statement and governance compliance statement are all consistent with the financial statements and properly prepared.

Financial management

3 The fund has effective arrangements in place for financial management. This includes comprehensive reporting of investment performance.

4 The fund's investment return performance in comparison to other Scottish LGPS funds has improved in 2017/18 compared to 2016/17, with a move from second lowest to second highest performer.

Financial sustainability

5 The 2017 triennial funding valuation assessed the Main Fund as 107% funded, an increase of 13% from the 2014 valuation. Council employers' contribution rates are maintained for 2018-2021 at 2017/18 levels. Other employers' contribution rates range from 11% to 33.8%.

6 The 2017 triennial funding valuation assessed the Transport Fund as 94% funded, an increase of 1% from the 2014 valuation. Employer contributions will remain at the current level for 2018-2021, but with an additional £1.5 million payment per annum, to reduce the deficit.

7 Although Main Fund contributions from members currently exceed benefits paid out, this is likely to change in the coming years.

Governance and transparency

8 The fund has effective governance arrangements in place that support scrutiny of decisions made by the Pensions Committee.

9 Decisions are transparent with committee papers and detailed minutes of meetings of the Pensions Committee available on the fund's website and on Aberdeen City Council's website.

Value for money

10 The fund has adequate arrangements in place for monitoring investment performance and scrutinising investment management expenses. Investment performance is subject to regular review and scrutiny by the Pensions Committee.

Introduction

1. This report is a summary of our findings arising from the 2017/18 audit of the North East Scotland Pension Fund (NESPF). The Fund consists of two funds, the North East Scotland Pension Fund (the main fund) and the Aberdeen City Council Transport Fund (the transport fund). Both funds are part of the Local Government Pension Scheme (LGPS). Hereafter we will refer to "the Fund" in the singular.

2. The scope of our audit was set out in our Annual Audit Plan presented to the March 2018 meeting of the Aberdeen City Council Pensions Committee. This report comprises:

- an audit of the Fund's annual accounts
- consideration of the wider dimensions that frame the wider scope of public audit set out in the *Code of Audit Practice 2016* as illustrated in Exhibit 1.

Exhibit 1
Audit dimensions

Source: Code of Audit Practice 2016

3. The main elements of our audit work in 2017/18 have been:

- a review of the Fund's main financial systems
- an audit of the fund's 2017/18 annual accounts including the issue of an independent auditor's report setting out our opinions
- consideration of the four audit dimensions.

4. Aberdeen City Council is the administering authority for the pension fund. The council delegates this responsibility to the Pensions Committee. The Committee is responsible for establishing effective governance arrangements and ensuring that financial management is effective. Additionally, the Committee is required to review the effectiveness of internal control arrangements and approve the annual accounts.

5. Our responsibilities as independent auditors are established by the Local Government (Scotland) Act 1973, the *Code of Audit Practice 2016*, and supporting guidance, and are guided by the auditing profession's ethical guidance.

6. As public sector auditors we give independent opinions on the annual accounts. We also review and provide conclusions on the effectiveness of the Fund's performance management arrangements, suitability and effectiveness of corporate governance arrangements, and financial position and arrangements for securing financial sustainability.

7. Further details of the respective responsibilities of management and the auditor can be found in the *Code of Audit Practice 2016.*

8. This report raises matters from the audit of the annual accounts, risks and control weaknesses. Communicating these does not absolve management from its responsibility to address the issues we raise, and to maintain adequate systems of control.

9. Our annual audit report contains an agreed action plan at Appendix 1 setting out specific recommendations, responsible officers and dates for implementation. It also includes outstanding actions from last year and progress against these.

10. We can confirm that we comply with the Financial Reporting Council's Ethical Standard. We can also confirm that we have not undertaken any non-audit related services and the 2017/18 audit fee of £40,000 as set out in our Annual Audit Plan, remains unchanged. We are not aware of any relationships that could comprise our objectivity and independence.

Adding value through the audit

11. Our aim is to add value to the North East Scotland Pension Fund by providing insight and foresight, by identifying areas of improvement and by recommending and encouraging good practice. In so doing, we aim to help the Fund promote improved standards of governance, better management and decision making and more effective use of resources.

12. This report is addressed to both the members of the Pensions Committee and the Controller of Audit and will be published on Audit Scotland's website www.audit-scotland.gov.uk.

13. We would like to thank all management and staff who have been involved in our work for their co-operational and assistance during the audit.

Part 1
Audit of 2017/18 annual accounts

Main judgements

In our opinion North East Scotland Pension Fund's financial statements give a true and fair view and were properly prepared.

The management commentary, annual governance statement and governance compliance statement are all consistent with the financial statements and properly prepared.

Unqualified audit opinions

14. The annual accounts for the year ended 31 March 2018 were approved by Aberdeen City Council Pensions Committee on 14 September 2018. We reported, within our independent auditor's report:

- an unqualified opinion on the financial statements;
- the management commentary, annual governance statement and governance compliance statement were all consistent with the financial statements and properly prepared in accordance with the guidance
- we have nothing to report in respect of those matters which we are required by the Accounts Commission to report by exception.

The Fund's annual accounts is the principal means by which the pension fund demonstrates effective stewardship and use of resources to its external stakeholders.

Submission of annual accounts for audit

15. We received the unaudited annual accounts on 25 June 2018, in line with the audit timetable set out in our 2017/18 Annual Audit Plan.

16. The working papers provided with the unaudited accounts were of a good standard and finance staff provided good support to the audit team. This helped ensure the final accounts audit process ran smoothly.

Risks of material misstatement

17. Appendix 2 provides a description of those assessed risks of material misstatement that were identified during the planning process which had the greatest effect on the overall audit strategy, the allocation of staff resources to the audit and directing the efforts of the audit team. We also include the wider dimension risks, how we addressed these and our conclusions in the appendix.

Materiality

18. Misstatements are material if they could reasonably be expected to influence the economic decisions of users taken based on the financial statements. The assessment of what is material is a matter of professional judgement and involves considering both the amount and nature of the misstatement.

19. Our initial assessment of materiality for the annual accounts was carried out during the planning phase of the audit. We assess the materiality of uncorrected misstatements, both individually and collectively. The assessment of materiality was recalculated on receipt of the unaudited financial statements and is summarised in Exhibit 2. The revised materiality levels were not sufficient to require a change in our audit approach.

Exhibit 2

Materiality values

Materiality level	Amount
Overall materiality – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It was set at 10% of contributions receivable for the year ended 31 March 2018 based on the unaudited accounts.	Main Fund £13.8 million Transport Fund £0.245 million
Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement, we have calculated performance materiality at 75% of overall materiality.	Main Fund £10.3 million Transport Fund £0.184 million
Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 2.5% of overall materiality. (With a maximum level of £100,000).	Main Fund £100,000 Transport Fund £6,000

How we evaluate misstatements

20. There were no material adjustments to the unaudited financial statements arising from our audit. In common with previous years, the Private Equity (type 3) investments have been updated in the audited accounts for more recent valuations received from the fund managers. The unaudited accounts were prepared with the most up to date figures available for Private Equity (type 3) investments, as at 31 December. The Private Equity valuations as at 31 March were received by the Pension Fund in August and the accounts were updated for these figures. The result was an increase of £8 million in Private Equity investments.

Significant findings from the audit in accordance with ISA 260

21. International Standard on Auditing 260 (UK & Ireland) requires us to communicate significant findings from the audit to those charged with governance. These are summarised below in Exhibit 3. Where a finding has resulted in a recommendation to management, a cross reference to the Action Plan in Appendix 1 has been included.

22. The findings include our views about significant qualitative aspects of the Fund's accounting practices including:

- Accounting policies
- Accounting estimates and judgements
- Significant financial statements disclosures
- Timing of transactions and the period in which they are recorded
- The impact on the financial statements of any uncertainties
- The effect of any unusual transactions on the financial statements
- Misstatements in the annual accounts
- Disagreement over any accounting treatment or financial statements disclosure

Exhibit 3
Significant findings from the audit of financial statements

Issue	Resolution
1. **Events after the reporting period** The risk of employers being unable to meet their pension obligations is managed through the NESPF Termination Policy and the NESPF Employer Covenant Assessment Policy. At 31 March 2018 the Fund recognised that there were three employers who had exited from the Fund where payment of the termination fee may not be recovered in full. For one of these, a termination fee of £0.212 million had been registered with the company liquidator but the final payment, received after the year end, was only £0.086 million. The fund therefore incurred a loss of £0.126 million. The current assets in the NESPF Net Assets Statement are overstated by £0.126 million and the impairment of this debt is understated by the same amount in the NESPF Fund Account.	Management decided that this amount was not material and therefore did not adjust the 2017/18 accounts. This is recorded as an unadjusted misstatement of £0.126 million.

Source: North East Scotland Pension Fund 2017/18 matters arising

Good practice in financial reporting

23. The annual report and accounts include all the required disclosures for pension fund accounts. We noted Section 12 “Corporate, Environmental and Social Governance” as a good practice example. It reports the activities and engagement of the fund in relation to good corporate governance and good social and environmental practice. This includes:

- Voting at the AGMs of companies the fund invests in, to influence the management of those companies. The main reasons for voting ‘against’ the companies are disclosed (e.g. vote on dividend or dividend policy not put to shareholders, not rotating audit firms on a regular basis, high level of audit fees potentially leading to undue influence over the auditor, executive pay deemed to be excessive etc.) A link to the fund’s voting record is included.

- Engagement through the Local Authority Pension Fund Forum (LAPFF) to support shareholder resolutions on climate change; to engage with companies on: employment standards, use of cluster munitions, sexual harassment, worker access to corporate boards; and seeking assurances from companies on how they are addressing cyber security risks.

- Principles for Responsible Investment (PRI): the fund signed up in 2010 to PRI’s aspirational and voluntary guidelines for investment entities wishing to address environmental, social and corporate governance issues. The disclosure includes 2017/18 issues (working practices: fire and building safety, labour issues: labour standards, and climate change) and a link to where further information can be found.

Other findings

24. Our audit identified several presentational and disclosure issues which were discussed with management. These were adjusted and reflected in the audited annual accounts. This includes disclosing the full Governance Compliance

Statement rather than including a link to the statement on the fund's website, which is a requirement of the guidance for local government pension fund annual report and accounts. The presentation of some performance measures was also amended to make it clearer.

Pre-audit inspection and objections to the accounts

25. The Local Authority Accounts (Scotland) Regulations 2014 require local government bodies to publish a public notice on their website that includes details of the period for inspecting and objecting to the accounts. This must remain on the website throughout the inspection period. The notice for the North East Scotland Pension Fund was published on the website of the administering authority (Aberdeen City Council) and complies with the regulations. No objections were received on the North East Scotland Pension Fund accounts.

Part 2

Financial management

Main judgements

The fund has effective arrangements in place for financial management. This includes comprehensive reporting of investment performance.

The Fund's investment return performance in comparison to other Scottish LGPS funds has improved in 2017/18 compared to 2016/17, with a move from second lowest to second highest performer.

Financial performance in 2017/18

26. Pension fund finances are independently assessed every three years by an actuary. This assessment determines the employer contribution rates and deficit funding payments for the upcoming three-year period and takes account of the strength of employer covenants and the fund's investment strategy (see paragraphs 40-44).

27. The Fund's performance in 2017/18 is summarised in Exhibit 4. This shows that the net assets of the Fund increased to £4.1 billion at 31 March 2018 from £3.8 billion at 31 March 2018. The Transport Fund's net assets increased by £0.1 million to £100 million. This represents an increase of 7.95% for the Main Fund and 0.11% for the Transport Fund.

Exhibit 4

Assets, liabilities, funding level and investment performance

Increase in net assets	Increase in estimated liabilities	Funding level	Investment performance
Main Fund	**Main Fund**	**107% Main Fund**	**7.95% Main Fund**
+£303 million	**+£174 million**	**94% Transport Fund**	**0.11% Transport Fund**
(+7.95%)	(+24.1%)	2017 Funding Valuation	Return on investments 2017/18
Transport Fund	**Transport Fund**		
+£0.1 million	**-£7.6 million**		
(0.11%)	(13.7%)		

Closing net assets: Main Fund £4,118 million Transport Fund £100.0 million	Closing liabilities: Main Fund £4,892 million Transport Fund £78 million	94% Main Fund 93% Transport Fund 2014 Funding Valuation	Return on investments over 5 years: Main Fund 10.7% Transport Fund not reported

Source: NESPF 2017/18 audited financial statements and NESPF reports

28. In addition to the Triennial Funding Valuation, the fund's actuary also undertakes a valuation of pension fund liabilities (actuarial present value of promised retirement benefits) at the accounting date as required by International Accounting Standard (IAS) 26 and calculated in line with IAS 19 assumptions. This uses the same base data as the Triennial Funding Valuation rolled forward to the current financial year, taking account of changes in membership numbers and updating assumptions to the current year. This valuation is not carried out on the same basis as that used for setting employer contribution rates and the Fund does not take account of liabilities to pay pensions and other benefits in the future.

29. The actuarial present value of promised retirement benefits estimates the Main Fund's liabilities increasing from £4.7 billion at 31 March 2017 to £4.9 billion at 31 March 2018 (£174 million increase). Transport Fund pension liabilities decreased from £85.6 million at 31 March 2017 to £78 million at 31 March 2018. It should be recognised that not all funds have liabilities assessed on the same prudential scales. The use of differing actuarial firms and assumptions creates difficulties in direct comparisons. It should be noted that this valuation is an accounting estimate.

Financial management arrangements

30. From 3 September 2018, the Chief Officer - Finance for Aberdeen City Council is the proper officer responsible for the North East Scotland Pension Fund. The financial regulations of Aberdeen City Council, as administering authority, apply to the pension fund. We consider these to be comprehensive, and current, and promote good financial management.

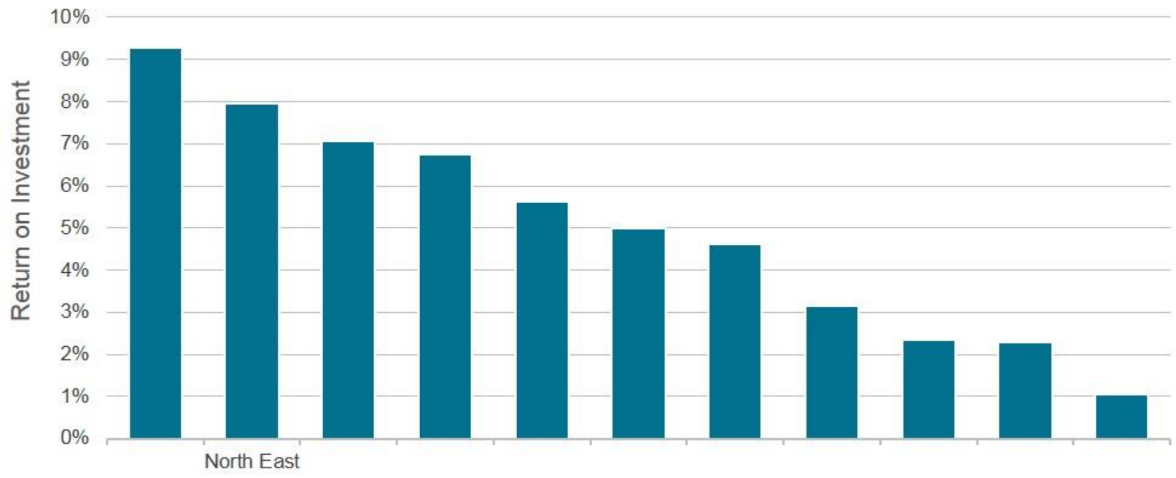
31. Investment and administration performance reports are submitted to the Pensions Committee on a quarterly basis. Reports are comprehensive covering reviews of the equity and bond markets, overall performance of the funds and reviews of the performance of each investment manager. Through our attendance at Pensions Committee meetings we have observed a good level of review and scrutiny by members.

32. Based on evidence reviewed, we conclude that the Fund has effective financial management arrangements in place, including comprehensive reporting and review of investment performance.

Financial outcomes

33. 2017/18 has been a relatively good year for investment performance for most LGPS pension funds across Scotland as illustrated in Exhibit 5.

Exhibit 5
LGPS pension funds – Net return on investment 2017/18 (unaudited figures)



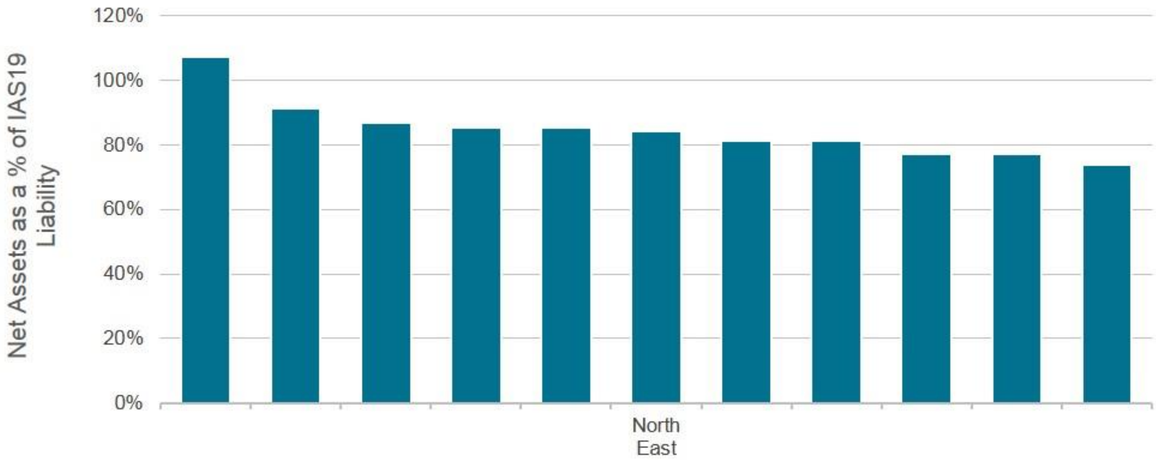
Source: 2017/18 LGPS pension fund unaudited financial statements

34. Exhibit 5 shows that the North East Scotland Pension Fund's in year investment return is 7.95% which, compared to other Scottish LGPS funds, sits in the top 2 performers in terms of net return on investments (based on unaudited figures for 2017/18). This is an improvement in its position compared to 2016/17 when its investment return placed the Fund second lowest across all local government pension funds in Scotland and below the Fund's own target. We note that the relative performance should not be considered without acknowledging that there are different investment strategies for different funds.

35. We have concluded that the pension fund's overall performance is good. However, the pension fund requires to continually monitor performance as it is unlikely that high performance returns will continue.

36. The IAS19 calculations give a guide to the relative funding positions of each fund as shown in Exhibit 6. When this is considered the North East Scotland Pension Fund is mid-range for 2017/18.

Exhibit 6
Net Assets as a proportion of IAS19 Liability as at 31 March 2018



Source: 2017/18 LGPS pension fund unaudited financial statements

Systems of internal control

37. As part of our audit we identify and inspect the key internal controls in those accounting systems which we regard as significant for the production of the financial statements.

38. The Pension Fund uses some of the administering authority's key financial systems, in particular the general ledger, payroll and accounts payable systems. We requested assurances from KPMG, the external auditor of Aberdeen City Council, that the internal controls over these financial systems were operating effectively during 2017/18. Initially their planned audit approach was to be fully substantive and would not provide the requested assurance. However, the 2017/18 interim and final audit reports for Aberdeen City Council reported controls testing in the following areas, with satisfactory results: journal authorisation; payroll controls related to employee standing data, when joining, leaving and making changes; and controls around the transfer of pension data from the pension team to the actuaries. There was one recommendation from the testing of general IT controls including user access: that the review of ledger user access includes consideration of whether access is appropriate to the user's role. (Internal audit also made recommendations about strengthening controls especially super user access.) KPMG have given an unmodified opinion on Aberdeen City Council's 's 2017/18 accounts.

39. Internal audit's annual opinion for Aberdeen City Council confirmed "that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's framework of governance, risk management and control in the year to 31 March 2018."

40. We have taken assurance over the administering authority's financial systems from these sources.

41. Our audit testing of the fund's own pension administration system did not identify any significant internal control weaknesses which could affect the Fund's ability to record, process, summarise and report financial and other relevant data to result in a material misstatement in the financial statements.

Part 3

Financial sustainability

Main judgement

The 2017 triennial valuation assessed the Main Fund as 107% funded, an increase of 13% from the 2014 valuation. Council employers' contribution rates are maintained for 2018-2021 at 2017/18 levels. Other employers' contribution rates range from 11% to 33.8%.

The 2017 triennial valuation assessed the Transport Fund as 94% funded, an increase of 1% from the 2014 valuation. Employer contributions will remain at the current level for 2018-2021, but with an additional £1.5 million payment per annum, to reduce the deficit.

Although Main Fund contributions from members currently exceed benefits paid out, this is likely to change in the coming years.

Funding position and financial planning

42. The March 2017 triennial funding valuation reports that the Main Fund assets were sufficient to meet 107% of its liabilities, which compares to 94% at the 2014 triennial review. The funding level means that, overall, the investment assets were higher than the projected liabilities. This enabled the fund to maintain the employer's contribution rate at 19.3% for the three councils for the period 2018-2021. The rates for the other bodies range from 11% to 33.8%.

Financial sustainability looks forward to the medium and longer term to consider whether the Fund maintains the capacity to meet the current and future needs of its members.

43. The Transport Fund was assessed as 94% funded, meaning that the Fund's assets were sufficient to cover 94% of its liabilities. The administering authority and the employer, First Aberdeen Limited, have agreed to maintain the current level of contributions which are 33% of pensionable pay (plus £1.5 million per annum which is being used to finance the costs in relation to future service). On this basis the deficit would be expected to be removed in around 5 years. These contributions will continue over the period 2018-2021 unless the funding level reaches 105% as assessed by the fund actuary.

44. As identified at Exhibit 10 the Main Fund still has a positive cash flow in that contributions received exceed benefits payable. However as shown at Exhibit 7 the increase in member numbers is decreasing, while the number of pensioners is increasing. The fund will move to a situation in the coming years where the benefits payable by the main fund will exceed contributions received and current pensioners will need to be paid from investment income or the sale of investments.

Membership levels

45. The pension fund is a multi-employer fund with 3 local authorities, and around 50 other employers. The current membership profile is shown at Exhibit 7. The number of active members continues to outweigh the number of pensioners.

Exhibit 7
Main Fund Membership

Source: NESPF 2017/18 audited financial statements

46. Membership of the main fund increased slightly by 239 in 2017/18 to 25,568 members at 31 March 2018; over the past 5 years membership has grown by 2,688 active members, which represents an increase of 11.7%. The impact of auto-enrolment contributed to the increase in members.

47. The Transport Fund, which is closed to new entrants, continues to fall in overall membership numbers and more members move to pensioner status. This is shown in Exhibit 8 below.

48. The Fund gives its members a guarantee that in exchange for contributions during their employment, the Fund will pay a pension until the end of each member's life. It is important that the fund maintains the capacity to meet the current and future needs of its members.

Exhibit 8
Transport Fund Membership

Source: NESPF 2017/18 audited financial statements

Contributions

49. Following the latest triennial valuation in 2017, the Actuary agreed employer contribution rates with individual employers for 2018/19 onwards. An element of these employer costs includes deficit recovery contributions to support employers financial planning. The approximate split of all contributions received in year is set out at Exhibit 9. Other scheduled bodies include Aberdeenshire Council, Moray Council and 8 other bodies.

Exhibit 9
Contributions in 2017/18

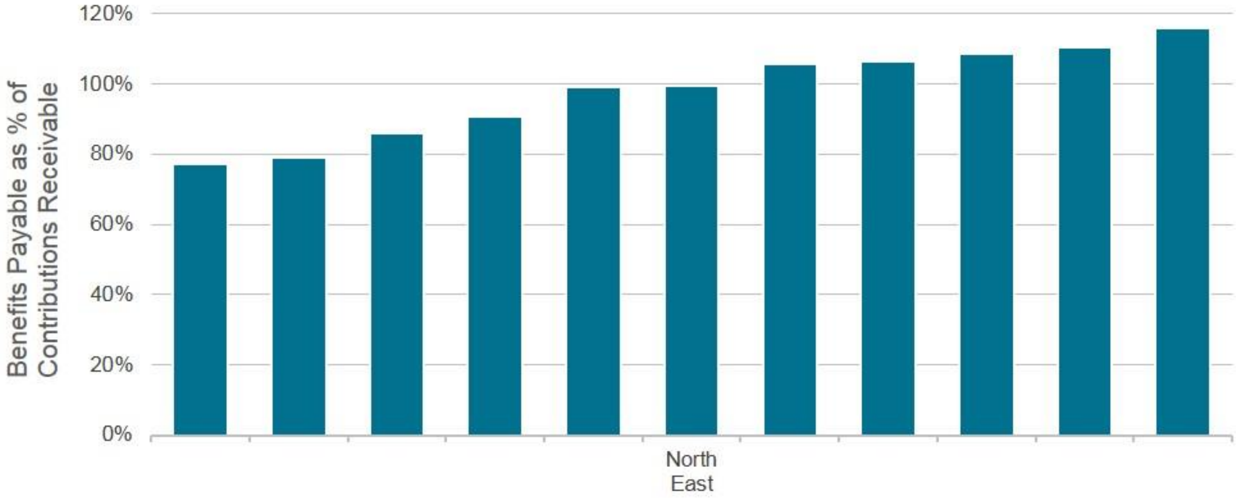
	Administering authority £m	Other scheduled bodies £m	Admitted bodies £m	Transferee Admission Bodies £m	Total £m
Employer contributions	26.751	56.009	6.427	3.251	92.438
Employee contributions	8.504	17.797	2.104	1.127	29.532
Strain Contributions	5.050	1.160	0.552	0	6.762
Deficit Recovery Contributions	2.312	3.513	0.095	0	5.920

Source: NESPF 2017/18 audited financial statements

50. The main fund reported a surplus from dealings with members of £2.9 million in 2017/18. This means that member contributions and investment income exceeded pension payments. Exhibit 10 below shows how North East Scotland Pension Fund compares with the other ten local government pension funds in Scotland in terms of contributions receivable and benefits payable. Five of the eleven pay out more than they receive. The North East Scotland Pension Fund is close to becoming one of the funds that pays out more in pensions than it receives in contributions. This is likely to be the case in future years. The Transport Fund has been in that position for a number of years.

Exhibit 10

Main Fund Benefits Payable as a proportion of contributions receivable

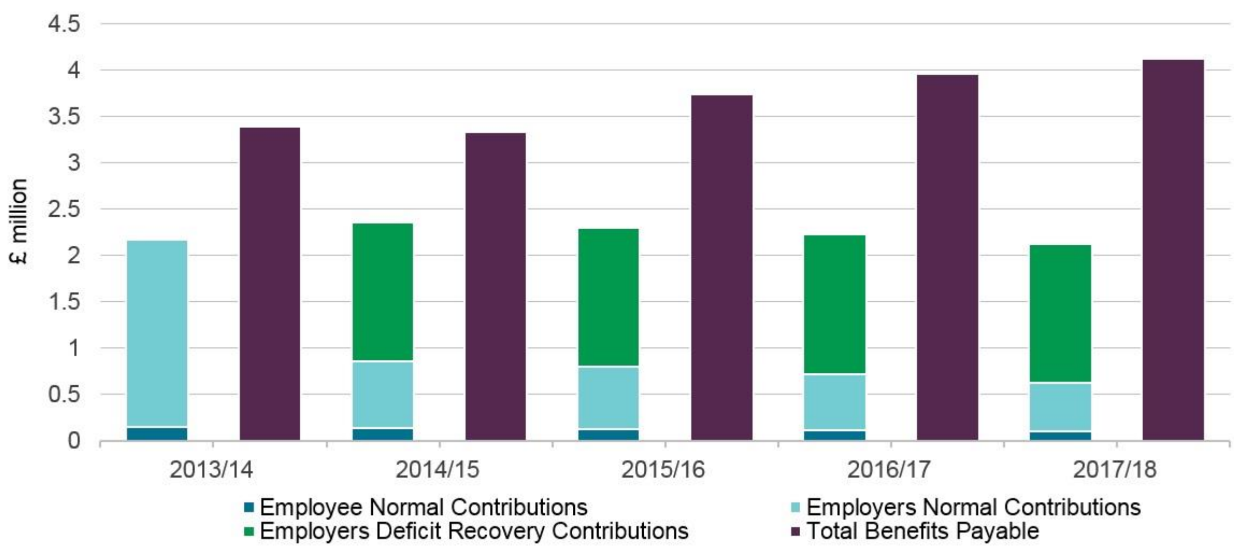


Source: 2017/18 LGPS pension fund unaudited financial statements

51. The Transport Fund is a closed fund and has not been open to new members for a number of years. Pension contributions, including £1.5 million annual deficit recovery payments, are exceeded significantly by benefits payable (see Exhibit 11 for contributions and benefits payable over the past 5 years). In 2017/18 total contributions were £2.448 million and benefits payable were £4.126 million. Therefore, investment income is relied on in funding pension payments.

Exhibit 11

Transport Fund Contributions in 2017/18



Source: NESPF 2017/18 audited financial statements

EU withdrawal

52. There remains significant uncertainty about the detailed implications of EU withdrawal (i.e. Brexit). It is critical that public sector bodies are working to understand, assess and prepare for the impact on their business in three broad areas:

- Workforce - the extent to which changes to migration and trade policies are likely to affect the availability of skilled and unskilled labour.
- Funding – the extent to which potential changes to funding flows are likely to affect the finances of the organisation and the activity that such funding supports.
- Regulation – the extent to which potential changes to regulation across a broad range of areas overseen at an EU level are likely to affect the activities of the organisation.

53. The fund recognises the difficulty of planning for Brexit amid considerable uncertainty. In terms of the market implications for investment performance, the fund is taking a diversified, balance approach to mitigate against the risk. For example, reducing equity investment and increasing investment in infrastructure, which is not as tied to global events.

Part 4

Governance and transparency

Main judgements

The fund has effective governance arrangements in place that support scrutiny of decisions made by the Aberdeen City Council Pensions Committee.

Decisions are transparent with committee papers and detailed minutes of meetings of the Pensions Committee available on the fund's website and on Aberdeen City Council's website.

Governance arrangements

54. Aberdeen City Council is the administering body for the North East Scotland Pension Fund. The Council has delegated responsibility for governance to the Pensions Committee. This committee, supported by the Pension Board, is responsible for establishing arrangements that ensure the proper conduct of the affairs of North East Scotland Pension Fund. It is also responsible for ensuring that decisions are made within the terms of the Local Government Pension Scheme.

55. The Pension Board was established by the Public Service Pensions Act 2013. Its role is to assist the Scheme Manager in securing compliance with scheme regulations and expectations set by the Pensions Regulator. The Pension Board meets concurrently with the Pensions Committee. Its annual report is available on the fund's website and on the administering authority's website.

56. There have been significant changes in the membership of the Pensions Committee and Pension Board during 2017/18, largely due to the local government elections in May 2017. The fund must ensure that members are provided with training so that they are clear about their roles and responsibilities and are kept up to date on current issues so that they can scrutinise papers effectively.

57. From our attendance at committee meetings we concluded that committee papers were well prepared and issued a week before meetings to allow time for review, sufficient time was given to discuss the issues on the agenda, and committee members asked appropriate questions. We concluded that arrangements were appropriate and supported good governance and accountability.

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

Transparency

58. Transparency means that the public, in particular pension fund members, have access to understandable, relevant and timely information about how the Fund is taking decisions and how it is using resources.

59. There is evidence from several sources which demonstrate the Fund's commitment to transparency. For example, the Fund's annual accounts and information on governance arrangements are available on the Fund's website. The annual accounts are also available on the administering authority's website.

60. The Pensions Committee and Pension Board meetings are held in public, with commercially sensitive information dealt with in private session. The committee papers and minutes of these meetings are publicly available on the pension fund's website and on the administering authority's website.

61. Overall, we concluded that the Fund conducts its business in an open and transparent manner.

Other aspects of governance

62. We reviewed various other aspects of governance that apply to the Fund including standing orders, financial regulations and arrangements for reporting breaches of regulation to the Pensions Regulator.

63. Last year we reported that the Orders of Reference for the Pensions Committee had not been updated. The Pension Fund provided updated Orders of Reference to the administering authority and these were approved by the council in March 2018.

64. Overall, we concluded that there are open and transparent arrangements in place.

Pensions Regulator Public Service Code

65. The Public Sector Pensions Act 2013 provided for extended regulatory oversight by the Pensions Regulator. The Pensions Regulator issued a code on the governance and administration of public service pension schemes in January 2015 which funds are expected to comply with. The last report assessing the Fund's compliance with the Pensions Regulator's code was submitted to the Pensions Committee and Pension Board in March 2018. This provided assurance that the Fund is largely in compliance with the regulations. There were no breaches of the Code that required to be reported to the Pensions Regulator in 2017/18.

Internal audit

66. Internal audit provides the Fund with independent assurance on the Fund's overall risk management, internal control and corporate governance processes.

67. The internal audit function is carried out by Aberdeenshire Council's internal audit service. We conducted a review of the adequacy of the internal audit function and concluded that it operates in accordance with the Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place.

68. Every local authority internal audit function must be externally assessed against the Public Sector Internal Audit Standards (PSIAS) once every 5 years. In 2017 Aberdeen City Council engaged KPMG to undertake a review of the internal audit function covering the PSIAS requirements and making comparisons to best practice for an entity listed on the London Stock Exchange. The report assessed internal audit as fully or generally compliant with the majority of the standards and partially compliant with the rest. Where the service was partially complaint, recommendations were made. These related to: closer linking of the audit plan to the council's risk register; a multi-year strategic plan; key performance indicators; management agreement of detailed scopes; communication with and feedback from key stakeholders. KPMG's report recommendations and Internal Audit's' response to these were presented to and noted by Aberdeen City Council's Audit, Risk and Scrutiny Committee in November 2017. Actions accepted by Internal Audit were approved by Committee, the majority of which have since been implemented.

69. To avoid duplication of effort we place reliance on the work of internal audit wherever possible. In 2017/18 we did not place any formal reliance on internal audit reviews for obtaining direct assurance for our financial statements work, as the coverage was not directly relevant to our audit of the financial statements. We considered internal audit's report findings on the pensions system as part of our wider dimension work.

Management commentary, annual governance statement and governance compliance statement

70. The applicable legislation and regulations require pension funds to prepare and publish, along with their financial statements, a management commentary (or equivalent), an annual governance statement, and a governance compliance statement that are consistent with the disclosures made in the financial statements. The management commentary should be fair, balanced and understandable and clearly address the longer-term financial sustainability of the body.

71. Based on our knowledge and work performed, we concluded that the management commentary, the annual governance statement and the governance compliance statement are consistent with the financial statements.

Standards of conduct for prevention and detection of fraud and error

72. We assessed the Fund's arrangements for the prevention and detection of fraud. The Fund relies on the administering body's (Aberdeen City Council) arrangements for the prevention and detection of fraud and corruption. These include Codes of Conduct for members and officers, a whistleblowing policy and a counter-fraud strategy.

73. We concluded that appropriate arrangements were in place for preventing and detecting fraud and corruption in 2017/18.

Cyber security

74. The Scottish Government issued a Public Sector Action Plan on Cyber Resilience in November 2017 which requires all public sector bodies to carry out a review to ensure their cyber security arrangements are appropriate. Bodies are encouraged to seek independent assurance of critical technical controls, which in the Scottish Government's view is achieved by obtaining Cyber Essentials or Cyber Essentials Plus accreditation. We note that the administering authority has Cyber Essentials (Plus) accreditation.

General Data Protection Regulation

75. The new General Data Protection Regulation (GDPR) came into force on 25 May 2018. This replaced the UK Data Protection Act 1998. As a Regulation, all EU member states must implement it in the same way. GDPR sets out further requirements than the DPA and has introduced new and significantly changed data protection concepts.

76. GDPR introduces a wide range of new rights for individuals in respect of their personal data. These include the right to be forgotten, the right to object to certain processing activities and to decisions taken by automated processes. Failure to comply with new GDPR data handling arrangements could result in the Fund incurring significant fines.

77. The North East Scotland Pension Fund project group, involving all teams, carried out a data gathering exercise to identify all areas that would be affected by GDPR. The fund has reviewed its documentation and contracts. It also met with other Scottish pension funds and the software supplier to identify system developments (delivered at the start of 2018) to ensure readiness for GDPR. Data protection information for members is easily accessible on its website. We concluded that the Pension Fund has made good progress in planning for and implementing GDPR requirements.

Good practice

78. The North East Scotland Pension Fund is a member of the software supplier's national Testing Working Party. The fund's receipt of early software releases (there were two in 2017/18, tested by NESPF and 5 other LGPS funds) contributes to its readiness for change, including readiness for GDPR.

Part 5
Value for money

Main judgements

The Fund's investment performance is subject to regular review and scrutiny by the Aberdeen City Council Pensions Committee.

The Fund has adequate arrangements in place for monitoring investment performance and scrutinising investment management expenses.

Investment performance

79. The Pensions Committee meets on a quarterly basis. A review of fund managers' performance is a standing item on the committee's agenda. At each meeting, committee members receive a report outlining overall fund performance including an analysis of risks and returns. The committee also considers the performance of individual investment managers.

80. In 2005 a long term investment strategy for the Main Fund was agreed with a customised benchmark that aimed to deliver a return of 1% above the benchmark over a rolling three year period. Exhibit 12 shows that over the year, the Fund generated a return of 11.1% against a benchmark of 3.0%. Equity portfolios were the most significant contributor to this increase.

Exhibit 12
Fund investment performance

Source: North East Scotland Pension Fund 2017/18 audited financial statements

81. Over the medium to longer term the Fund has outperformed its benchmark over three years, five years and over the longer term since inception.

82. As shown earlier in Exhibit 5 net investment performance compared favourably with other local government pension funds in Scotland.

Value for money is concerned with using resources effectively and continually improving services.

83. The Fund appoints several external investment managers. Individual investment manager performance is reported on a quarterly basis to the Pensions Committee. The Fund's investments team also carries out annual diligence reviews for each appointed fund manager.

84. Investment return and risk are inextricably linked, and it is not possible for us to give an opinion on the relative performance of the Fund's investments given the risk exposure of the asset allocation and investments made. However, we are aware that the Pensions Committee is regularly updated with details of how closely aligned the Fund's investments are with its investment strategy. The Fund is currently taking steps to realign the portfolio asset allocations with the investment strategy, which have become out of line due to the increase in equity valuations.

85. We concluded that the Fund has adequate arrangements in place for monitoring investment performance.

Management expenses

86. There are three main categories of management expense, with the largest being investment management costs. Other expenses are the cost of the administration services provided by the council and the governance fees for actuarial and audit services.

87. CIPFA published revised guidance on local government pension scheme management expenses (LGPS). This guidance sets out a framework for the reporting of investment management costs and was applied from 2016/17. The new guidance recommends that only expenses that can be directly controlled by the fund should be included.

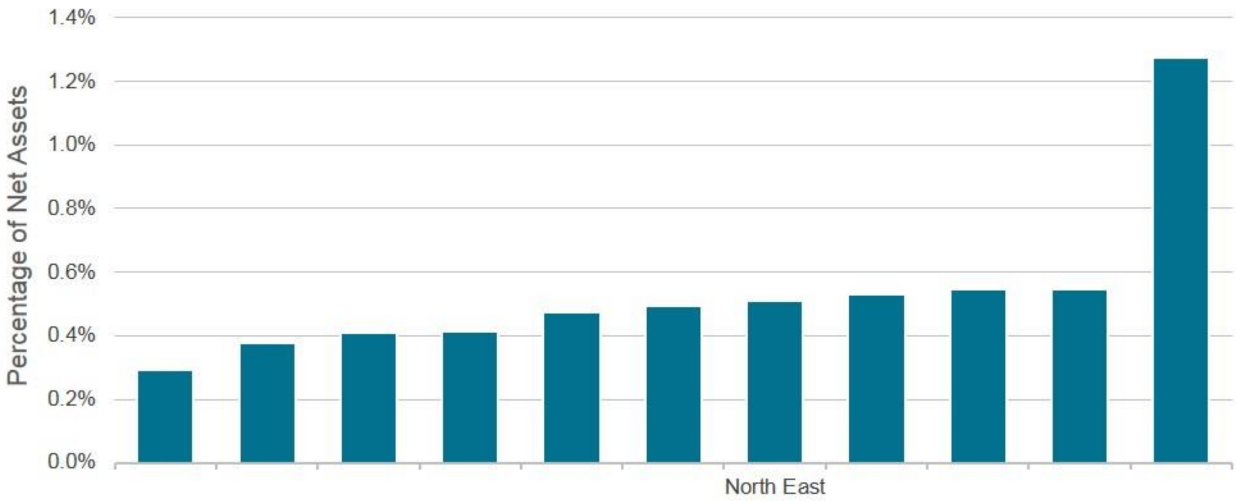
88. Now that the additional information on the cost of LGPS investment management services is available, the Fund should continue to review the level of management expenses. This includes the development of bench-marking information and in the context of returns achieved, to ensure that value for money is being secured.

89. External investment manager fees are agreed in the respective mandates governing their appointments. Generally, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments changes.

90. Total management expenses have increased from £18.5m in 2016/17 to £20.9m in 2017/18. This is primarily due to increased investment management fees aligned to the increased value of the Fund and an increase in performance fees as a result of the relative return on investments in 2017/18 against benchmarks.

91. Exhibit 13 (page 26) shows figures for total management expenses relative to net assets across the Scottish Local Government Pension Funds, with investment management expenses for the North East Scotland Pension Fund highlighted. The Fund had the fourth highest percentage in Scotland; however, variances in investment strategies and administrative structures (e.g. in-house staff vs. outsourced services) will impact on the amount of external investment management expertise purchased.

Exhibit 13
Investment Management Expenses



Source: 2017/18 LGPS pension fund unaudited financial statements

Administrative expenses

92. The workload of the pension administration section continues to grow, primarily due to the introduction of the career average pension scheme (CARE) from 1 April 2015. Other factors, such as auto enrolment, also increase the administration workload. Fund membership has increased by 11.7% in the past 5 years.

93. Employers are required to submit contributions returns to the Pension Fund; this is an important control over the accuracy of pension contributions received and recorded in the pensions system and is of increased importance following the introduction of CARE as the member benefit statement requires actual salary data from all employers. The fund made monthly online submissions of data a mandatory requirement for employers from 1st April 2017. This facility was an extension of a system used by larger employers, which was amended to cater towards the needs and capabilities of smaller employers, with 96% of employers providing information online.

94. The Fund's business plan sets out a range of service standards against which administration performance is monitored. These are measured on a regular basis and are reported to the Pensions Committee.

National performance audit reports

95. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2017/18, we published reports which might be of direct interest to the Fund. These are outlined in Appendix 3 accompanying this report.

96. The Pensions Committee considered the LGPS supplement to the Local Government in Scotland: Financial Overview 2016/17 at its March 2018 meeting. We have drawn other relevant publications to the attention of the committee during the year.

Good practice

97. The pension fund was named “Public Sector Scheme of the Year” at the Professional Pensions Pension Scheme Awards. The Fund was judged against several criteria including investment management, communications, governance, innovation and administration and the win recognises the achievements made in improving their service to members and employers.

Appendix 1

Action plan 2017/18

2017/18 recommendations for improvement

No.	Issue/risk	Recommendation	Agreed management action/timing
Follow up of prior year recommendations			
b/f	**1. Pensions Committee Orders of Reference** The Pensions Committee Orders of Reference within Aberdeen City Council's Standing Orders have not been updated to reflect changes in pension fund governance. The Orders of Reference still refer to the Joint Investment Advisory Committee, which was disbanded in March 2015. **Risk** Out of date committee information on the website may reduce public confidence in the quality of published information and imply that regular review of governance information does not occur.	The Pension Fund should request that the administering authority updates the Pension Committee Orders of Reference within the council's Standing Orders.	**Updated audit response** The Pension Fund provided the administering authority with a revised version of the Orders of Reference and these were approved by the council in March 2018. No further action required: **closed**.

Appendix 2

Significant audit risks identified during planning

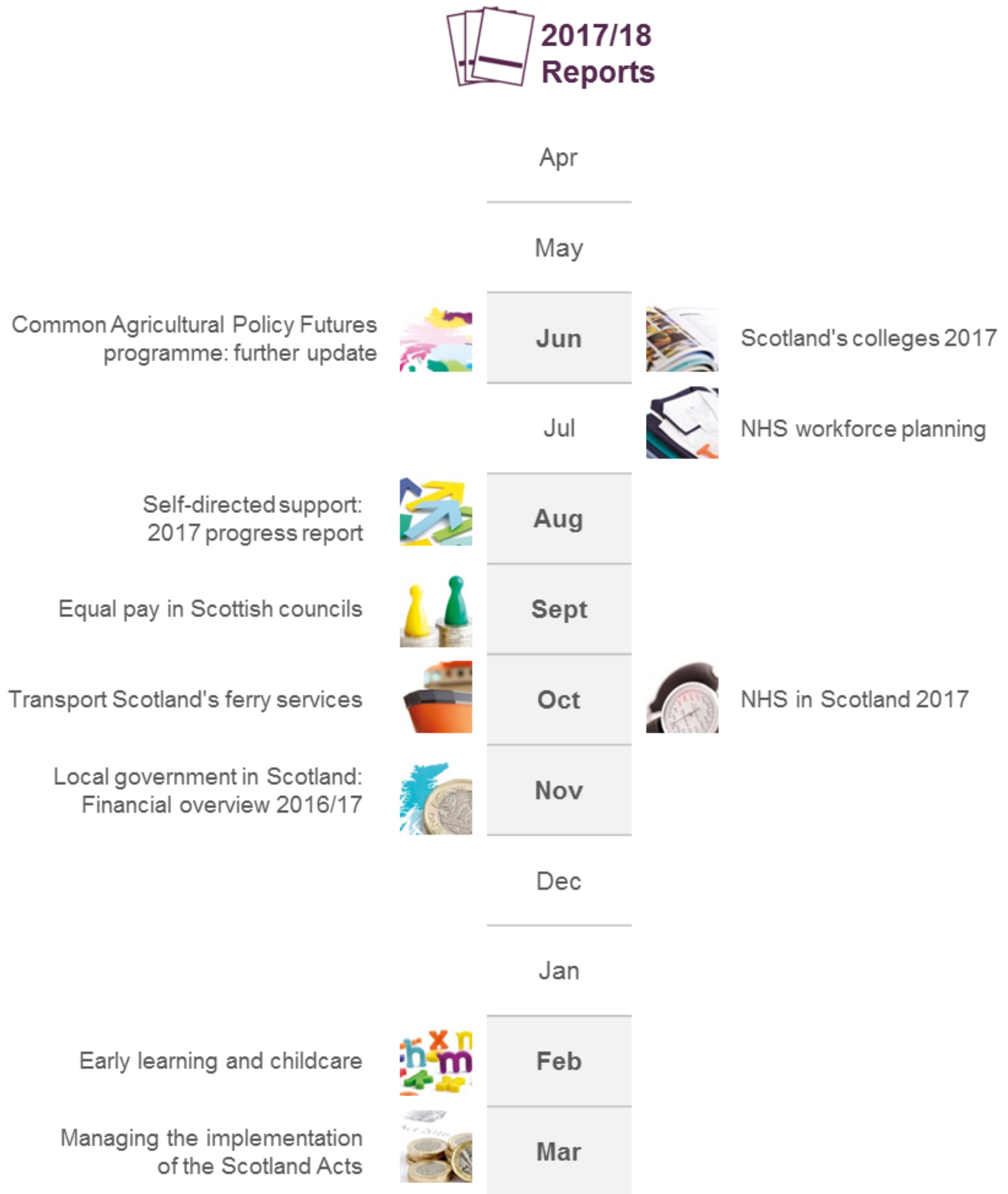
The table below sets out the audit risks we identified during our planning of the audit and how we addressed each risk in arriving at our conclusion. The risks are categorised between those where there is a risk of material misstatement in the annual accounts and those relating our wider responsibility under the *Code of Audit Practice 2016*.

Audit risk	Assurance procedure	Results and conclusions
Risks of material misstatement in the financial statements		
1 Assurances on administering authority key financial systems used by NESPF Aberdeen City Council (ACC) is the administering authority for the North East Scotland Pension Fund. Several ACC key financial systems (general ledger; accounts payable; accounts receivable) underpin the NESPF accounting records. We are dependent on the council's external auditor, KPMG, for audit assurances on these systems.	• Assurances will be agreed with and obtained from KPMG on key Aberdeen City Council financial systems which underpin NESPF accounting records.	Requested assurances were not provided due to the planned substantive nature of the Aberdeen City Council audit. We have taken assurance from KPMG's interim and annual audit reports to Aberdeen City Council, which reported on controls testing undertaken. We anticipate requiring additional assurances on internal controls next year as we can no longer take prior year assurance from earlier work by the previous auditor.
2 Risk of management override of controls ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.	• Detailed testing of journal entries. • Review of accounting estimates. • Evaluation of significant transactions that are outside the normal course of business.	Based on our testing, we found no evidence of bias in accounting estimates, no evidence of transactions out with the scope of the pension fund and no evidence to suggest that management were overriding controls.
3 Risk of fraud over income and expenditure ISA 240 presumes a risk of fraud over income; this is expanded to include the risk of fraud over expenditure in the public sector by the Code of Audit Practice and the Financial Reporting Council's Practice Note 10 (revised). The North East Scotland Pension Fund receives a significant amount of investment income from third	• Evaluating the effectiveness of systems for income recognition and recording. • Conduct a review of third party service providers, where relied upon by management, including review of service auditor reports. • Analytical procedures on income and expenditure streams.	Interim controls testing results were satisfactory. We carried out 'reliance on a management expert' work on the custodian and the actuary and concluded that we could place reliance on third parties. Analytical procedures on income and expenditure, sample checking of pension contributions and confirmation of investment income did not identify any issues.

Audit risk	Assurance procedure	Results and conclusions
party sources. This presents a risk due to the extent and complexity of income. The Pension Fund also makes a high volume of payments, including high value payments, which can constitute a risk of misstatement of expenditure.	• Agree income to third party confirmation. • Substantive testing of expenditure. • Assurances on contributions obtained from scheduled body external auditors.	We found no evidence of fraud over income.
4 **Estimation and judgements** There are two areas with a significant degree of subjectivity: • the measurement and valuation of investments; • the actuarial valuation. Investments include level 3 investments such as unquoted equity (private equity) where valuations use techniques that require significant judgement in determining appropriate assumptions. The actuarial valuation depends on a number of assumptions about the future. These include investment returns, contribution rates, commutation assumptions, pensioner mortality, discount rates and earning assumptions. This subjectivity represents an increased risk of misstatement in the financial statements.	• Confirm valuations to valuation reports and/or other supporting documentation. • Completion of 'review of the work of an expert' in accordance with ISA500, for the work of the actuary and the custodian. • Consideration of the report by PwC in their capacity as consulting actuary to Audit Scotland on actuarial assumptions in use in 2017/18. • Consideration of GAD reports under Section 13 of the Local Government Pension Scheme (Scotland) of LGPS Scotland funding valuations and employer contribution rates.	We carried out 'reliance on a management expert' work on the custodian and the actuary. This included review of the PwC report on actuarial assumptions. We concluded that we could place reliance on the custodian and the actuary. The draft accounts were amended to reflect the Private Equity level 3 investment valuations which were available in August 2018. We substantively checked all valuations to fund manager reports.
5 Changes to financial reporting Pension funds will be required to disclose information on investment management transaction costs, including the amount for each asset class, their nature, and how they arise for different types of investment. It is essential that the pension fund is in a position to capture these costs.	• Communication of technical changes with officers. • Agree amounts in primary financial statements to supporting documentation from third parties.	Officers were aware of the requirements when preparing the accounts. We agreed the disclosure on investment management transaction costs to supporting documentation. We concluded that the disclosure of this information was in line with the requirements.

Appendix 3

Summary of national performance reports 2017/18



Reports relevant to local government pension funds

Local Government in Scotland: financial overview 2016/17 - LGPS Supplement – November 2017

North East Scotland Pension Fund DRAFT

2017/18 Annual Audit Report

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or **info@audit-scotland.gov.uk**

For the latest news, reports and updates, follow us on:

Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
T: 0131 625 1500 E: **info@audit-scotland.gov.uk**
www.audit-scotland.gov.uk

AS.1.4

ABERDEEN CITY COUNCIL

COMMITTEE	PENSIONS COMMITTEE
DATE	14 SEPTEMBER 2018
REPORT TITLE	CONSIDERATION AND SIGNING OF AUDITED ANNUAL REPORT AND ACCOUNTS
REPORT NUMBER	PC/SEPT18/ACC
DIRECTOR	STEVEN WHYTE
CHIEF OFFICER	JONATHAN BELFORD
REPORT AUTHOR	LAURA COLLISS
TERMS OF REFERENCE	PENSIONS COMMITTEE 3.1

1. PURPOSE OF REPORT

1.1 To provide the Audited Annual Report and Accounts for the North East Scotland Pension Fund (NESPF) and the Aberdeen City Council Transport Fund (ACCTF) for consideration and signing.

2. RECOMMENDATION

That the Committee: -

2.1 Consider and approve the Audited Annual Report and Accounts for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund; and

2.2 Instruct the Chief Officer - Finance as the Local Government (Scotland) Act 1973 - Section 95 Officer to sign the accounts on behalf of the Funds.

3. BACKGROUND/MAIN ISSUES

3.1 Further to The Local Authority Accounts (Scotland) Regulations 2014 the audited Annual Report and Accounts for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund are presented to Committee for their consideration and approval.

Appendix I, North East Scotland Pension Fund and the Aberdeen City Council Transport Fund Annual Report and Accounts.

4. FINANCIAL IMPLICATIONS

4.1 There are no direct financial implications arising from the recommendations of this report.

5. LEGAL IMPLICATIONS

5.1 The Local Authority Accounts (Scotland) Regulations 2014 require the accounts to be approved no later than 30th September.

Section 95 of The Local Government (Scotland) Act 1973 requires the Council to make arrangements for the proper administration of their financial affairs and to secure that the proper officer of the administering authority has responsibility for the administration of those affairs. For the North East Scotland Pension Funds, that officer is the Chief Officer - Finance of Aberdeen City Council.

6. MANAGEMENT OF RISK

6.1 There are no direct risk implications arising from the recommendations of this report.

7. OUTCOMES

Design Principles of Target Operating Model	
	Impact of Report
Governance	This report links to the 'Governance' design principle as its publication demonstrates the Council's proper stewardship and accountability of the public funds with which it is entrused.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Equality & Human Rights Impact Assessment	Not required
Privacy Impact Assessment	Not required
Duty of Due Regard / Fairer Scotland Duty	Not applicable

9. BACKGROUND PAPERS

None

10. APPENDICES

Appendix I, North East Scotland Pension Fund and the Aberdeen City Council Transport Fund Annual Report and Accounts

11. REPORT AUTHOR CONTACT DETAILS

Laura Colliss
Pensions Manager
LColliss@nespf.org.uk
01224 264158

This page is intentionally left blank

North East Scotland
PENSION FUND

ANNUAL REPORT & ACCOUNTS

FOR THE PERIOD

1 APRIL 2017 TO 31 MARCH 2018

ABERDEEN CITY COUNCIL, ADMINISTERING AUTHORITY FOR THE ABERDEEN CITY COUNCIL PENSION FUND, KNOWN AS NORTH EAST SCOTLAND PENSION FUNDS

ABERDEEN
CITY COUNCIL

Contents

Management Commentary

1. About the North East Scotland Pension Funds

The North East Scotland Pension Fund (NESPF) and the Aberdeen City Council Transport Fund (ACCTF) are administered by Aberdeen City Council within Local Government Pension Scheme (LGPS) regulations.

The Scheme was established under the Superannuation Fund Act 1972 and is open to all employees of the 11 scheduled bodies, except for those whose employment entitles them to belong to another statutory pension scheme (e.g. Police, Fire, Teachers). Employees of admitted bodies can join the Scheme subject to the admitted bodies' individual admission criteria, which are outwith the control of Aberdeen City Council.

The Funds' investments are externally managed in accordance with the Local Government Pension Scheme (Scotland) (Management and Investment of Funds) Regulations 2010.

All pension benefits are paid in accordance with the Local Government Pension Scheme (Benefits Membership and Contributions) (Scotland) Regulations 2008 as amended.

The Aberdeen City Council Transport Fund was created in October 1986 for employees of the former passenger Transport Undertaking who transferred to the limited company now known as First Aberdeen, which was created at that time.

The Funds are built up from contributions from both employees and employing bodies, together with interest, dividends and rent from investments, out of which pensions and other benefits are paid.

Employee contributions are fixed by statute while employer contributions are assessed every three years by an independent Actuary to determine the level of contributions necessary by employing bodies to ensure that the Funds are able to meet all future benefits.

With effect from 1 April 2009, employee contributions are based on tiered rates. Below are the tiered rates for 2017/18:

Band	Range	Contribution Rate
1	On earnings up to and including £20,700	5.50%
2	On earnings above £20,700 and up to £25,300	7.25%
3	On earnings above £25,300 and up to £34,700	8.50%
4	On earnings above £34,700 and up to £46,300	9.50%
5	On earnings above £46,300	12.00%

2. Administration 2017/18

Administering Authority	Aberdeen City Council
Committees	Pensions Committee, Pension Board
Director of Resources*	Steven Whyte
Chief Officer – Finance*	Jonathan Belford
Actuary	Mercer
Global Custodian	BNP Paribas
Performance Measurement	BNP Paribas
Bank	Clydesdale Bank
AVC Providers	Prudential, Standard Life Assurance Company
External Auditors	Audit Scotland
Internal Auditors	Aberdeenshire Council
Investment Consultant	KPMG
Employers	For full details see Appendix 2

*The Section 95 Officer is responsible for the financial administration of the Pension Fund. Steven Whyte, Director of Resources was the Section 95 Officer until 2 September 2018 after which Jonathan Belford, Chief Officer – Finance subsumed this role.

3. Pensions Committee & Pension Board

Pensions Committee

Aberdeen City Council is the administering authority for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund. The Council delegates this responsibility to the Pensions Committee.

The Pensions Committee carries out a role similar to that of trustees of a pension scheme. It is the key decision maker for all matters under LGPS Regulations including benefit administration and investment management.

The Council and the Pensions Committee recognise that they have fiduciary duties and responsibilities towards pension scheme members, participating employers and local taxpayers.

The Pensions Committee is comprised of 9 elected members of Aberdeen City Council.

Membership during 2017/18

Councillor M. Tauqueer Malik (Convener)
Councillor John Reynolds (Vice Convener)
Councillor Barney Crockett
Councillor Neil MacGregor
Councillor Jim Noble (left May 2017)
Councillor Aileen Malone (left May 2017)
Councillor Alan Donnelly (left August 2017)
Councillor James Kiddie (left May 2017)
Councillor Willie Young (left May 2017)
Councillor Steve Delaney (joined May 2017)
Councillor Jennifer Stewart (joined August 2017)
Councillor Philip Bell (joined May 2017)
Councillor John Cooke (joined May 2017)
Councillor Christian Allard (joined May 2017)

Pension Board

In line with scheme regulations, the Funds established a Pension Board in 2015/16. The Pension Board is responsible for assisting the Scheme Manager in relation to compliance with scheme regulations and the requirements of the Pensions Regulator.

Board membership should consist of equal numbers of trade union representatives and employer representatives, drawn from Councils and scheduled or admitted bodies.

Membership during 2017/18:

Ms. M Lawrence	Unison		
Mr. K Masson	GMB		
Mr. A Walker	Unite		
Mr S Clunes	UCATT	Joined Feb 2018	
Councillor L Ironside	Aberdeen City Council	Left May 2017	
Councillor F John	Aberdeen City Council	Joined May 2017, Left Aug 2017	
Councillor A Donnelly	Aberdeen City Council	Joined Aug 2017, left Mar 2018	
Councillor W Howatson	Aberdeenshire Council	Left May 2017	
Councillor A McKelvie	Aberdeenshire Council	Joined May 2017	
Councillor J Cowe	The Moray Council		
Ms. M Hart	Police Scotland	Left Apr 2018	
Councillor B Stuart	Aberdeenshire Council	Substitute	Left May 2017
Councillor A Bews	Aberdeenshire Council	Substitute	Joined May 2017

In line with the training policy, Board members undertook 4 training sessions within 2017/18 with further dates/opportunities identified including Fund Manager Presentations and investment seminars in 2018/19.

The Board sits at the same time as the Pensions Committee and receives the Committee report for each meeting which includes reports on all areas of the Pension Funds: Investment, Accounting, Governance, Employer Relationship, Administration and Technical.

In assisting with compliance the Board can report the Funds to the Pensions Regulator for non-compliance with guidance or regulations. In 2017/18 no issues were reported by the Board to the Pensions Regulator.

The full Pension Board Annual Report can be viewed on our website at www.nespf.org.uk

4. Administration and Performance

This year's administration report focuses on statement compliance, General Data Protection Regulation (GDPR), Guaranteed Minimum Pension (GMP) reconciliation, Testing Working Party (TWP), actuarial valuation and the pension administration strategy.

Statement Compliance

The biggest administrative challenge for the NESPF continues to be the requirement to issue benefit statements to all active members by the 31 August. In total 24,409 statements were issued to active members prior to the deadline which represented 99.76% compliance. We were able to identify the outstanding members to allow us to rectify the data issues on the administration system and prevent future reoccurrence. As we did not achieve 100% compliance this was recorded in line with the NESPF Breaches of Law Policy but not reported to the Pensions Regulator.

There were no significant governance issues during the year however the Governance Team carried out and were involved in several projects which included contributing to the Governance Framework review within Aberdeen City Council, reviewing and implementing policy documents and monitoring ongoing compliance with the LGPS (Scotland) and the Pensions Regulator requirements.

General Data Protection Regulation

The General Data Protection Regulation (GDPR) came into force on 25 May 2018 and replaced the EU 1995 Data Protection Directive and 1998 Data Protection Act in the UK.

To prepare for change the Technical Team chaired a project group that had representatives from all teams within the NESPF. A data gathering exercise was carried out to identify all areas that would be affected, and all documentation and contracts were reviewed. The NESPF arranged to meet with other Scottish funds and our software provider to discuss required system developments which were delivered at the start of 2018 making us ready for GDPR.

Guaranteed Minimum Pension Reconciliation

With contracting out ending on 6 April 2016, Her Majesty's Revenue and Customs (HMRC) provided a Scheme Reconciliation Service to assist pension funds with reconciling members guaranteed minimum pension (GMP) values held on their systems with the values held on the pension administration system. To date NESPF has reconciled more than 13,000 deferred and pensioner members and more than 9,000 active members and is on course to complete the exercise by December 2018.

Testing Working Party

The NESPF continues to be actively involved in the national Testing Working Party (TWP) for software releases from our supplier. During 2017/18 there were two releases and we participated in both along with 5 other LGPS funds. The benefits of receiving early releases, which included the development for reporting transactional data from 1 April 2018 and being GDPR compliant for 25 May 2018, ensures our readiness for change and makes the many hours of testing worthwhile.

Actuarial Valuation

As required by the LGPS (Scotland) Regulations 2014 the Fund commissioned the scheme actuary, Mercer, to carry out the triennial valuation as at 31 March 2017 for both the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund. The valuation exercise is carried out to determine the overall funding level(s) as well as determine the individual contribution rates for all participating employers within both Funds.

The exercise started in early 2017 to determine the methodology and assumptions that were to be applied by the scheme actuary for the calculation of the liabilities. The process to gather and reconcile member data, extract the data and carryout the calculations meant that the proposed employer contribution requirements were provided by the actuary by September 2017. This allowed the Employer Relationship Team (ERT) to begin the process of communicating these requirements with the individual employers through a full employer consultation. This included discussions on the appropriateness of the assumptions used by the actuary, affordability and the potential impact of changes to the admission agreements.

The valuation certificate was signed off by the scheme actuary in March 2018 following the completion of the consultation process, reaching an agreement on the contribution rates for each employer and approval from the Pensions Committee. The valuation reports detailing the funding levels and the finalised rates were issued to all employers and published on the NESPF website following the completion of the actuarial process.

Pension Administration Strategy

In January 2017 our Pension Administration Strategy (PAS) was revised to incorporate the new LGPS regulations introduced from 1 April 2015. The revised PAS was introduced from 1 April 2017 and continues to focus on NESPF processing against key performance measurements and the quantity and quality of monthly data provision from employers.

NESPF processing performance

Key performance measurements	Target	2016/17	Amount	Achieved	2017/18
Letter notifying death in service to dependent	5 days	84%	40	33	83%
Letter notifying retirement estimate	10 days	98%	915	895	98%
Letter notifying actual retirement benefits	10 days	97%	1,596	1,550	97%
Letter notifying deferred benefits	10 days	79%	1,174	1,094	93%
Letter notifying amount of refund	10 days	79%	1,427	1,323	93%
Letter detailing transfer in quotes	10 days	91%	133	118	89%
Letter detailing transfer out quotes	10 days	97%	471	459	98%

2017/18 saw a strong processing performance by the Benefits Team which was achieved by introducing specialisation and leavers being managed by the Employer Relationship Team. This contributed to the significant percentage increases for both deferred and refund processing.

Retirement processing percentage remained high at 97% despite having to process over 200 more cases than ever before because of Voluntary Severance/Early Retirement undertaken by employers.

With the introduction of freedom and choice there was also a significant increase in requests for transfer out information however performance slightly increased as staff were able to target these more efficiently through group working.

Employer data provision

The NESPF identified the need for receiving monthly information from employers in 2014. Since then the secure i-Connect portal has been rolled out to participating employers with the smaller employers using the online returns version of the system from April 2017. The NESPF now receives, processes and reconciles monthly data files from 52 of the 55 participating employers with 2 employers currently testing monthly submissions.

The NESPF has experienced many benefits of monthly data provision. Efficiencies and savings have been made in the year end process, provision of information for the actuarial valuation and benefits processing. In addition, the quality of the data held by the NESPF on the member records is very high resulting in more accurate calculations and a greater confidence in the actuarial results.

Updates from I-Connect	2015/16	2016/17	2017/18
Starters	4,355	4,029	4,415
Amendments	33,464	12,430	30,314
Leavers	3,416	3,256	3,345
Contributions (employee, employer and additional)	260,665	184,205	261,380
Salary	148,677	178,650	259,913
CARE pay	231,866	176,274	251,773
	682,443	**558,844**	**811,140**

Data received from employers is monitored and classed as being of high, medium or low quality depending on amount of event updates successfully processed and validated by the Employer Relationship Team (ERT). All data submissions received in 2017/18 were of a high quality.

It is essential that data is received from employers in a timely manner to ensure that it can be reconciled against the payment of contributions being received by the NESPF. The vast majority of data for 2017/18 was uploaded by employers in advance of the deadline of the 19th of the month following the deduction of contributions from the member. Any late uploads are monitored by the ERT who are working with employers to ensure the provision of data is carried out in a timely and consistent manner.

The success of receiving monthly data has resulted in several requests for us to share our experiences. In 2017/18 Strathclyde Pension Fund and Health and Social Care – Northern Ireland visited the ERT and conference calls were held with Buckinghamshire County Council and Plumbing Pensions UK.

Employer discretions

Under Regulation 58 of the LGPS (Scotland) Regulations 2014 employers must have a policy on the discretionary regulations. These policies must be published to allow members to access the information and a copy of policies held must be provided to the NESPF. As at 31 March 2018 the NESPF holds copies of discretions policies for 85% of the participating employers.

Communications

Following the development of the Funds' member self-service website, My Pension, 2017/18 saw the NESPF continue to promote and develop the service, with over 12,300 members registered at 31 March of 2018. Plans were also put in place for My Pension to accommodate the 2018 Deferred Benefit Statement as it moves to become an online only document.

A restructure of the NESPF website was also completed to ensure ease and efficiency for members when seeking information. The website was split into main areas including – Active, Deferred, Pensioners, and Thinking of Joining resulting in specific information for each member group being promptly accessible.

The NESPF also continued to monitor customer satisfaction levels, utilising surveys to gauge opinion. Results illustrated over 80% of new members either agreed or strongly agreed they were satisfied with the service provided by the Fund with 85% of pensioners also stating they were satisfied with the Fund's service.

A particularly notable achievement for the NESPF in 2017 was winning the Public Sector Scheme of the Year award at the Professional Pensions Pension Scheme of the Year Awards.

Investment and Accounting

The Investment and Accounting Teams are responsible for the financial management of the Pension Funds, including the delivery of investment strategies; to receive monies in respect of contributions, transfer values and investment income; to carry out the Funds' investment business; and to account for the Funds' assets and all monies received and paid from the Funds.

The Accounting Team gives support across the Funds to ensure accurate and timely data. In 2017/18, the Team continues to hold high level discussions with the Management Team on cost awareness. The first phase of financial coding simplification has been successfully completed with a view to reducing the number of cost centres and improving data accuracy.

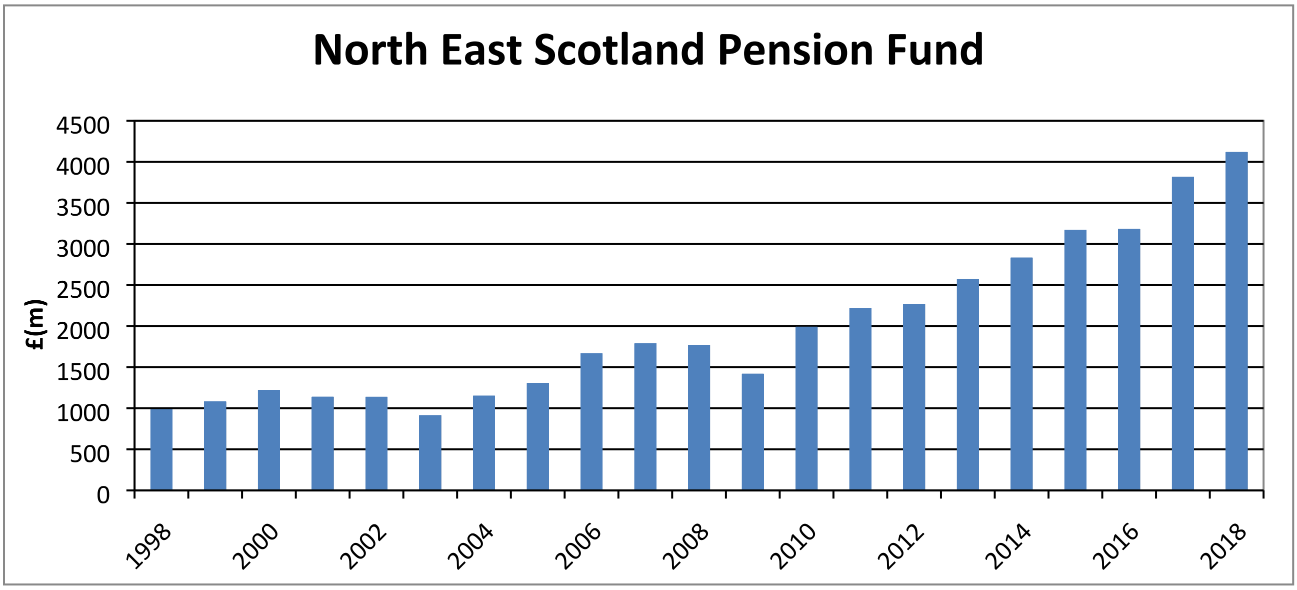
5. Financial Performance

North East Scotland Pension Fund Financial Summary

	2013/14 £000	2014/15 £000	2015/16 £000	2016/17 £000	2017/18 £000
Contributions Less benefits and expenses paid **Net additions/ (deductions)***	**(14,958)**	**(12,357)**	**(13,485)**	**(15,456)**	**(18,219)**
Net investment income Change in Market Value **Net return on Investment**	**278,513**	**350,131**	**23,929**	**648,411**	**329,035**
Net increase in Fund	**263,555**	**337,774**	**10,444**	**632,955**	**310,816**
Fund Balance as at 31 March (Market Value)	**2,833,575**	**3,171,349**	**3,181,793**	**3,814,748**	**4,125,564**

Net Additions/(deductions)* - From 2013/14 onwards 'Management Expenses' are included within this figure resulting in a negative position.

Fund balance as at 31 March 2018 (£m)



North East Scotland Pension Fund's achievements in 2017/18:

+2.1%

£29.5m
Total member contributions
£28.9m in 16/17

+6.4%

£138m
Total income in respect of members
£129.7m in 16/17

£52.8m
Total investment income
£49.8m in 16/17

+7.6%

£156.3m
Total expenditure
£145.2m in 16/17

-53.8%

£276.3m
Total profit & loss & change in market value of investments
£598.6m in 16/17

-50.9%

£310.8m
Rise in the value of the Fund
£633m in 16/17

The Aberdeen City Council Transport Fund's achievements in 2017/18:

-13%

£100k
Total member contributions
£115k in 16/17

-4%

£2.4m
Total income in respect of members
£2.5m in 16/17

-46.7%

£0.8m
Total investment income
£1.5m in 16/17

+18.6%

£5.1m
Total expenditure
£4.3m in 16/17

-85.6%

£2m
Total profit & loss & change in market value of investments
£13.9m in 16/17

-99.3%

£0.1m
Rise in the value of the Fund
£13.7m in 16/17

North East Scotland Pension Fund (2017/18)

+6.4%

£138m
Contributions receivable
£129.7m in 16/17

+6.6%

£135.1m
Benefits payable
£126.7m in 16/17

£21.2m
Management expenses
£18.5m in 16/17

-49.3%

£329m
Net return on investments
£648.4m in 16/17

+8.2%

£4,125.6m
Net assets of Fund at end of year
£3,814.7m in 16/17

Aberdeen City Council Transport Fund (2017/18)

-4%

£2.4m
Contributions receivable
£2.5m in 16/17

+2.5%

£4.1m
Benefits payable
£4m in 16/17

+304.5%

£991k
Management expenses
£245k in 16/17

-81.9%

£2.8m
Net return on investments
£15.5m in 16/17

+0.1%

£100.1m
Net assets of Fund at end of year
£100m in 16/17

The monies belonging to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund are managed entirely by appointed investment fund managers and are held separate from any of the employing bodies which participate in the North East Scotland Pension Funds. The only exception to this is a small investment in Aberdeen City Council's Loan Fund, which varies year on year, and represents surplus cash from contributions not yet transferred to the fund managers.

After meeting the cost of current benefits, all surplus cash is invested and the increasing value of investment is then available to meet future liabilities to employees within the Funds. In addition to a contingent liability to meet future pension benefits payable to existing employees, the Funds must also provide for the future payment of deferred pension benefits which have been preserved by former employees in respect of service prior to their leaving.

Membership Statistics

NESPF	**2013/14**	**2014/15**	**2015/16**	**2016/17**	**2017/18**
Active	22,880	24,089	24,546	25,329	25,568
Pensioners	17,106	17,726	18,328	19,111	20,023
Deferred	17,267	17,759	18,455	19,120	19,653

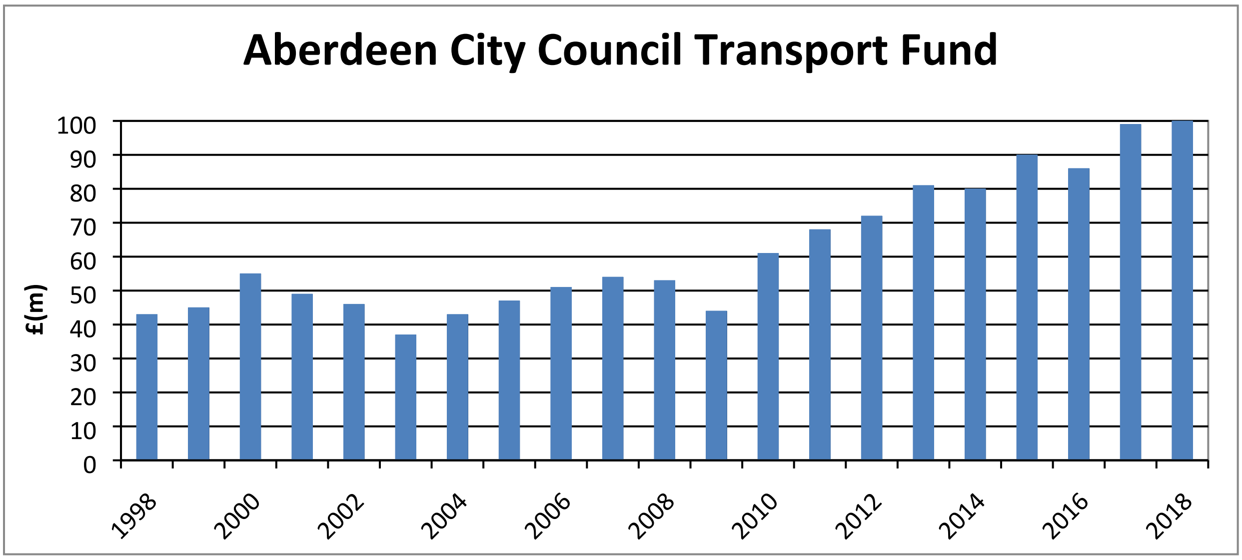
Active membership has continued to rise steadily over a 5 year period, with factors such as auto enrolment and Fund promotion positively impacting membership. Pensioner numbers continue to rise because of several potential factors such as an accelerated trend in longevity seen in recent years.

Aberdeen City Council Transport Fund Financial Summary

	2013/14 £000	2014/15 £000	2015/16 £000	2016/17 £000	2017/18 £000
Contributions Less benefits and expenses paid **Net additions/ (deductions)***	**(1,033)**	**(762)**	**(1,347)**	**(1,731)**	**(2,669)**
Net investment income Change in Market Value **Net return on Investment**	**137**	**10,564**	**(2,050)**	**15,454**	**2,774**
Net increase in Fund	**(896)**	**9,802**	**(3,397)**	**13,723**	**105**
Fund Balance as at 31 March (Market Value)	**79,838**	**89,640**	**86,243**	**99,966**	**100,071**

Net Additions/(deductions)* - From 2013/14 onwards 'Management Expenses' are included within this figure resulting in a negative position. In addition, the ACC Transport Fund is a closed fund which means a reducing balance of active members contributing toward the Scheme.

Fund balance as at 31 March 2018 (£m)



Membership Statistics

Transport Fund	2013/14	2014/15	2015/16	2016/17	2017/18
Active	85	78	71	61	48
Pensioners	405	403	411	423	434
Deferred	155	150	142	130	123

Active and deferred membership numbers for the Transport Fund have reduced over a 5 year period due to the closed nature of the Fund resulting in more members moving to a pensioner status.

Remuneration Report
There is no need to produce a remuneration report for the Pension Funds as the Funds do not directly employ any staff. All staff are employed by Aberdeen City Council and their costs reimbursed by the Pension Funds. The councillors who are members of the Pensions Committee and the Pension Board are also remunerated by the Council.

Key management personnel for the Funds are explained in the North East Scotland Pension Fund and the Transport Fund annual accounts. Full details of councillor and senior employee remuneration can be found in the Remuneration Report in Aberdeen City Council's financial statements.

6. Economic and Market Background

Major equity and bond markets saw positive returns over the last 12 months. While it may seem that there were many events which could have upset the apple cart – the stalemate of Brexit negotiations; the rise of political populism; the unpredictability of President Trump; the threat of North Korea and unrest in the Middle East – nothing succeeded in doing so. Ultimately, the only thing that mattered was the continued optimistic sentiment around the global economy.

However, we have witnessed a change in direction for monetary policy with the Bank of England raising rates for the first time in a decade and the European Central Bank announcing its intention to begin reducing its monetary stimulus programme this year. As we entered 2018, the concerns surrounding the potential impacts of interest rates rises, coupled with global trade tensions and whether high returns and high valuations were sustainable, began to weigh on sentiment. As a result, we've seen a return of volatility.

US:
As 2017 drew to a close, Trump's tax reform bill was squeezed through the Senate. It represents the most drastic changes to the US tax code for more than 30 years, slashing corporate tax rates and provided an immediate boost to corporate profits and the US market performance. However, as we entered 2018 the market began to worry about risks of further overheating of an economy that was already running with full employment and emerging signs of wage inflation. The origin of the latest bout of volatility can probably be traced back to the release of US wage data early in February, which indicated that wage inflation had taken hold and overall inflation would follow. As a result, we saw volatility in the US market and slightly more muted 12-month performance of +1.3%.

UK:
UK stock market returns, while strong, have been relatively muted when compared to most major markets globally. Possible reasons include the strength of sterling this year, at least when compared to the US dollar. Additionally, there is some ongoing uncertainty around the Brexit negotiations and the still unknowable implications for the UK economy and corporate sector.

Europe:
In Europe, there has been plenty to discuss in the political sphere. Merkel has secured another term as German chancellor, which is perhaps key for that market and the stability of the core Eurozone. In France, it is still early days for Macron, but there are signs that he is having some success at home and on the European stage. On the other hand, in southern Europe, the recovery is still weak. Youth unemployment, for example, remains both depressingly and stubbornly high. However, Europe is looking better than in recent years – it is now growing at its fastest rate in a decade, industrial production has picked up and consumer confidence has risen. European markets continue to perform strongly on the back of upbeat economic outlook, rising 4.3%.

Japan:
Japan continues to enjoy its longest period of economic expansion since the 1980s. At

the turn of the year, its economy grew by 1.6%, as a result of stronger than projected corporate capex. Unemployment continues to trend down. Corporate profits are also growing strongly and, based on company forecasts for the year to end March, aggregate return on equity for listed Japanese companies will reach double digits for the first time. In stock market terms, the Japanese market has been strong, up 7.5% in dollar terms as the yen strengthened against the dollar.

Emerging Markets:
US tariffs on China and US sanctions on Russia have raised market uncertainty and volatility but have had limited impact on economic fundamentals or on corporate profitability among Emerging Market companies.

A number of commodity exporting countries have been through sharp corrections from which they are now recovering. The likes of Brazil, Russia and Indonesia have seen inflation subside, allowing aggressive interest rate cuts, which should kick off a new credit cycle as non-performing loans and provisions subside and loan growth returns. Banks in these countries have been trading at low valuations but should see earnings accelerate and valuations re-rate once the inflection point in the credit cycle is reached.

Bonds:
Government bond yields ended the period slightly higher than where they started but were volatile over the period. The emergency interest rate cut made by the Bank of England following the EU membership referendum was reversed in November, taking the bank rate to 0.5%. The Bank of England expects to continue to raise interest rates barring unexpected economic or political events. The markets are monitoring developments in the Brexit negotiations warily. Inflation moderated over the period but, at 2.7%, remains slightly above the Bank's target. President Trump's tax cuts in the US, along with high employment levels, have raised fears of inflationary overheating.

Corporate profitability remains at high levels. Default rates on riskier companies have been below average. Corporate bond yield spreads – the additional yield over government bonds to compensate for credit risk – fell very slightly. Higher income from investment grade bonds meant that they performed marginally better than equivalent gilts at 0.6%.

There have been indications recently of growing nervousness in financial markets. Major central banks are likely to decrease the amount of bonds held on their balance sheets, reversing the positive boost to global bond prices this had been giving. It is likely that government bond returns will be poor and corporate bond markets must adjust to tighter monetary conditions.

Property:
Over the 12 months to March 2018, according to the IPD Monthly Index property recorded a total return of 11.3%. This was similar to the 11.8% recorded over the previous 12 month period. Capital values rose by 5.6% in the year to March 2018, derived mostly from a fall in yields, with rental value growth of only 2%.

The retail sector was once again the weakest of the main sectors over the 12 months to March 2018, according to IPD, recording a total return of 7.1%. While this was not dramatically lower than the 8.6% delivered by offices, industrials hugely outperformed the wider market once again, recording a total return of 21.6% over the period. While capital values only rose by 1% in the retail sector, its income return of 6% was considerably higher than the other sectors. Capital growth in offices was 3.6% for the year to March, split relatively evenly between rental value growth (1.6%) and yield impact (2%). Industrials, while seeing very strong rental value growth of 4.9% over the period, derived the majority of its 15.5% capital growth from the impact of yields falling as a result of keen investor demand.

Market Returns	**1 Year (%)**	**3 Years (% p.a.)**	**5 Years (% p.a.)**
Equities:-			
FTSE All Share Index	1.3	5.9	6.6
FTSE All World Index	2.9	10.9	11.6
FTSE All World ex UK	3.1	11.2	12.1
FTSE North American Index	1.3	12.3	14.4
FTSE Europe (ex UK) Index	4.3	8.5	10.0
FTSE Japan Index	7.5	11.4	11.6
FTSE Developed Asia (ex Japan) Index	1.9	9.8	6.5
FTSE Emerging Markets Index	8.8	10.4	6.9
Bonds:-			
FTA Government Securities All Stocks	0.5	3.4	4.2
ML UK Corporate Bonds	1.3	3.6	5.1
FTA Index Linked All Stocks	0.7	7.8	7.7
Above are total returns in Sterling Source: Thomson Reuters and FTSE			

7. NESPF Investment Strategy

The NESPF's investment strategy is one of diversified investment, which means that investments are spread across different investment asset types and different countries, sectors and companies, in order to reduce the overall risk.

Equity benchmarks are designed to encourage diversification of the equity mix. There are a range of fund managers to again spread risk, each with clear and documented agreements in place detailing their investment mandates. The Funds also employ an independent Global Custodian.

The objective of the investment strategy is to deliver long term returns which are greater than the growth in expenditure to be paid out in pensions. The investment strategy has been monitored on an ongoing basis by the Pensions Committee, focusing on long term policies with consideration given to short tactical strategies.

The suitability of particular investments and types of investments are detailed in the Statement of Investment Principles.

The Funds take proper advice at reasonable intervals regarding their investments, through their advisors to the Pensions Committee.

Asset Structure 2017/18

Asset Class	Distribution as at 31 March 2017		Distribution as at 31 March 2018	
	Fund Actual %	Fund Benchmark %	Fund Actual %	Fund Benchmark %
Equities (including Alternative Assets)	79.4	70.0	76.8	57.5
Bonds / Credit	12.4	15.0	11.4	20.00
Property / Infrastructure	7.1	10.0	10.0	20.00
Cash / Other	1.1	5.0	1.8	2.5
Total	**100.0**	**100.0**	**100.0**	**100.0**

During the year a revised Investment Strategy was put in place for the North East Scotland Pension Fund and this is set out in the Statement of Investment Principles as follows:

Equities	45.0% (range +/- 5%)
Alternative Assets (including private equity)	12.5% (range +/- 5%)
Bonds / Credit	20.0% (range +/- 5%)
Property / Infrastructure	20.0% (range +/- 5%)
Cash / Other	2.5% (range +/- 5%)

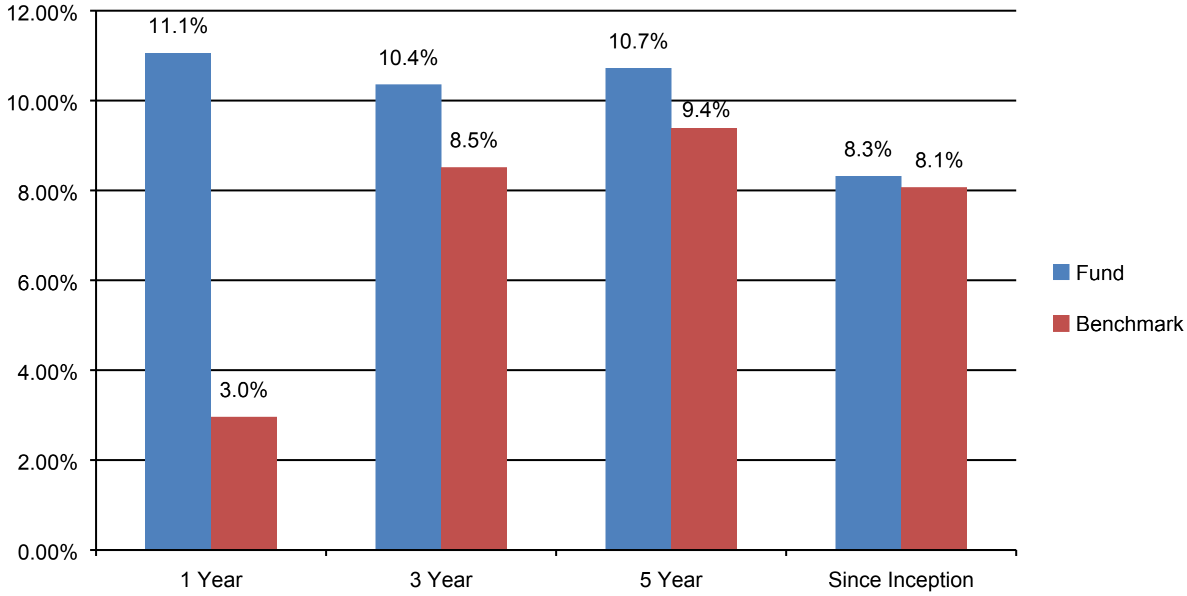
The NESPF continues to rebalance assets in line with its revised investment strategy, aiming to de-risk by reducing exposure to equities and increasing infrastructure, alternatives and credit opportunities.

North East Scotland Pension Fund Performance

2017/18 was a great year for investment returns with equities in particular posting strong positive performance. The strong one year numbers versus the benchmark are attributable to the active managers excelling in particular.

Longer term over all periods the Fund has also outperformed the benchmark returns and longer term comparators such as CPI and Average Earnings. This provides assurance that the Fund's Investment Strategy will continue to deliver the required returns over the longer term.

The graph below shows the Fund's performance over the short, medium and long term against the Fund's customised benchmark.



Whilst employee contribution rates and benefits payable are set by statute, the long-term liabilities of the Fund are linked either to wage inflation or to price inflation. It is the Fund's performance against these benchmarks that affect the long-term employer contribution rate, which is variable. **Over the longer term, performance of the Fund remains ahead of both Average Earnings and CPI.**

Year Ending	2015/16 %	2016/17 %	2017/18 %	Since inception Annualised %
CPI*	0.5	2.3	2.5	2.6
Average Earning*	1.9	2.4	2.6	2.9
NESPF Return	0.7	20.0	11.1	8.3

*Source: Office of National Statistics

Investment Management Structure

The investment management structure is contained within Note 11: “Investments Analysed by Fund Manager” within the NESPF accounts and within Note 9 of the ACC Transport Fund accounts.

8. ACCTF De-Risking Strategy and Performance

With effect from 1 April 2015 the Administering Authority and the scheme employer agreed a revised investment strategy for the Transport Fund – 'a de-risking or "flightpath" strategy'. That is to say, the performance of the Fund will no longer be measured against a benchmark of global equities and bonds but rather against its funding target of 100%.

The aim of the strategy is to reach the funding requirement of 100% funding in a manner that reduces both interest and inflation risk exposure. The strategy consists of a portfolio of growth assets to achieve the 100% funding target and portfolio of matching assets to meet current liabilities.

The aim of the flightpath is to "lock in" improvements in funding by switching from growth to defensive or matching assets. The de-risking plan is to be reviewed triennially in line with the triennial actuarial valuation and is structured to keep contributions as stable as possible.

The flightpath continues to move in a favourable direction, providing the Fund the opportunity to de-risk. As of March 2017, the funding level was 94% and continues to rise in line with the flightpath.

This year's administration report focuses on statement compliance, GDPR, GMP reconciliation, TWP, actuarial valuation and the pension administration strategy.

Statement Compliance

The biggest administrative challenge for the NESPF continues to be the requirement to issue benefit statements to all active members by the 31 August. In total 24,409 statements were issued to active members prior to the deadline which represented 99.76% compliance. We were able to identify the outstanding members to allow us to rectify the data issues on the administration system and prevent future reoccurrence. As we did not achieve 100% compliance this was recorded in line with the NESPF Breaches of Law Policy but not reported to the Pensions Regulator.

There were no significant governance issues during the year however the Governance Team carried out and were involved in several projects which included contributing to the Governance Framework review within Aberdeen City Council, reviewing and implementing policy documents and monitoring ongoing compliance with the LGPS (Scotland) and the Pensions Regulator requirements.

GDPR

The General Data Protection Regulation (GDPR) comes into force on 25 May 2018 and replaces the EU 1995 Data Protection Directive and 1998 Data Protection Act in the UK.

To prepare for change the Technical Team chaired a project group that had representatives from all teams within the Fund. A data gathering exercise was carried out to identify all areas that would be affected, and all documentation and contracts were reviewed. The NESPF arranged to meet with other Scottish funds and our software provider to discuss required system developments which were delivered at the start of 2018 making us ready for GDPR.

GMP Reconciliation

With contracting out ending on 6 April 2016 HMRC provided a Scheme Reconciliation Service to assist pension funds with reconciling members guaranteed minimum pension (GMP) values held on their systems with the values held on the pension administration system. To date NESPF have reconciled more than 13,000 deferred and pensioner members and more than 9,000 active members and are on course to complete the exercise by December 2018.

Testing Working Party

NESPF continue to be actively involved in the national Testing Working Party (TWP) for software releases from our supplier. During 2017/18 there were two releases and we participated in both along with 5 other LGPS funds. The benefits of receiving early releases, which included development for reporting transactional data from 1 April 2018 and GDPR compliant for 25 May 2018, ensures we ready for change and makes the many hours of testing worthwhile.

Actuarial Valuation

As required by the LGPS (Scotland) Regulations 2014 the Fund commissioned the scheme actuary, Mercer, to carry out the triennial valuation as at 31 March 2017 for both the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund. The valuation exercise is carried out to determine the overall funding level(s) as well as determine the individual contribution rates for all participating employers within the main Fund.

The exercise started in early 2017 to determine the methodology and assumptions that were to be applied by the scheme actuary for the calculation of the liabilities. The process to gather and reconcile member data, extract the data and carryout the calculations meant that the proposed employer contribution requirements were provided by the actuary by September 2017. This allowed the Employer Relationship Team (ERT) to begin the process of communication and discussing these requirement with the individual employers through a full employer consultation. This included discussions on the appropriateness of the assumptions used by the actuary, affordability and the potential impact of changes to the admission agreements.

The valuation certificate was signed off by the scheme actuary in March 2018 following the completion of the consultation process, reaching an agreement on the contribution rates for each employer and approval form the Pensions Committee. The valuation reports detailing the funding levels and the finalised rates was issued to all employers and published on the Pension Fund website following the completion of the actuarial process.

Pension Administration Strategy

In January 2017 our Pension Administration Strategy (PAS) was revised to incorporate the new LGPS regulations introduced from 1 April 2015. The revised PAS was introduced from 1 April 2017 and continues to focus on NESPF processing against key performance measurements and the quantity and quality of monthly data provision from employers.

NESPF processing performance

Key performance measurements	Target	2016/17	Amount	Achieved	2017/18
Letter notifying death in service to dependent	5 days	84%	40	33	83%
Letter notifying retirement estimate	10 days	98%	915	895	98%
Letter notifying actual retirement benefits	10 days	97%	1596	1550	97%
Letter notifying deferred benefits	10 days	79%	1174	1094	93%
Letter notifying amount of refund	10 days	79%	1427	1323	93%
Letter detailing transfer in quotes	10 days	91%	133	118	89%
Letter detailing transfer out quotes	10 days	97%	471	459	98%

2017/18 saw a strong processing performance by the Benefits Team which was achieved by introducing specialisation and leavers being managed by the Employer Relationship Team. This contributed to the significant percentage increases for both deferred and refund processing.

Retirement processing percentage remained high at 97% despite having to process more than 200 more cases than ever before because of Voluntary Severance/Early Retirement undertaken by employers.

With the introduction of freedom and choice there was also a significant increase in requests for transfer out information however performance slightly increased as staff were able to target these more efficiently through group working.

Employer data provision

The NESPF identified the need for receiving monthly information from employers in 2014. Since then the secure i-Connect portal has been rolled out to participating employers with the smaller employers using the online returns version of the system from April 2017. NESPF now receive, process and reconcile monthly data files from 53 of the 57 participating employers with 2 employers currently testing monthly submissions.

The Fund has experienced many benefits of monthly data provision. Efficiencies and savings have been made in the year end process, provision of information for the actuarial valuation and benefits processing. In addition, the quality of the data held by the Fund on the member records is very high resulting in more accurate calculations and a greater confidence in the actuarial results.

Updates from I-Connect	**2015/16**	**2016/17**	**2017/18**
Starters	4,355	4,029	4,175
Amendments	33,464	12,430	27,826
Leavers	3,416	3,256	3,198
Contributions (employee, employer and additional)	260,665	184,205	249,347
Salary	148,677	178,650	253,576
CARE pay	231,866	176,274	249,255
	682,443	**558,844**	**787,377**

Data received from employers is monitored and classed as being of high, medium or low quality depending on amount of event updates successfully processed and validated by the Employer Relationship Team (ERT). All data submissions received in 2017/18 were of a high quality.

It is essential that data is received from employers in a timely manner to ensure that it can be reconciled against the payment of contributions being received by the Fund. The vast majority of data for 2017/18 was uploaded by employers in advance of the deadline of the 19th of the month following the deduction of contributions from the member. Any late uploads are monitored by the ERT who are working with employers to ensure the provision of data is carried out in a timely and consistent manner.

The success of receiving monthly data has resulted in several requests for us to share our experiences. In 2017/18 Strathclyde Pension Fund and HSC – Northern Ireland visited the ERT and conference calls were held with Buckinghamshire County Council and Plumbing Pensions UK.

Employer discretions

Under Regulation 58 of the LGPS (Administration) (Scotland) Regulations 2014 employers must have a policy on the discretionary regulations. These policies must be published to allow members to access the information and a copy of policies held must be provided to the Pension Fund. As at 31 March 2018 the NESPF hold copies of discretions policies for 85% of the participating employers.

9. Risk

A key element to risk management is the structured delegation of powers from the Council to the Pensions Committee and then to senior officers. To complement the delegation to senior managers, there is an extensive and detailed accountability back to Committee on how these delegations have been exercised. Full details of the structure of delegated powers are contained in the Pension Fund Governance Statement.

Investment risk is recognised as falling into distinct areas: manager skill (alpha) and market risk (beta).The structure of the investment strategy reflects this and is designed with the support of external expert advice. Details are contained in the Statement of Investment Principles and the Funding Strategy Statement.

The operational management of investment risk forms the basis of quarterly reporting to the Pensions Committee and Pension Board.

The Funds' approach to risk is dynamic and can be revised in response to short term market events.

Benefits risk is recognised as falling into distinct areas: operational risk (regulation compliance and staffing) and Information Technology (IT) risks. The risks associated with the operational payment of benefits and recording of pensioner records produces a complex set of risks, which are mitigated with the use of a dedicated pension fund administration system that is thoroughly and regularly tested, combined with the technical hierarchy checking of output by pension staff. IT risk is mitigated through the use of an externally hosted benefit administration system subject to regular update and review.

It is recognised that all NESPF services are very dependent upon third party contracts ranging from IT through to investment managers. All are subject to regular review and monitoring.

Risk Management

Risk management is an on-going process with quarterly reporting provided to the Pensions Committee. These reports detail the progress achieved in the implementation of the action plan, the ongoing review of the Risk Register and reporting of new risks that have been identified.

The full Register is available on the website www.nespf.org.uk.

10. Funding Strategy Statement

The Local Government Pension Scheme (Administration) (Scotland) Regulations 2008 and its subsequent amendments require administering authorities to prepare, maintain and publish a written Funding Strategy Statement (FSS).

The FSS sets out how the administering authority balances the potentially conflicting aims of affordability of contributions, transparency of process, stability of employers' contributions, and prudence in the funding basis.

As part of the 2017 actuarial valuation exercise, the Funding Strategy Statement was reviewed, providing a statement that was prepared by Aberdeen City Council (the Administering Authority) to set out the funding strategy for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund (the Funds), in accordance with Regulation 56 of the Local Government Pension Scheme (Scotland) Regulations 2014 (as amended) and the guidance papers issued in March 2004 by the Chartered Institute of Public Finance and Accountancy (CIPFA) Pensions Panel.

Copies of the full statements are available on the website www.nespf.org.uk.

11. Statement of Investment Principles

This statement sets out the principles governing decisions about investments for the North East Scotland Pension Fund and Aberdeen City Council Transport Fund.

All investment decisions are governed by The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010.

The Funds' objective is to meet the benefit liabilities as they fall due at a reasonable cost to the participating employers, given that employee contributions are fixed. Reasonable, in this context, refers to both the absolute level of contribution – normally expressed as a percentage of pensionable payroll – and its predictability. The employer contribution rates are impacted by both the assessed level of funding – ratio of the value of assets to liabilities – and the assumptions underlying the actuarial valuation.

The Funds target a 100% funding level. 'Growth' assets, such as equities, are expected to give a higher long-term return than 'liability-matching' assets, such as bonds. The benefit of higher investment returns is that, over the long-term, a higher level of funding should achieve lower employer contribution rates. However, the additional investment returns from growth assets come with a price: greater volatility relative to the liabilities, thus introducing risk. The risk is evidenced by the potential volatility of both the funding level and the employer contribution rate. There is therefore a trade-off between the additional investment return from greater exposure to growth assets and its benefits - higher funding level, lower employer contribution level - and the benefits of greater predictability - of both funding level and employer contribution rate - from having greater exposure to liability matching assets.

The trade-off, and its consequences on both funding level and employer contribution level, were examined by the Pensions Committee and led to the strategic benchmarks.

The full statement is available on the website www.nespf.org.uk.

12. Corporate, Environmental and Social Governance

The North East Scotland Pension Funds support the view that the willingness and ability of a company to adopt the highest standards of corporate responsibility is increasingly important to its long-term growth.

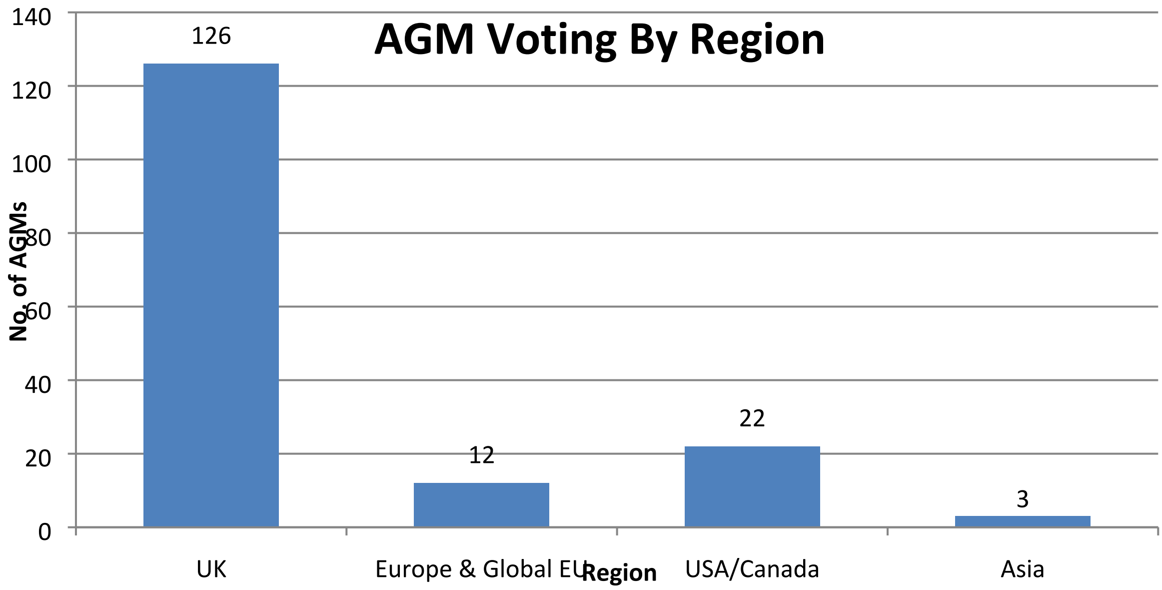
Good corporate governance and good social and environmental practice can have a favourable effect on financial performance and improve investment returns to shareholders as well as society at large.

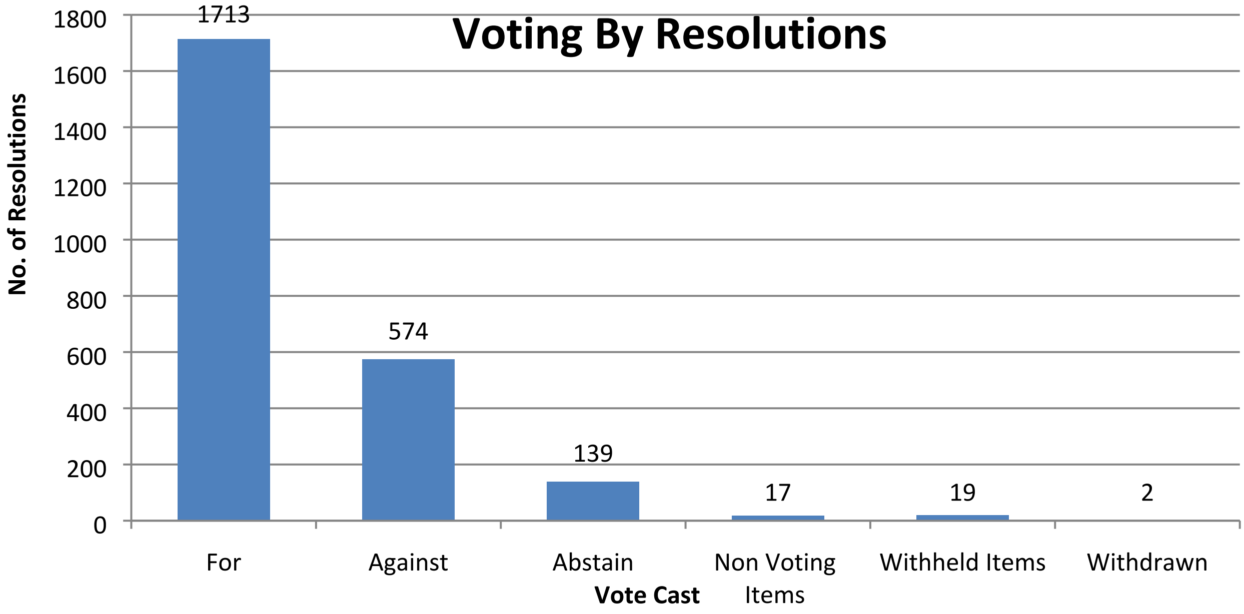
The below gives a snap shot of the activities that the NESPF has undertaken over the past year.

Voting

Voting is an integral part of good governance; it gives the NESPF a direct route to influence the company's management. The NESPF votes in-house for all our Active Managers and over the last year has voted at 163 Annual General Meetings/Special meetings on 2,464 resolutions. The Funds' voting advice is provided by P.I.R.C (Pensions & Investments Research Consultants Ltd). Additional advice is also received from the Local Authority Pension Fund Forum

Further information on the Funds' Voting record can be found on our website http://www.nespf.org.uk/TheFund/Investment/ResponsibleInvestment/Fund_Voting.aspx





During the last financial year, the main reasons for casting a vote 'Against' a company we invest in are given below:

Annual Reports

- Vote on Dividend or Dividend Policy not put to shareholders which is contrary to best practice.

Share Issues/Re-purchase

- No clear justification for the Re-purchase put forward by the Board

Auditors Appointment

- Not rotating Audit Firms on a regular basis
- Concerns about high levels of non-audit fees creating the potential for conflicts of interest.

Executive Pay Schemes

- Potential Executive Pay deemed to be excessive

Engagement

Local Authority Pension Fund Forum (LAPFF)

LAPFF is the UK's leading collaborative shareholder engagement group with combined assets of over £200 billion and brings together over 75 local authority pension funds. The Forum provides a unique opportunity for Britain's local authority pension funds to discuss shareholder engagement and investment issues. The Lord Provost Barney Crockett who sits on the Pensions Committee is a member of the LAPFF executive committee.

Some examples of the engagement work undertaken by the Funds through LAPFF are noted below.

<u>Environmental</u>

Shareholder Resolution Support
In what turned out to be landmark victories for shareholders on climate change disclosure, LAPFF issued voting alerts recommending members support shareholder resolutions at PPL, Chevron and Exxon Mobil. The resolutions sought to require the companies to undertake analysis and produce publicly-available reports on the impact that a two-degree scenario, as outlined in the Paris Agreement, would have on their business and shareholder value. The resolutions at Exxon, the world’s largest oil and gas company, and PPL both received majority backing of shareholders.

<u>Social Risk</u>

Human Rights
Historically, much of LAPFF’s engagement around human rights has been through the lens of employment standards. This approach continues to be the case to a large extent with companies such as Sports Direct and Ryanair.

This year, though, the range of human rights engagements seems to have increased. For example, LAPFF engaged again on the use of cluster munitions, as well as with companies operating in Israel and the settlements. LAPFF also engaged with extractives companies facing pressure from community groups over their mining practices. These engagements reflect human rights concerns on which LAPFF has engaged previously. However, LAPFF also engaged with 21st Century Fox over its sexual harassment scandal, which seems to be snowballing across the entertainment industry and has even played a role in its attempted acquisition of Sky. This development and the government’s focus on worker access to corporate boards also drives home the link between corporate governance and employment rights, highlighting the need for good human capital management, or workforce management as it is increasingly known.

<u>Governance</u>

Cyber security
Cyber security currently ranks as one of the biggest concerns for investors and company boards alike. Recent high-profile cyberattacks have highlighted the operational and reputational costs at stake. To safeguard against these threats, LAPFF has sought further detail and assurances from companies about how they are mitigating the risks posed.

The Forum had meetings with the Chairmen at BT and Vodafone to discuss cybersecurity as both companies are at the forefront of the threat given their role in the exchange of information. At this year’s Tesco AGM, LAPFF asked the chairman, in light of the cyberattack on Tesco Bank the previous year, whether the board had the right competencies to mitigate future attacks and gained a better understanding of how cyber risk is managed within the company and the training the board had received. LAPFF also asked about cyber security at the Scottish Southern Energy AGM. It appears that this issue will continue to increase in importance for investors in the coming years.

Further information of LAPFF engagements can be found at http://www.lapfforum.org

Principles for Responsible Investment (PRI)

PRI is the world's leading proponent of responsible investment with over 1,800 signatories with approx. $70 trillion of assets under management.

This is a worldwide initiative with a set of aspirational and voluntary guidelines for investment entities wishing to address environmental, social, and corporate governance (ESG) issues. The North East Scotland Pension Fund signed up to these guidelines in August 2010.

Through being members of the PRI, we have the opportunity to become involved in issues at an early stage and to effect change on a global basis.

Through the year the Fund has added its name to:

Jan 2018:	Working Practices – Re-commit to the Bangladesh Accord for Fire and Building Safety
Sep 2017:	Labour Issues – Letter to the Leather Working Group urging them to expand their remit to include Labour Standards
Jul 2017:	Climate Change – Letter from Global; Investors to Governments of the G7 and G20 Nations
Apr 2017:	Working Practices – Statement of support for new Accord for Fire and Building Safety in Bangladesh.

More information on the above can be found on our website at http://www.nespf.org.uk/TheFund/Investment/ResponsibleInvestment/ResponsibleInvesting.aspx

13. Future

During 2017/18, the Funds continued to build on technological advances with the implementation of a new online system. This facility was an extension of a system our larger employers use but was amended to cater towards the needs and capabilities of our smaller employers. With online solutions available for all employers, the Funds made monthly online submissions of data a mandatory requirement for employers from 1 April 2017.

The Funds conducted their Triennial Valuations in 2017/18 to overwhelming success. The results showed a strong improvement in the NESPF's funding position with an increase from 94% (2014) to 107%. The Transport Fund also saw a small increase with the funding position rising from 93% (2014) to 94%.

Further to the significant achievements above, the Funds will continue to transform and improve their capabilities, seeking to take advantage of ever changing technology solutions to enhance customer and staff experience.

The Funds will continue to ensure full utilisation of existing technology along with seeking new solutions to enhance service delivery.

14. Acknowledgement

The production of the Annual Report and Accounts is very much a team effort involving many staff as well as information supplied from our advisors. We would like to take this opportunity to acknowledge the considerable efforts of all staff in the production of the 2017/18 Annual Report and Accounts.

Angela Scott	**Jonathan Belford**	**Councillor M Tauqeer Malik**
Chief Executive	**Chief Officer - Finance**	**Pensions Committee Convener**

On behalf of Aberdeen City Council

14 September 2018

Statement of Responsibilities

The North East Scotland Pension Funds are governed by an Administering Authority, Aberdeen City Council, and are required to:

- Make arrangements for the proper administration of their financial affairs and to secure that the proper officer of the authority has responsibility for the administration of those affairs (section 95 of the Local Government (Scotland) Act 1973). For the North East Scotland Pension Funds, that officer is the Chief Officer - Finance for Aberdeen City Council.

- Manage their affairs to secure economic, efficient and effective use of resources and safeguard its assets.

- Ensure the Annual Accounts are prepared in accordance with legislation (The Local Authority Accounts (Scotland) Regulations 2014), and so far as is compatible with the legislation, in accordance with proper accounting practices (section 12 of the Local Government in Scotland Act 2003).

- Approve the Annual Accounts for signature.

I confirm that these Annual Accounts were approved for signature by the Pensions Committee at its meeting on 14 September 2018.

Signed on behalf of Aberdeen City Council

Councillor M Tauqeer Malik
Pensions Committee Convener

The Chief Officer - Finance responsibilities:

The Chief Officer - Finance is responsible for the preparation of the Pension Funds' Annual 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 Chief Officer - Finance has:

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

The Chief Officer - Finance has also:

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

Financial Position:

I certify that the Annual Accounts give a true and fair view of the financial position of the North East Scotland Pension Funds at the reporting date and the transactions of the Funds for the year ended 31 March 2018.

Jonathan Belford, CPFA
Aberdeen City Council, Chief Officer - Finance
Date: 14 September 2018

Annual Governance Statement

Scope of Responsibility

Aberdeen City Council has statutory responsibility for the administration of the Local Government Pension Scheme (LGPS) in the North East of Scotland, both on its own behalf and in respect of the other 2 local authorities in the area and some 50 other employers.

As the administering authority for the Pension Funds, the Council is responsible for ensuring that its business, including that of the Pension Funds, is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

In discharging this overall responsibility, the Aberdeen City Council Pensions Committee is responsible for putting in place proper arrangements for the governance of the Funds' affairs and facilitating the effective exercise of its functions, which includes arrangements for the management of risk.

The Council has approved and adopted a Local Code of Corporate Governance which is consistent with the principles of the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Society of Local Authority Chief Executives (SOLACE) Framework: Delivering Good Governance in Local Government.

Purpose of the Governance Framework for North East Scotland Pension Funds

The governance framework comprises the systems and processes and culture and values by which Aberdeen City Council as the administering authority, and therefore the Pension Funds, is directed and controlled, and its activities through which it accounts to and engages with its stakeholders. It enables the Pension Funds to monitor the achievement of their strategic objectives and to consider whether those objectives have led to the delivery of effective services.

The North East Scotland Pension Funds are governed by the Local Government Pension Scheme (Scotland) Regulations. These include requirements for the preparation and production of a number of key policy documents including a Funding Strategy Statement and Statement of Investment Principles. These documents set out the Funds' objectives together with the main risks facing the Funds and the key controls in place to mitigate those risks.

The system of internal control is a significant part of the governance framework and is designed to manage risk to a reasonable level. It cannot eliminate all risk of failure to achieve policies, aims and objectives and can therefore only provide reasonable and not absolute assurance of effectiveness.

A governance framework has been in place at Aberdeen City Council and North East Scotland Pension Funds for the year ended 31 March 2018 and up to the date of approval of the Annual Report and Accounts.

The Governance Framework

The Funds' place reliance upon the internal financial controls within the Council's financial systems and the monitoring in place to ensure the effectiveness of those controls. Within the overall control arrangements, the system of internal control is intended to ensure that assets are safeguarded, transactions are authorised and properly recorded, and material errors or irregularities are either prevented or would be detected within a timely period.

To help provide a framework of control, the Council's governance framework includes standing orders, financial regulations, financial monitoring and financial and administrative procedures (including segregation of duties, management supervision, and a system of delegation and accountability). In addition, the terms of reference for the Pensions Committee sets out its role and delegated functions.

The systems include:

- Managing receipt of contributions from employees and employers and payment of benefits to retired members of the Funds;
- Review of financial and performance reports against forecasts, benchmarks and targets set;
- The preparation of regular financial reports which include funding updates and actual expenditure against forecasts; and
- Consideration of external and internal audit reports by the Audit, Risk and Scrutiny Committee and by the Pensions Committee.

These arrangements also include:

- A training programme to ensure that Pensions Committee and Pension Board members develop the required standard of knowledge and understanding of the LGPS;
- Identifying the objectives of the Funds in the Funding Strategy Statement, Statement of Investment Principles and Service Plan. A written report covering the Pension Fund's Investment Strategy was presented to the Pensions Committee in March 2018, with quarterly updates;
- Monitoring the achievement of objectives by the Pensions Committee and senior officers;
- A systematic approach to monitoring service performance by the Pensions Committee, senior officers and stakeholders including benchmarking of services in terms of quality and cost against other Local Government Pension Scheme funds;
- A clear statement of risk, combined with effective risk management arrangements. A risk register is updated and regularly reported to the Pensions Committee;
- The Monitoring Officer reports on any non-compliance with laws and regulations of which they are made aware to the Pensions Committee in respect of the Funds;
- Operating within clearly established investment guidelines defined by the Local Government Pension Scheme Investment Regulations and the Funds' Statement of Investment Principles;

- Compliance with the CIPFA Principles for Investment Decision Making in the Local Government Pension Scheme and the Myners Principles on investment;
- Appropriate investment custody arrangements with a global custodian and access to the custodian's extensive internal control framework;
- Monitoring of appointed fund managers and third party providers ensuring compliance within their management agreements and receipt of assurances from them on the adequacy of the internal financial control systems operated by them.

The Public Service Pensions Act 2013 introduced new regulatory requirements including the introduction of a Pension Board. The Board assist the Administering Authority in delivering a regulatory compliant scheme and was implemented from the 1 April 2015. In addition, the Scheme now reports to The Pensions Regulator under the new governance arrangements. This provides additional assurances to all stakeholders that the Scheme has the appropriate internal and external governance framework in place.

From 1 April 2016, the Pension Funds have also implemented a new structure that identified six key areas; Investment, Accounting, Administration, Technical, Employer Relationship and Governance.

Teams are now in place to continue to deliver an efficient and effective service to all stakeholders while providing succession planning and clear and accountable roles.

Review of Effectiveness

The Pension Funds have a responsibility for conducting, at least annually, a review of the effectiveness of their control environment including the system of internal control.

The Pension Funds approach this with reference to the Council and its approach. This considers different layers of assurance, namely management assurance both internally through the Council and the assurance and recommendations provided by internal audit; and external audit and other external scrutiny reports.

Management Assurance:

As the administration of the Pension Funds was directly within the remit of the Director of Resources during 2017/18, (now within the remit of the Chief Officer – Finance), assurance was sought from the Director of Resources in relation to the effectiveness of internal financial controls. These assurances include internal financial controls and provide the opportunity to highlight any weaknesses or areas of concern that should be taken account of. For 2017/18, no significant areas of weakness were highlighted.

In reviewing this, it has been assessed that the Council's financial management arrangements conform to the governance requirements of the CIPFA statement on the Role of the Chief Financial Officer in Local Government (2010). Furthermore, in relation to statutory postholders, the effectiveness of the Council's arrangements can be evidenced through the relationship that they have had throughout the year with the Council and its officers, being full members of the Corporate Management Team. In addition, the Director of Resources (CFO) and the Monitoring Officer are generally in attendance to advise not only the Council at its meetings, but the Audit, Risk and

Scrutiny Committee, Finance, Policy and Resources Committee and the Pensions Committee.

The Audit, Risk and Scrutiny Committee remains responsible for ensuring the effectiveness of the internal audit function and also considering reports prepared by the external auditor. Further to this, the Pensions Committee is responsible for the internal and external audit functions in respect of the Pension Funds.

Assurance from Internal Audit:

The internal audit function, for the Council and the Pension Funds, was under contract to Aberdeenshire Council during the financial year.

During 2017/18, internal audit focused on the Pension Funds' Payroll with the outcome being reported to the Pensions Committee during June 2018.

At the Pensions Committee meeting on the 16th March 2018, the 2018/19 internal audit plan was approved to review Governance arrangements including risk management.

The objective is to provide assurance over the governance arrangements and procedures in place including risk management and performance management.

External Audit and Other External Scrutiny:

The external auditor, Audit Scotland, reports to the Pensions Committee on the year-end financial audit and also issue national performance audit reports.

Governance Compliance Statement

The LGPS regulations require administering authorities to measure their 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. There are no significant issues to highlight on the Governance Compliance Statement.

A copy of the Governance Compliance Statement can be found on our website www.nespf.org.uk.

Certification

It is our opinion that reasonable assurance can be placed upon the adequacy and effectiveness of systems of governance operated by Aberdeen City Council and the North East Scotland Pension Funds and that the annual review demonstrates sufficient evidence that the governance and internal control environment operated effectively during the 2017/18 financial year. On a quarterly basis, written updates regarding the Pension Funds' adherence to Investment Strategies and Performance are provided to the Pensions Committee.

Angela Scott	**Jonathan Belford, CPFA**	**Councillor M Tauqeer Malik**
Chief Executive	**Chief Officer - Finance**	**Pensions Committee Convener**

On behalf of Aberdeen City Council

14 September 2018

Governance Compliance Statement

Principle	Compliance
1. Structure	
a) The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing Council.	Partially compliant as per the Scheme Governance Statement
b) That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.	
c) That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	
d) That 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.	
2. Committee Membership and Representation	
a) That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include:- i) employing authorities (including non-scheme employers, e.g. admitted bodies); ii) scheme members (including deferred and pensioner scheme members), iii) where appropriate, independent professional observers, and iv) expert advisors (on an ad-hoc basis).	Partially compliant as per the Scheme Governance Statement
b) That 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 full opportunity to contribute to the decision making process, with or without voting rights.	
3. Voting	
a) 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.	Fully compliant as per the Scheme Governance Statement

4.) Training/Facility time/Expenses	
a) That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process.	Fully compliant as per the Scheme Governance Statement
b) That where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	
c) That the administering authority considers the adoption of annual training plans for committee members and maintains a log of all such training undertaken.	
5.) Meetings (frequency /quorum)	
a) That an administering authority's main committee or committees meet at least quarterly.	Fully compliant as per the Scheme Governance Statement
b) That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committee sits.	
c) That an administering authority who does not include lay members in their formal governance arrangements, must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	
6. Access	
a) That subject to any rules in the Council's constitution, all members of main and secondary committees or panels have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	Fully compliant as per the Scheme Governance Statement
7. Scope	
a) That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Fully compliant as per the Scheme Governance Statement
8. Publicity	
a) That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express an interest in wanting to be part of those arrangements.	Fully compliant as per the Scheme Governance Statement

Accounting Policies

The North East Scotland Pension Funds' Accounts have been prepared in accordance with the Code of Practice on local authority accounting in the UK (the Code).

The Annual Accounts summarise the Funds' transactions for the 2017/18 financial year and its position at year end as at 31 March 2018.

The Annual Accounts do not take account of the obligation to pay pensions and benefits which fall due after the end of the year.

The Funds' Annual Accounts are generally prepared on an accruals basis.

Contribution Income

Normal contributions, from both members and employers, are accounted for on an accruals basis. Employers' deficit funding contributions are accounted for on the due dates on which they are payable under the schedule of contributions set by the Scheme Actuary or on receipt (if earlier than the due date).

Employers' pension strain contributions are accounted for in the period in which the liability arises. Any amounts due in year but unpaid will be classed as a current financial asset.

Transfers to and from other Schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the Fund during the financial year and are calculated in accordance with the Local Government Pension Scheme Regulations.

Individual transfers in/out are accounted for when received/paid, which is normally when the member liability is accepted or discharged.

Investment Income

Interest income is recognised in the Fund accounts as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination.

Dividend income is recognised on the date the shares are quoted ex-dividend. Any amount not received by the end of the reporting period is disclosed in the net assets statement as a current financial asset.

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the net assets statement as a current financial asset.

Property related income consists primarily of rental income. Rental income is demanded in accordance with the terms of the lease, generally being quarterly in advance.

The property portfolio accounts are prepared on an accrual basis.

Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during the year.

Fund Account - Expenses

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.

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 a Fund expense as it arises.

Management Expenses

The Code does not require any breakdown of Pension Fund management expenses. However, in the interests of greater transparency, the Pension Fund discloses its management expenses in accordance with CIPFA guidance on Accounting for Local Government Pension Scheme Management Costs.

a.) Administrative Expenses and Oversight and Governance Costs

All administrative expenses and oversight and governance costs are accounted for on an accruals basis. All staff costs are charged direct to the Fund. Accommodation and other overheads are apportioned to the Fund in accordance with Aberdeen City Council policy.

b.) Investment Management Expenses

All investment management expenses are accounted for on an accrual basis.

Fees of the external investment managers and custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.

In addition, the Fund has negotiated performance related fees with a number of its investment managers. Performance related fees were £5,032,863 in 2017/18 (2016/17 £4,654,645).

Where an investment manager’s fee note has not been received by the balance sheet date, an estimate based upon the market value of their mandate as at the end of the year is used for inclusion in the Fund account.

Financial Assets

Financial assets are included in the net assets statement on a fair value basis at the reporting date. A financial asset is recognised in the net assets statement on the date the Fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in the fair value of the asset are recognised by the Fund.

Valuation of Investments

All investments are valued at their market value at 31 March 2018 and are determined as follows:

All stocks within the FTSE 100 are valued on the basis of the last traded price recorded on SETS (the Stock Exchange Electronic Trading Service), while all other listed securities are valued on the basis of the market conventions where primarily traded, which is either last traded or bid market price.

Investments held in foreign currency have been valued on the above basis and translated into sterling at the rate ruling at the balance sheet date.

Managed funds including unit trusts are stated at the bid price of the latest prices quoted or the latest valuation by the Funds’ custodian.

Private equity assets are independently valued by the appointed Fund Manager and General Partners. Fair value is calculated by applying Private Equity and Venture Capital Valuation Guidelines.

Unlisted investments are valued using one of the following methodologies:

- Multiple (based on comparable quoted multiples and significant third party transactions)
- Price of Recent Investment
- Net Assets
- Discounted Cash Flows or Earnings from Underlying Business

When applying an Earning Multiple, the Fund Manager/General Partner will use the best estimate of maintainable earnings. In accordance with guidelines, discounts have been applied for size, quality of earnings, gearing and dependency on one customer where appropriate. A Marketability Discount will also have been applied to reflect liquidity.

Direct property investments are valued by an external valuer (Colliers International), in accordance with the Valuation Standards issued by The Royal Institute of Chartered Surveyors.

The valuer’s opinion of Market Value was primarily derived using:

- Comparable recent market transactions on arm's length terms.

A full copy of the valuer's report including all general assumptions and definitions is available on request from the Director of Resources, Aberdeen City Council, Resources, Level 1 West, Business Hub 7, Marischal College, Broad Street, Aberdeen, AB10 1AB.

Derivatives

Derivative contract assets are valued at bid price and liabilities are fair valued at offer price. Changes in the fair value of derivative contracts are included in the change in market value.

The value of future contracts is determined using exchange prices at the reporting date. Amounts due from or owed to the broker are the amounts outstanding in respect of the initial margin and variation margin.

The future value of forward currency contracts is based on market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year end with an equal and opposite contract.

Cash

Cash comprises cash in hand and demand deposits.

Cash equivalents are short term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal risk of changes in value.

Financial Liabilities

The Fund recognises financial liabilities at fair value as at the reporting date. A financial liability is recognised in the net assets statement on the date the fund becomes party to the liability. From this date any gains or losses arising from the change in the fair value of the liability are recognised.

Actuarial Present Value of Promised Retirement Benefits

The actuarial present value of promised retirement benefits of each of the Funds is assessed on a quarterly basis by the Scheme Actuary, and in accordance with the requirements of IAS 19 and relevant actuarial standards.

As permitted under IAS 26, the Funds have opted to disclose the actuarial present value of promised retirement benefits by way of a note to the net assets statement, (Note 1) together with the full Statement by the Consulting Actuary found on Appendix 1.

Orphan liabilities are liabilities in the North East Scotland Pension Fund for which there is no sponsoring employer within the Fund. Ultimately, orphan liabilities must be underwritten by all other employers of the Fund.

Under the termination policy of the Funds, as set out by the Scheme Actuary, a termination assessment will be made on a least risk funding basis, unless the admission body has a guarantor within the Fund or a successor body exists to take over the liabilities. This is to protect the other employers in the Fund as, at termination, the admitted body's liabilities will become "orphan liabilities" within the Fund.

Additional Voluntary Contributions

North East Scotland 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 Fund has appointed Prudential as its AVC provider together with Standard Life. AVCs are paid to the AVC provider by the employers and are specifically for providing additional benefits for the individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and the movements in the year, from each service provider. AVCs are not included within the Annual Accounts however they are detailed in Note 22.

Critical Judgments in applying Accounting Policies

Unquoted Private Equity Investments

It is important to recognise the highly subjective nature of determining the fair value of private equity investments. They are inherently based on forward looking estimates and judgments involving many factors. Unquoted private equities are valued by the investment managers.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which follow the valuation principles of IFRS.

The value of unquoted private equities at 31 March 2018 was £232,460,096 (31 March 2017 £220,649,167).

Actuarial Present Value of Promised Retirement Benefits

Each fund is required to disclose the estimated actuarial present value of promised retirement benefits as at the end of the financial year. These estimates are prepared by the Fund Actuary. These values are calculated in line with International Accounting Standard 19 (IAS 19) assumptions and comply with requirements of IAS 26. However, the results are subject to significant variances based on changes to the underlying assumptions.

The figures are only prepared for the purposes of IAS 26 and have no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

Events after the Reporting Period

Events after the reporting period are those events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the Statement of Accounts is authorised for issue. Two types of events can be identified:

- those that provide evidence of conditions that existed at the end of the reporting period – the Statement of Accounts is adjusted to reflect such events
- those that are indicative of conditions that arose after the reporting period – the Statement of Accounts is not adjusted to reflect such events, but where a category of events would have a material effect, disclosure is made in the notes of the nature of the events and their estimated financial effect

Events taking place after the date of authorisation for issue are not reflected in the Statement of Accounts.

Changes in Accounting Policies

Changes in accounting policies are only made when required by proper accounting practices or the changes provide more reliable or relevant information. Where a change is made, it is applied retrospectively by adjusting opening balances and comparative amounts for the prior period as if the new policy had always been applied.

Accounting Standards That Have Been Issued but Have Not Yet Been Adopted

The Code requires the disclosure of information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted. The following new or amended standards have been published but not yet adopted:

- **IFRS 9 Financial Instruments**, which introduces extensive changes to the classification and measurement of financial assets, and a new "expected credit loss" model for impairing financial assets. The impact will be to reclassify assets currently classified as loans and receivables to amortised cost. There are not expected to be any changes in the measurement of financial assets and the Fund does not at this stage anticipate any adjustments for impairments.

- **IFRS 15 Revenue from Contracts with Customers,** presents new requirements for the recognition of revenue, based on a control-based revenue recognition model. The Fund does not have any revenue streams within the scope of the new standard.

- **IAS 7 Statement of Cash Flows (Disclosure Initiative),** will potentially require some additional analysis of Cash Flows from Financing Activities, however since the Fund is not currently required to prepare a Cash Flow Statement it does not anticipate any additional disclosure.

- **IAS 12 Income Taxes (Recognition of Deferred Tax Assets for Unrealised Losses),** applies to deferred tax assets related to debt instruments measured at fair value. Currently the Fund does not hold such financial instruments.

NORTH EAST SCOTLAND PENSION FUND ACCOUNTS

Fund Account for the year ended 31 March 2018

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

	Notes	**2016/17**	**2017/18**
		£'000	**£'000**
Contributions Receivable			
Employees' Contributions	2	28,856	29,533
Employers' Contributions	2	98,538	105,124
Transfer Values	3	2,343	3,371
Other Income		2	4
		129,739	**138,032**
Benefits Payable			
Retirement Pensions	4	94,624	99,288
Retirement Allowances	4	22,552	26,184
Death Gratuities	4	4,230	4,646
Contributions Refunded	5	678	563
Transfer Values	5	4,625	4,373
		126,709	**135,054**
Management Expenses	6	**18,486**	**21,197**
Return on Investment			
Investment Income	7	49,813	52,770
Profits and (Losses) on Disposal of Investments and Changes in Market Value of Investments	8	598,598	276,265
Net Return on Investments		**648,411**	**329,035**
Net Increase/(Decrease) in the Net Assets available for Benefits during the year		**632,955**	**310,816**
Opening Net Assets of the Fund		**3,181,793**	**3,814,748**
Net Assets of the Fund at the end of the year		**3,814,748**	**4,125,564**

Notes to Accounts – Please refer to the Contents Page for the page numbers relevant to the North East Scotland Pension Fund.

NORTH EAST SCOTLAND PENSION FUND ACCOUNTS

Net Assets Statement as at 31 March 2018

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

	Notes	2016/17	2017/18
Investment Assets		**£'000**	**£'000**
Fixed Interest, Public Sector		108,069	0
Fixed Interest, Corporate		11,652	0
Fixed Interest, Overseas		163,871	0
Index Linked		7,382	0
UK Equities		740,007	734,875
Overseas Equities		674,024	819,078
Pooled Vehicle		1,554,264	1,944,722
Direct Property	13	259,146	293,045
Unit Trust - Other		3,457	0
Derivative Contracts (including, Futures Options, Forward Foreign Exchange Contracts and Swaps)		0	0
Private Equity - Other		240,975	232,461
Funds held by Investment Managers		18,594	90,704
ACC Loans Fund Deposit	19	39,740	22,780
Total Investment Assets		**3,821,181**	**4,137,665**
Investment Liabilities			
Derivative Contracts (including, Futures Options, Forward Foreign Exchange Contracts and Swaps)		(493)	0
Net Investment Assets		**3,820,688**	**4,137,665**
Long Term Asset	18	**78**	**33**
Current Assets	18	17,028	14,824
Current Liabilities	18	(23,046)	(26,958)
Net Current Assets/(Liabilities)		**(6,018)**	**(12,134)**
Net Assets of the Fund at the end of the year		**3,814,748**	**4,125,564**

Jonathan Belford, CPFA
Aberdeen City Council, Chief Officer - Finance
Date: 14 September 2018

The unaudited accounts were issued on 22 June 2018 and the audited accounts were authorised for issue by Jonathan Belford on 14 September 2018.

ABERDEEN CITY COUNCIL TRANSPORT FUND ACCOUNTS

Fund Account for the year ended 31 March 2018

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

	Notes	2016/17	2017/18
		£'000	£'000
Contributions Receivable			
Employees' Contributions	2	115	100
Employer's Contributions	2	2,109	2,028
Other Income		320	320
		2,544	**2,448**
Benefits Payable			
Retirement Pensions	3	3,083	3,210
Retirement Allowances	3	802	914
Death Gratuities	3	80	2
Transfer Values	4	65	0
		4,030	**4,126**
Management Expenses	5	**245**	**991**
Return on Investment			
Investment Income	6	1,505	812
Profits and (Losses) on Disposal of Investments and Changes in Market Value of Investments	7	13,949	1,962
Net Return on Investments		**15,454**	**2,774**
Net Increase/ (Decrease) in the Net Assets available for Benefits during the year		**13,723**	**105**
Opening Net Assets of the Fund		**86,243**	**99,966**
Net Assets of the Fund at the end of the year		**99,966**	**100,071**

Notes to Accounts - Please refer to the Contents Page for the page numbers relevant to the Aberdeen City Council Transport Fund.

ABERDEEN CITY COUNCIL TRANSPORT FUND ACCOUNTS

Net Assets Statement as at 31 March 2018

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

	Notes	2016/17	2017/18
Investment Assets		**£'000**	**£'000**
Pooled Vehicle		88,705	97,060
Index Linked Securities		7,527	1,117
Funds held by Investment Managers		3,318	1,450
ACC Loans Fund Deposit	16	320	171
Net Investment Assets		**99,870**	**99,798**
Long Term Asset	15	**350**	**324**
Current Assets	15	180	314
Current Liabilities	15	(434)	(365)
Net Current Assets/ (Liabilities)		**(254)**	**(51)**
Net Assets of the Fund at the end of the year		**99,966**	**100,071**

Jonathan Belford, CPFA
Aberdeen City Council, Chief Officer - Finance
Date: 14 September 2018

The unaudited accounts were issued on 22 June 2018 and the audited accounts were authorised for issue by Jonathan Belford on 14 September 2018.

NOTES TO THE NORTH EAST SCOTLAND PENSION FUND ACCOUNTS

Note 1: Actuarial Valuation Report

An Actuarial Report for the North East Scotland Pension Fund (NESPF) was provided as at 31 March 2017.

Information from the 2017 Actuarial Valuation is detailed below:

Market Value of Assets at Valuation	£3,815,000,000
Liabilities	£3,576,000,000
Surplus	£ 239,000,000

Funding Level

The Level of Funding in Terms of the Percentage of Assets available to meet Liabilities	107%

Achieving the Solvency Funding Target

The funding objective as set out in the Funding Strategy Statement (FSS) is to achieve and maintain a solvency funding level of 100% of liabilities (**the solvency funding target**). In line with the FSS, the Fund has determined a contribution requirement for each employer taking into account the offset of any surplus held or the recovery of any deficit due. The average spread/recovery period adopted by the Fund is 24 years.

The valuation determined that the average employer cost of providing members benefits across the Fund was 22.0% (the Primary contribution rate.) By spreading the surplus over 24 years the Secondary contribution rate for the whole Fund is -2.4% meaning that the average employer contribution rate is 19.4% of pensionable pay.

In practice, each employer's position is assessed separately, details of which can be found in the 2017 Actuarial Valuation, this sets out the contributions for each employer over the three year period to 31 March 2021.

Schedule to the Rates and Adjustments Certificate

The Schedule to the Rates and Adjustments Certificate for the Fund sets out the contributions for the employer over the three year period to 31 March 2021. The rates have been determined in accordance with the FSS. Any adjustments made to the rates proposed by the scheme actuary were made as a result of the consultation carried out by the Fund and were made in line with the approaches agreed with the Scheme Actuary. Contribution requirements for the period from 1 April 2021 onwards will be revised as part of the next actuarial valuation as at 31 March 2020 and will be confirmed in the Rates and Adjustments Certificate and Schedule accompanying that valuation report.

Assumptions used to Calculate Funding Target

Discount Rate	4.15% p.a.
Assumed Long Term Price Inflation (CPI)	2.40% p.a.
Salary Increases – Long term	3.90% p.a.
Salary Increases – Short term	Varied by employer*
Pension Increases in Payment	2.40% p.a.

*Where an allowance for short term pay restraint was determined appropriate either 1% or 2.4% (CPI) was applied.

The full Actuarial Report and the Funding Strategy Statement are available from the office of the Director of Resources, Aberdeen City Council, Resources, Level 1 West, Business Hub 7, Marischal College, Broad Street, Aberdeen, AB10 1AB.

Actuarial Statement

The Scheme Actuary has provided a statement describing the funding arrangements of the Fund.

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standards 26 (IAS 26) assumptions, is estimated to be £4,892m (2017 £4,718m). The figure is used for the statutory accounting purposes by North East Scotland Pension Fund and complies with the requirements of IAS 26.

The figure is only prepared for the purposes IAS 26 and has no validity in other circumstances payable to the Fund. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

The full statement by the Consulting Actuary can be found in Appendix 1.

Note 2: Contributions Receivable

By Category	**2016/17**	**2017/18**
	£'000	**£'000**
Employees' Normal Contributions	**28,856**	**29,533**
Employers' Normal Contributions	94,772	101,226
Employers' Deficit Recovery Contributions	3,766	3,898
Total Employers' Contributions	**98,538**	**105,124**
Total	**127,394**	**134,657**

By Authority	**2016/17**	**2017/18**
	£'000	**£'000**
Administering Authority	36,869	42,619
Scheduled Bodies	75,366	78,481
Admitted Bodies	10,928	9,179
Transferee Admission Bodies	4,231	4,378
Total	**127,394**	**134,657**

Note 3: Transfers in from other Pension Funds

	2016/17	**2017/18**
	£'000	**£'000**
Individual Transfers	2,343	3,371
Total	**2,343**	**3,371**

Note 4: Benefits Payable

By Category	**2016/17**	**2017/18**
	£'000	**£'000**
Pensions	94,624	99,288
Commutation and Lump Sum Retirement Benefits	22,552	26,184
Lump Sum Death Benefits	4,230	4,646
Total	**121,406**	**130,118**

By Authority	2016/17	2017/18
	£'000	£'000
Administering Authority	31,452	35,474
Scheduled Bodies	79,549	81,587
Admitted Bodies	9,162	10,145
Transferee Admission Bodies	1,243	2,912
Total	**121,406**	**130,118**

Note 5: Payment to and on Account of Leavers

	2016/17	2017/18
	£'000	£'000
Refunds to Members Leaving Service	527	562
Payments for Members Joining State Scheme	151	1
Individual Transfers	4,625	4,373
Total	**5,303**	**4,936**

Note 6: Management Expenses

	2016/17	2017/18
	£'000	**£'000**
Pension Fund Staffing Costs – Administration	971	1,070
Support Services including IT	563	549
Printing and Publications	29	19
Administration Expenses Total	**1,563**	**1,638**
Pension Fund Staffing Costs – Investment	131	189
Pension Fund Committee	12	12
Pension Board	2	3
External Audit Fee	32	39
Internal Audit Fee	6	9
Actuarial Fees	112	109
General Expenses	173	106
Oversight and Governance Expenses Total	**468**	**467**
Investment Management	10,214	10,997
Performance Fees	4,655	5,033
Direct Operating Property Expenses	347	259
Transaction Costs	1,117	2,679
Custody Fees	122	124
Investment Management Expenses Total	**16,455**	**19,092**
Management Expenses Grand Total	**18,486**	**21,197**

Analysis of Transaction Costs:

Commission £'000	Fees/Tax £'000	2016/17 Total £'000	Asset Type	Commission £'000	Fees/Tax £'000	2017/18 Total £'000
0	0	0	Fixed Income	781	0	**781**
315	802	1,117	Equities	239	806	**1,045**
0	0	0	Pooled Investments	0	842	**842**
0	0	0	Private Equity	11	0	**11**
315	**802**	**1,117**	**Total**	**1,031**	**1,648**	**2,679**

Note 7: Investment Income

	2016/17	2017/18
	£'000	**£'000**
Fixed Interest Securities	6,225	27
Equity Dividends	20,270	23,402
Pooled Property Investments	7	0
Property Rental Income	14,255	14,969
Interest on Cash Deposit	346	90
Other (including P/L from		
Currency and Derivatives)	8,780	14,582
Total	**49,883**	**53,070**
Tax		
Withholding Tax - Fixed Interest Securities	0	(16)
Withholding Tax – Equities	(63)	(284)
Withholding Tax – Pooled	(7)	0
Total Tax	**(70)**	**(300)**
Net Total	**49,813**	**52,770**

Note 8: Investment Assets

Reconciliation of Movements in Investments and Derivatives

	Market Value 31 March 2017	Purchases	Sales	Change in Market Value	Market Value 31 March 2018
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Fixed Interest	290,974	437,404	(719,824)	(8,554)	0
UK Equities	740,007	158,397	(165,636)	2,107	734,875
Overseas Equities	674,024	63,054	(97,976)	179,976	819,078
Pooled Investments	1,557,721	835,168	(519,339)	71,172	1,944,722
Property	259,146	35,136	(12,372)	11,135	293,045
Private Equity	240,975	61,906	(87,400)	16,980	232,461
	3,762,847	**1,591,065**	**(1,602,547)**	**272,816**	**4,024,181**
Derivative Contracts					
FX Contracts	(493)	3,456,730	(3,459,686)	3,449	0
	3,762,354	**5,047,795**	**(5,062,233)**	**276,265**	**4,024,181**
Other					
Cash	58,334				113,484
Net Investment Assets	**3,820,688**				**4,137,665**

Reconciliation of Movements in Investments and Derivatives (continued)

	Market Value 31 March 2016	**Purchases**	**Sales**	**Change in Market Value**	**Market Value 31 March 2017**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Fixed Interest	281,221	355,089	(366,906)	21,570	290,974
UK Equities	607,732	174,716	(173,997)	131,556	740,007
Overseas Equities	749,792	65,885	(319,577)	177,924	674,024
Pooled Investments	1,097,674	342,908	(132,192)	249,331	1,557,721
Property	232,555	37,161	(6,063)	(4,507)	259,146
Private Equity	179,867	50,920	(37,111)	47,299	240,975
	3,148,841	**1,026,679**	**1,035,846)**	**623,173**	**3,762,847**
Derivative Contracts					
FX Contracts	(8,227)	909,161	(876,852)	(24,575)	(493)
	3,140,614	**1,935,840**	**(1,912,698)**	**598,598**	**3,762,354**
Other					
Cash	46,129				58,334
Net Investment Assets	**3,186,743**				**3,820,688**

Note 9: Analysis of Investments

	2016/17	2017/18
Fixed Interest Securities	**£'000**	**£'000**
UK		
Public Sector Quoted	108,069	0
Corporate Quoted	11,652	0
Overseas		
Public Sector Quoted	115,574	0
Corporate Quoted	48,297	0
Subtotal Fixed Interest Securities	**283,592**	**0**
Subtotal Index Linked Securities	**7,382**	**0**
Equities		
UK		
Quoted	740,007	734,875
Overseas		
Quoted	674,024	819,078
Subtotal Equities	**1,414,031**	**1,553,953**
Pooled Funds – Additional Analysis		
UK		
Unit Trusts	783,054	938,293
Pooled Indexed Linked	190,720	251,551
Overseas		
Unit Trusts	583,947	636,218
Global Pooled Bonds	0	118,660
Subtotal Pooled Funds	**1,557,721**	**1,944,722**
Private Equity	240,975	232,461
Property, Direct	259,146	293,045
Funds held by Investment Managers	18,594	90,704
ACC Loans Fund Deposit	39,740	22,780
Investment Assets Total	**3,821,181**	**4,137,665**
Investment Liabilities		
Forward Ex	(493)	0
Derivatives	0	0
Investment Liabilities Total	**(493)**	**0**
Net Investment Assets	**3,820,688**	**4,137,665**

Note 10: Analysis of Derivatives

Futures

There were no outstanding exchange traded future contracts.

Forward Foreign Currency

In order to maintain appropriate diversification and to take advantage of overseas investment returns, a significant proportion of the Fund's quoted portfolio is in passive overseas stock markets. To reduce the volatility associated with fluctuating currency rates, the Fund has applied, through the passive manager, a dynamic currency hedge on a pooled basis.

Settlement	Currency Bought	Local Value	Currency Sold	Local Value	Asset Value	Liability Value
		£'000		**£'000**		**£'000**
Open forward Currency Contracts as at 31 March 2018					0	0
Net Forward Currency Contracts at 31 March 2018						**0**
Prior Year Comparative						
Open Forward Currency Contracts at 31 March 2017					447	(940)
Net Forward Currency Contacts at 31 March 2017						**(493)**

Note 11: Investments Analysed by Fund Manager

	31 March 2017	%	31 March 2018	%
	£'000		£'000	
Investment Assets				
State Street Global Advisors	1,327,587	34.8	1,420,631	34.4
Baillie Gifford	991,344	26.0	1,130,668	27.4
BlackRock Asset Management	454,539	11.9	465,188	11.3
BlackRock DGF	103,389	2.7	157,367	3.8
Baring Asset Managers	279,992	7.3	(3)	0.0
AAM Property (API)	265,311	7.0	312,228	7.6
AAM Property Residential	6,890	0.2	8,136	0.2
HarbourVest	117,261	3.1	82,365	2.0
Standard Life	53,791	1.4	54,377	1.3
ACC Loans Fund Deposit	39,740	1.0	22,780	0.5
Global Custodian	3,392	0.1	15,758	0.4
Partners Group	45,962	1.2	52,313	1.3
NESPF*	49	0.0	0	0.0
Maven Capital	2,894	0.1	2,925	0.1
Capital Dynamics	7,325	0.2	15,003	0.4
RCP Advisors	1,528	0.1	7,289	0.2
Unigestion	15,269	0.4	11,808	0.3
Invesco DGF	104,425	2.7	153,663	3.7
Russell Overlay	0	0.0	33,960	0.8
Russell Multi Asset Credit	0	0.0	101,831	2.5
Russell Transition	0	0.0	479	0.0
Aviva Infrastructure	0	0.0	88,899	2.1
	3,820,688	**100.2**	**4,137,665**	**100.3**
Net Long and Current Assets				
Bank Account	78	0.0	19	0.0
Long Term and Current Debtors Less Creditors	(6,018)	(0.2)	(12,120)	(0.3)
Net Assets	**3,814,748**	**100.0**	**4,125,564**	**100.0**

*Note: During 2016-17, the following former Fund Managers were merged into one 'In House' Account for the purpose of collecting any residual income:

AAM Global Excluding UK, Aberdeen Frontier, Capital, In House, RREEF and Rogge

The following investments represent more than 5% of the Net Investment Assets:

Security	Market Value 31 March 2017	% of Net Investment Assets	Market Value 31 March 2018	% of Net Investment Assets
	£'000	**%**	**£'000**	**%**
MPF International Equity Index Pooled Fund	583,947	15.3	279,983	6.8
MPF UK Equity Pooled Fund	552,920	14.5	337,317	8.2

The investments listed above are Pooled Investments, i.e. where two or more parties 'pool' or combine their investments. This type of investment allows the Fund to gain from economies of scale, i.e. lower transaction costs, and diversification that can help reduce risk.

Note 12: Stock Lending

Stock Lending is the lending of stock from one investor to another that entitles the lender to continue to receive income generated by the stock plus an additional payment by the borrower.

Collateral is held at a minimum of 105% in respect of each borrower, consisting of UK and Overseas Gilts, UK Equities, Certificates of Deposit and Letters of Credit.

There was no stock lending in operation as at 31 March 2018.

Note 13: Property Holdings

	2016/17	2017/18
	£'000	**£'000**
Opening Balance	232,555	259,146
Purchases	34,932	22,393
Construction	2,215	12,705
Subsequent Expenditure	14	38
Disposals	(6,063)	(12,372)
Net Increase in Market Value	(4,507)	11,135
Closing Balance	**259,146**	**293,045**

The property holdings note shows those UK properties directly held by the Fund and as such the Fund is responsible for all repairs, maintenance or enhancements. There are no restrictions on the reliability of the property or the remittance of income or proceeds on disposal and the Fund is not under any contractual obligations to purchase, construct or develop any of these properties, as all are addressed within the Fund's Property Investment Strategy.

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

	2016/17	2017/18
	£'000	**£'000**
Within One Year	13,984	15,144
Between One Year and Five Years	52,638	55,604
Later than Five Years	96,061	98,560
Total	**162,683**	**169,308**

Note 14: Financial and Non-Financial Instruments

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

Non-financial instruments have been added to the table for reconciliation to the Net Assets of the Fund.

31 March 2017				31 March 2018		
Designated as Fair Value through Profit & Loss	**Loans and Receivables**	**Financial Liabilities at Amortised Cost**		**Designated as Fair Value through Profit & Loss**	**Loans And Receivables**	**Financial Liabilities at Amortised Cost**
£'000	**£'000**	**£'000**		**£'000**	**£'000**	**£'000**
			Financial Assets			
290,974			Fixed Interest	0		
1,414,031			Equities	1,553,953		
1,557,721			Pooled	1,944,722		
240,975			Private Equity	232,461		
0			Derivative Contracts	0		
	58,334		Cash		113,484	
	17,106		Debtors		14,857	
3,503,701	**75,440**		**Subtotal**	**3,731,136**	**128,341**	
			Financial Liabilities			
(493)			Derivative Contracts	0		
		(23,046)	Creditors			(26,958)
(493)		**(23,046)**		**0**		**(26,958)**
3,503,208	**75,440**	**(23,046)**	**Financial Instruments Total**	**3,731,136**	**128,341**	**(26,958)**
			Non-Financial Instruments			
259,146			Property	293,045		
3,762,354	**75,440**	**(23,046)**		**4,024,181**	**128,341**	**(26,958)**
		3,814,748	**Net Assets of the Fund**			**4,125,564**

Note 15: Net Gains and Losses on Financial and Non-Financial Instruments

31 March 2017		31 March 2018
£'000	**Financial Assets**	**£'000**
627,594	Fair Value through Profit and Loss	265,280
	Financial Liabilities	
(24,489)	Fair Value through Profit and Loss	(150)
603,105	**Net Gains and Losses on Financial Instruments**	**265,130**
	Non-Financial Instruments	
(4,507)	Fair Value through Profit and Loss	11,135
598,598	**Net Gains and Losses of the Fund**	**276,265**

Note 16: Valuation of Financial and Non-Financial Instruments carried at Fair Value

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

Level 1

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

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

Level 2

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

Level 3

Financial instruments at level 3 are those where at least one input that could have a significant effect on the instruments valuation is not based on observable market data.

Such instruments would include unquoted equity investments and hedge fund of funds, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investment in private equity are based on valuations provided by the general partners to the private equity funds in which North East Scotland Pension Fund has invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which follow the valuation principles of IFRS and US GAAP. Valuations are usually undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

The following table provides an analysis of the financial assets and liabilities of the Pension Fund grouped into Levels 1 to 3, based on the level at which the fair value is observable.

Non-Financial instruments have been added to the table for reconciliation to Net Assets of the Fund.

Note 16A: Fair Value – Basis of Valuation

The basis of the valuation of each class of investment asset is set out below. There have been no changes in the valuation techniques used during the year. All assets have been valued using fair value techniques which represent the highest and best price available at the reporting date.

Description of Asset	Valuation Hierarchy	Basis of Valuation	Observable and Unobservable Inputs	Key Sensitivities affecting the Valuations provided
Market Quoted Investments	Level 1	Published bid market price ruling on the final day of the accounting period	Not required	Not required
Quoted Bonds	Level 1	Fixed interest securities are valued at a market value based on current yields	Not required	Not required
Futures and Options in UK Bonds	Level 1	Published exchange prices at the year-end	Not required	Not required
Exchange Traded Pooled Investments	Level 1	Closing bid value on published exchanges	Not required	Not required
Unquoted Bonds	Level 2	Average of broker prices	Evaluated price feeds	Not required
Forward Foreign Exchange Derivatives	Level 2	Market forward exchange rates at the year-end	Exchange rate risk	Not required
Overseas Bond Options	Level 2	Option pricing model	Annualised volatility of counterpart credit risk	Not required
Pooled Investments – Overseas Unit Trusts and Property Funds	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
Freehold and Leasehold Properties	Level 2	Valued at fair value at the year –end using the investment	Existing lease terms and rentals	

		method of valuation by Paul Willis Bsc (Hons) MRICS of Colliers International in accordance with the *RICS Valuation Professional Standard*	Independent market research Nature of tenancies Covenant strength for existing tenants Assumed vacancy levels Estimated rental growth Discount rate	
Pooled Investments – Hedge Funds	Level 3	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	Valuations could be affected by material events occurring between the date of the financial statements provided and the Pension Fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts
Unquoted Equity	Level 3	Comparable valuation of similar companies in accordance with *International Private Equity and Venture Capital Valuation Guidelines* (2012)	EBITDA multiple Revenue multiple Discount for lack of marketability Control premium	Valuations could be affected by material events occurring between the date of the financial statements provided and the Pension Fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts

.

Values at 31 March 2018	Quoted Market Price Level 1	Using Observable Inputs Level 2	With Significant Unobservable Inputs Level 3	Total
	£'000	£'000	£'000	£'000
Financial Assets				
Financial Assets at Fair Value through Profit and Loss	3,498,675	0	232,461	3,731,136
Loans and Receivables	128,341			128,341
Total Financial Assets	**3,627,016**	**0**	**232,461**	**3,859,477**
Financial Liabilities				
Financial Liabilities at Fair Value through Profit and Loss	0	0	0	0
Financial Liabilities at Amortised Cost	(26,958)	0	0	(26,958)
Total Financial Liabilities	**(26,958)**	**0**	**0**	**(26,958)**
Total Financial Instruments	**3,600,058**	**0**	**232,461**	**3,832,519**
Non-Financial Instruments				
Non-Financial Instruments at Fair Value through Profit and Loss	0	293,045	0	293,045
Net Assets of the Fund	**3,600,058**	**293,045**	**232,461**	**4,125,564**

Values at 31 March 2017	Quoted Market Price Level 1	Using Observable Inputs Level 2	With Significant Unobservable Inputs Level 3	Total
	£'000	£'000	£'000	£'000
Financial Assets				
Financial Assets at Fair Value through Profit and Loss	3,283,052	0	220,649	3,503,701
Loans and Receivables	75,440			75,440
Total Financial Assets	**3,358,492**	**0**	**220,649**	**3,579,141**
Financial Liabilities				
Financial Liabilities at Fair Value through Profit and Loss	0	(493)	0	(493)
Financial Liabilities at Amortised Cost	(23,046)	0	0	(23,046)
Total Financial Liabilities	**(23,046)**	**(493)**	**0**	**(23,539)**
Total Financial Instruments	**3,335,446**	**(493)**	**220,649**	**3,555,602**
Non-Financial Instruments				
Non-Financial Instruments at Fair Value through Profit and Loss	0	259,146	0	259,146
Net Assets of the Fund	**3,335,446**	**258,653**	**220,649**	**3,814,748**

Note 16B: Transfers between Levels 1 and 2

There were no transfers between levels 1 and 2.

Note 16C: Reconciliation of Fair Value Measurements within Level 3

2016/17	Market Value 1 April 2017	Transfers Into Level 3	Transfers Out of Level 3	Purchases during the year & Derivative Payments	Sales during the year & Derivative Receipts	Realised Gains & Losses	Unrealised Gains & Losses (a)	Market Value 31 March 2018
	£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Private Equity	220,649	0	0	52,370	(53,989)	26,572	(13,141)	232,461
Total	**220,649**	**0**	**0**	**52,370**	**(53,989)**	**26,572**	**(13,141)**	**232,461**

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

Note 16D: Sensitivity of Assets Valued at Level 3

Having analysed historical data and current market trends, and consulted with independent investment advisors, the Fund has determined that the valuation methods described above are likely to be accurate to within the following ranges, and has set out below the consequent potential impact on the closing value of investments held at 31 March 2018.

	Assessed Valuation Range (+/-)	Value at 31 March 2018	Value on Increase	Value on Decrease
		£000	**£000**	**£000**
Private Equity	30%	232,461	302,199	162,723
Total		**232,461**	**302,199**	**162,723**

Note 17: Risk arising from Financial and Non-Financial Instruments

The Fund's primary long term risk is that the Fund's 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 Fund and to maximise the opportunity for gains across the whole Fund portfolio.

The 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 Fund manages its liquidity risk, ensuring there is sufficient liquidity to meet the Fund's forecast cash flows.

The Fund manages these investment risks as part of its overall Pension Fund risk management strategy.

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

Market Risk

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

The objective of the 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 industry sectors and individual securities.

Specific risk exposure is limited by applying risk weighted maximum exposures to individual investments.

Other Price Risk – Sensitivity Analysis

Following analysis of historical data and expected investment return movement during the financial year and in consultation with the Fund's Investment Advisor, the Fund has determined that the following movements in market price risk are reasonably possible for the 2017/18 reporting period.

Asset Type	Potential Market Movements (+/-)
UK Bonds	5.6%
Overseas Bonds	5.6%
UK Equities	16.0%
Overseas Equities	20.5%
Pooled - DGF	12.0%
Private Equity	30.0%
Property	13.0%
Cash	1.0%

The potential price changes disclosed above are broadly consistent with a one standard deviation movement in the value of the assets. The sensitivities are consistent with the assumptions contained in the Investment Advisor's most recent review. This analysis assumes that all other variables, in particular foreign currency exchange rates and interest rates, remain the same.

Had the market price of the 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 follows (the prior year comparator is shown overleaf).

Non-Financial instruments have been added to the table for reconciliation to the Net Investment Assets.

Asset Type	Value as at 31 March 2018	Percentage Change	Value on Increase	Value on Decrease
	£’000	**%**	**£’000**	**£’000**
Cash and Cash Equivalents	113,484	1.0	114,619	112,349
Investment Portfolio Assets				
UK Bonds	251,551	5.6	265,638	237,464
Overseas Bonds	220,491	5.6	232,838	208,144
UK Equities	1,273,241	16.0	1,476,960	1,069,522
Overseas Equities	1,353,465	20.5	1,630,925	1,076,005
Pooled – Diversified Growth Funds	311,028	12.0	348,351	273,705
Pooled - Infrastructure	88,899	13.0	100,456	77,342
Private Equity	232,461	30.0	302,199	162,723
Total Financial Instruments	**3,844,620**		**4,471,986**	**3,217,254**
Non-Financial Instruments				
Property	**293,045**	13.0	**331,141**	**254,949**
Total Assets Available to Pay Benefits	**4,137,665**		**4,803,127**	**3,472,203**

Asset Type	Value as at 31 March 2017	Percentage Change	Value on Increase	Value on Decrease
	£'000	**%**	**£'000**	**£'000**
Cash and Cash Equivalents	57,841	1.1	58,477	57,205
Investment Portfolio Assets				
UK Bonds	317,823	5.5	335,303	300,343
Overseas Bonds	163,871	5.5	172,884	154,858
UK Equities	1,315,246	16.0	1,525,685	1,104,807
Overseas Equities	1,257,971	20.5	1,515,855	1,000,087
Pooled – Diversified Growth Funds	207,815	12.0	232,753	182,877
Private Equity	240,975	30.0	313,268	168,682
Total Financial Instruments	**3,561,542**		**4,154,225**	**2,968,859**
Non-Financial Instruments				
Property	259,146	13.0	292,835	225,457
Total Assets Available to Pay Benefits	**3,820,688**		**4,447,060**	**3,194,316**

Interest Rate Risk

The Fund invests in financial assets for the primary purpose of obtaining a return on investments. These investments are subject to interest rate risks which represents the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Fund's interest rate risk is routinely monitored by the Fund in accordance with the Fund's risk management strategy, including monitoring the exposure to interest rates and assessment of actual interest rates against the relevant benchmarks.

The Fund's direct exposure to interest rate movements as at 31 March 2017 and 31 March 2018 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value:

Asset Type	**As at 31 March 2017**	**As at 31 March 2018**
	£'000	**£'000**
Cash and Cash Equivalents	58,334	113,484
Cash Balances	78	19
Fixed Interest Securities	481,694	472,041
Total	**540,106**	**585,544**

Interest Rate Risk Sensitivity Analysis

The Fund recognises that interest rates can vary and can affect both income to the Fund and the value of the net assets available to pay benefits. A 100 basis point (BPS) movement in interest rates is consistent with the level of sensitivity applied as part of the Fund's risk management strategy. The Fund's long term average rates are expected to move less than 100 basis points from one year to the next and experience suggests that such movements are likely.

The analysis that follows assumes that all other variables, in particular exchange rates, remain constant, and shows the effect in the year on the net assets available to pay benefits of a +/- 100 BPS change in interest rates:

Asset Type	**Carrying Amount as at 31 March 2018**	**Change in Year in the Net Assets available to Pay Benefits**	
		+ 100 BPS	**- 100 BPS**
	£'000	**£'000**	**£'000**
Cash and Cash Equivalents	113,484	114,619	112,349
Cash Balances	19	19	19
Fixed Interest Securities	472,041	476,761	467,321
Total Change in Assets Available	**585,544**	**591,399**	**579,689**

Asset Type	Carrying Amount as at 31 March 2017	Change in Year in the Net Assets available to Pay Benefits	
		+ 100 BPS	- 100 BPS
	£'000	£'000	£'000
Cash and Cash Equivalents	58,334	58,917	57,751
Cash Balances	78	79	77
Fixed Interest Securities	481,694	486,511	476,877
Total Change in Assets Available	**540,106**	**545,507**	**534,705**

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 Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Fund (£UK). The Fund holds both monetary and non-monetary assets denominated in currencies other than £UK.

The Fund's currency rate risk is routinely monitored by the Fund in accordance with the Fund's risk management strategy, including monitoring the range of exposure to currency fluctuations.

The following table summarises the Fund's currency exposure as at 31 March 2018 and as at the previous period end:

Currency Exposure – Asset Type	Asset Value as at 31 March 2017	Asset Value as at 31 March 2018
	£'000	£'000
Overseas Quoted Securities	694,350	819,078
Overseas Unquoted Securities	203,627	206,396
Overseas Unit Trusts	583,947	636,218
Overseas Public Sector Bonds (Quoted)	115,574	0
Overseas Corporate Bonds (Quoted)	48,297	0
Overseas Global Pooled Bonds	0	118,660
Total Overseas Assets	**1,645,795**	**1,780,352**

Currency Risk – Sensitivity Analysis

Following analysis of historical data in consultation with the Fund's investment advisors, the Fund considers the likely volatility associated with foreign exchange rate movements to be 11.6%.

This analysis assumes that all other variables, in particular interest rates, remain constant.

An 11.6% strengthening/weakening of the pound against the various currencies in which the Fund holds investments would increase/decrease the net assets to pay benefits as shown below:

Currency Exposure – Asset Type	**Asset Value as at 31 March 2018**	**Change to Net Assets**	**Change to Net Assets**
		+11.6%	**-11.6%**
	£'000	**£'000**	**£'000**
Overseas Quoted Securities	819,078	914,091	724,065
Overseas Unquoted Securities	206,396	230,338	182,454
Overseas Unit Trust	636,218	710,019	562,417
Overseas Public Sector Bonds (Quoted)	0	0	0
Overseas Corporate Bonds (Quoted)	0	0	0
Overseas Global Pooled Bonds	118,660	132,425	104,895
Total Change in Assets Available	**1,780,352**	**1,986,873**	**1,573,831**

Currency Exposure – Asset Type	**Asset Value as at 31 March 2017**	**Change to Net Assets**	**Change to Net Assets**
		+11.7%	**-11.7%**
	£'000	**£'000**	**£'000**
Overseas Quoted Securities	694,350	775,589	613,111
Overseas Unquoted Securities	203,627	227,451	179,803
Overseas Unit Trust	583,947	652,269	515,625
Overseas Public Sector Bonds (Quoted)	115,574	129,096	102,052
Overseas Corporate Bonds (Quoted)	48,297	53,948	42,646
Total Change in Assets Available	**1,645,795**	**1,838,353**	**1,453,237**

Credit Risk

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

Deposits are not made with banks and financial institutions unless they are rated independently and meet the Fund's credit criteria. The Local Government Pension Scheme investment regulations have limits as to the maximum percentage of the deposits placed with any one class of financial institution. Money market fund deposits are made through the Funds' Global Custodian and are evaluated according to their internal criteria.

Deposits made to the Aberdeen City Council (ACC) loans fund are administered within the City Council treasury policy.

The Fund believes it has managed its exposure to credit risk and has had no experience of default or uncollectable deposits. The Fund's cash holding at 31 March 2018 was £113,503,000 (31 March 2017 £58,412,000). This was held with the following institutions as shown below:

Summary	**Rating**	**Balance as at 31 March 2017**	**Balance as at 31 March 2018**
		£'000	**£'000**
Bank Deposit Accounts			
ACC Loans Fund Deposit	N/A	39,740	22,780
BNP Paribas	AAAm	18,594	90,704
Subtotal		**58,334**	**113,484**
Bank Current Accounts			
Clydesdale Bank	BBB+	78	19
Total		**58,412**	**113,503**

Liquidity Risk

Liquidity risk represents the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund ensures that it has adequate cash resources to meet its commitments. The Fund has immediate access to its cash holdings at all times.

The Fund defines liquid assets as assets that can be converted to cash within three months. Illiquid assets are those assets which will take longer than three months to convert into cash. As at 31 March 2018 the value of illiquid assets was £525,505,096 which represented 12.7% of the total fund assets (31 March 2017 £479,795,433 which represented 12.6% of the total fund assets).

Note 18: Breakdown of Long Term and Current Assets and Liabilities

	31 March 2017	31 March 2018
	£'000	**£'000**
Long Term Assets	**78**	**33**
Current Assets		
Employees' Contributions due	2,395	2,329
Employers' Contributions due	7,115	7,367
Sundry Debtors	7,440	5,109
	16,950	**14,805**
Bank	78	19
Total Current Assets	**17,028**	**14,824**
Total Long Term and Current Assets	**17,106**	**14,857**

Analysis of Assets (Debtors only)*	**31 March 2017**	**31 March 2018**
	£'000	**£'000**
Long Term Assets		
Other Entities and Individuals	**78**	**33**
Central Government Bodies	1,202	193
Other Local Authorities	8,686	8,773
Other Entities and Individuals	7,062	5,839
Total Current Assets*	**16,950**	**14,805**
Total Long Term and Current Assets	**17,028**	**14,838**

*The above is an analysis of debtors only and does not include the Bank.

	31 March 2017	**31 March 2018**
Current Liabilities	**£'000**	**£'000**
Sundry Creditors	16,000	19,245
Benefits Payable	7,046	7,713
Total Current Liabilities	**23,046**	**26,958**

Analysis of Liabilities	**31 March 2017**	**31 March 2018**
	£'000	**£'000**
Central Government Bodies	1,040	1,606
Other Local Authorities	263	760
Other Entities and Individuals	21,743	24,592
Total Current Liabilities	**23,046**	**26,958**

Note 19: Related Party Transactions

Aberdeen City Council provides administration services for the Pension Funds, the costs of which are reimbursed by the Funds.

The costs of these services for the North East Scotland Pension Fund amounted to £1,388,413 (2016/17 £1,214,654).

Prior to the remittance of excess cash to the investment fund managers, surplus cash is invested as a temporary loan with the Council. At the year end this amounted to £22,780,000 (2016/17 £39,740,000) for the North East Scotland Pension Fund.

Interest was received from the Council of £36,330 (2016/17 £86,124) for the North East Scotland Pension Fund.

Note 20: Key Management Personnel

Certain employees of Aberdeen City Council hold key positions in the financial management of the North East Scotland Pension Fund. One employee was identified and his financial relationship with the Fund (expressed as an accrued pension) is set out below:

		Accrued Pension 2016/2017	**Accrued Pension 2017/2018**
		£'000	**£'000**
Steven Whyte	Director of Resources	26	30

Governance

As at 31 March 2018, 8 members of the Pensions Committee and 6 members of the Pension Board were active members or pensioners of the North East Scotland Pension Fund.

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

In 2017/18, Elected Members' had interests in Sport Aberdeen, Aberdeen Performing Arts and Aberdeen International Youth Festival.

Note 21: Contractual Commitments as at 31 March 2018

As at 31 March 2018 the NESPF had contractual commitments in respect of Private Equity and Global Real Estate portfolios;

	Contractual Commitments	Undrawn Commitments
	£'000	£'000
HarbourVest	153,374	40,163
Standard Life	127,570	23,201
Partners Group	88,628	30,217
Maven (SLF)	6,444	181
Capital Dynamics	60,000	45,740
RCP Advisors	32,101	23,327
Unigestion	57,038	46,064
AAM Residential Property	30,000	22,398
Total	**555,155**	**231,291**

Note 22: Additional Voluntary Contributions (AVC)

Additional Voluntary Contributions are not included in the Pension Funds' Accounts.

Members of the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund are included in the following tables. Standard Life and the Prudential do not provide this information by Fund.

The amount of additional voluntary contributions paid by members during the year is shown as income in the table below:

2016/2017		Income (AVCs Paid by Members)		2017/2018
£'000				£'000
51		Standard Life		32
2,203		Prudential		2,653

The closing net assets values represent the value of the separately invested additional voluntary contributions. These closing values are subject to revaluation.

Market Value		Additional Voluntary Contributions		Market Value
31 March 2017				31 March 2018
£'000				£'000
1,720		Standard Life		1,580
24,666		Prudential		25,267

Note 23: Contingent Assets/Liabilities

The North East Scotland Pension Fund holds three insurance bonds and one cash bond. These bonds guard against the possibility of being unable to recover pension liabilities from these admission bodies should they terminate their participation in the scheme. These bonds are drawn in the favour of the Pension Fund and payment will only be triggered in the event of employer default. Previously, one further insurance bond was held for an employer, however, following a termination event where the liabilities were subsumed by another employer, therefore, rendering this bond no longer valid.

The pension liabilities for all Transferee Admission Bodies are guaranteed by the originating employer as per Regulation 62 of the Local Government Pension Scheme (Scotland) Regulations 2014. In total, the Fund has secured guarantees for 25 Community Admission Bodies and Transferee Admission Bodies.

Note 24: Impairment for Bad and Doubtful Debts

The risk of employers being unable to meet their pension obligations is managed through the NESPF Termination Policy and the NESPF Employer Covenant Assessment Policy. As at 31 March 2018 the Fund recognises that there are three employers who have exited from the Fund where payment of the termination fee may not be recovered in full. A termination fee of £211,900 has been registered with the company liquidator, one fee of £130,664 will be settled upon wind up of the admission body and the Fund is currently in discussions with one other employer regarding an amount of £452,000.

The above amounts have not been included within the Annual Accounts, as the extent of the impairment is unknown.

Note 25: Investment Principles

A summary of the Statement of Investment Principles is available on our website www.nespf.org.uk. A full version of the Statement of Investment Principles is available on request from Director of Resources, Aberdeen City Council, Resources, Level 1 West, Business Hub 7, Marischal College, Broad Street, Aberdeen, AB10 1AB.

The Statement of Investment Principles is reviewed on an annual basis by the Pensions Committee and in light of any change to the investment strategies of the Pension Funds.

Note 26: Critical Judgements in applying Accounting Policies

Assumptions made about the future and other major sources of estimation uncertainty.

The items in the net asset statement at 31 March 2018 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

Item	Uncertainties	Effect if Actual Results Differ from Assumption
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.	The methodology used by the Scheme Actuary is in line with accepted guidelines. Further to the Fund's liability being calculated every three years, an update of the funding position is calculated by the Scheme Actuary every 3 months. Further information can be found in note 1.
Private Equity	Private equity investments are valued at fair value in accordance with International Private Equity and Venture Capital Valuation guidelines. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total private equity investments in the Annual Accounts are £232 million. There is a risk that this investment may be under or overstated in the accounts.

Note 27: Events after the Balance Sheet Date

The draft Statement of Accounts was authorised for issue by the Director of Resources on 22 June 2018, and the audited accounts were issued by the Chief Officer - Finance on 14 September 2018. Events taking place after this date are not reflected in the Annual Accounts or Notes. Where events taking place before this date provided information about conditions existing at 31 March 2018, the figures in the Annual Accounts and Notes have been adjusted in all material respects to reflect the impact of this information. No such adjustments have been required.

At the time of publication there were no material post balance sheet events to report, the Fund continues to implement the approved Investment Strategy and has initiated some of the agreed changes post year end.

Global Custody services post year end are provided by HSBC following transition from BNPP on 2 April 2018.

Note 28: Agency Arrangements for Administering Compensatory 'Added' Years

The North East Scotland Pension Fund administers compensatory 'added' years payments for those awarded up to 2011. The Fund acts as an agent of employing bodies, in respect of staff that have had their pension augmented under *The Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998.*

The cash flows in respect of the relevant employing bodies and associated payroll cost for those compensatory 'added' years' payments are:

	2016/17	2017/18
	£'000	**£'000**
Cost incurred/recovered on behalf of:		
Aberdeen City Council	2,331	2,317
Aberdeenshire Council	1,357	1,341
Moray Council	710	703
Scottish Water	1,262	1,261
Other	298	303
Total	**5,958**	**5,925**
Associated Payroll Cost	**4**	**4**

Note 1: Actuarial Valuation Report

An Actuarial Report for the Transport Fund was provided as at 31 March 2017. Information from the 2017 Actuarial Valuation is detailed below:

Market Value of Assets at Valuation	£100,000,000
Liabilities	£106,500,000
Deficit	£ 6,500,000

Funding Level

The Level of Funding in Terms of the Percentage of Assets available to meet Liabilities	94%

Addressing the Shortfall

The funding objective as set out in the Funding Strategy Statement is to achieve and maintain a funding level of 100% of liabilities (the funding target). In line with the Funding Strategy Statement, where a shortfall exists at the effective date of the valuation a deficit recovery plan will be put in place which requires additional contributions to correct the shortfall.

The average employer cost of providing members benefits (the Primary contribution rate) has been determined as 58.5% of pensionable pay. The Fund have agreed following a consultation with First Aberdeen Limited that the contribution requirement would be set at the same level as the previous valuation of 33% plus £1.5m per annum. This means that the payment towards the deficit will be around £1.1m allowing for the deficit to be recovered over 5 years.

Total Contribution Rate	**2018/19**	**2019/20**	**2020/21**
(as percentage of payroll)	33% plus £1,500,000	33% plus £1,500,000	33% plus £1,500,000

Within the FSS there is the option for the Fund to reassess the contribution requirement for First Aberdeen upon reaching a funding level of 105%.

Contribution requirements for the period from 1 April 2021 onwards will be revised as part of the next actuarial valuation as at 31 March 2020 and will be confirmed in the Rates and Adjustments Certificate and Schedule accompanying that valuation report.

Assumptions Used to Calculate Funding Target

Pre-retirement	1.6% p.a
Assumed Long Term Price Inflation (CPI)	2.9% p.a
Salary Increases – Long term	3.4% p.a
Salary Increases – Short term	2.9% p.a (to 31 March 2018)
Pension Increases in Payment	2.9% p.a

The Transport Fund used the Attained Age method for the employing body First Aberdeen, to reflect that this scheme was closed to new entrants from 31 March 1994.

The full Actuarial Report and the Funding Strategy Statement for the Fund is available from the office of the Director of Resources, Aberdeen City Council, Resources, Level 1 West, Business Hub 7, Marischal College, Broad Street, Aberdeen, AB10 1AB.

Actuarial Statement

The Scheme Actuary has provided a statement describing the funding arrangements of the Fund.

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standards 26 (IAS 26) assumptions, is estimated to be £78.0m (2017 £85.6m). The figure is used for the statutory accounting purposes by Aberdeen City Council Transport Fund and complies with the requirements of IAS 26.

The figure is only prepared for the purposes of IAS 26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

The full statement by the Consulting Actuary can be found in Appendix 1.

Note 2: Contributions Receivable

	2016/17	2017/18
	£'000	**£'000**
Employees' Normal Contributions	**115**	**100**
Employer's Normal Contributions	609	528
Employer's Deficit Recovery Contributions	1,500	1,500
Total Employer's Contributions	**2,109**	**2,028**
Total	**2,224**	**2,128**

	2016/17	2017/18
	£'000	**£'000**
Scheduled Body	2,224	2,128
Total	**2,224**	**2,128**

Note 3: Benefits Payable

	2016/17	2017/18
	£'000	**£'000**
Pensions	3,083	3,210
Commutation and Lump Sum Retirement Benefits	802	914
Lump Sum Death Benefits	80	2
Total	**3,965**	**4,126**

	2016/17	2017/18
	£'000	**£'000**
Scheduled Body	3,965	4,126
Total	**3,965**	**4,126**

Note 4: Payment to and on Account of Leavers

	2016/17	2017/18
	£'000	**£'000**
Individual Transfers	65	0
Total	**65**	**0**

Note 5: Management Expenses

	2016/17 £'000	2017/18 £'000
Pension Fund Staffing Costs – Administration	29	32
Support Services including IT	20	18
Printing and Publications	1	1
Administration Expenses Total	**50**	**51**
Pension Fund Staffing Costs – Investment	4	6
Pension Fund Committee	4	1
External Audit Fee	1	1
Actuarial Fees	26	61
General Expenses	3	3
Oversight and Governance Expenses Total	**38**	**72**
Investment Management	154	825
Custody Fees	3	43
Investment Management Expenses Total	**157**	**868**
Management Expenses Grand Total	**245**	**991**

Note 6: Investment Income

	2016/17 £'000	2017/18 £'000
Fixed Interest Securities	147	687
Pooled Investments	0	95
Interest on Cash Deposit	2	3
Other (including P/L from Currency and Derivatives)	1,356	27
Total	**1,505**	**812**
Tax -		
Withholding Tax – Fixed Interest Securities	0	0
Withholding Tax – Pooled	0	0
Total Tax	**0**	**0**
Net Total	**1,505**	**812**

Note 7: Investment Assets

Reconciliation of Movements in Investments and Derivatives

	Market Value 31 March 2017	Purchases	Sales	Change in Market Value	Market Value 31 March 2018
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Fixed Interest	7,527	0	(6,313)	(97)	1,117
UK Equities	0	0	0	0	0
Pooled Investments	88,705	32,608	(26,312)	2,059	97,060
	96,232	**32,608**	**(32,625)**	**1,962**	**98,177**
Cash	3,638				1,621
Net Investment Assets	**99,870**				**99,798**

	Market Value 31 March 2016	Purchases	Sales	Change in Market Value	Market Value 31 March 2017
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Fixed Interest	37,135	41,400	(75,237)	4,229	7,527
UK Equities	0	0	(87)	87	0
Pooled Investments	48,304	101,119	(70,351)	9,633	88,705
	85,439	**142,519**	**(145,675)**	**13,949**	**96,232**
Cash	385				3,638
Net Investment Assets	**85,824**				**99,870**

Note 8: Analysis of Investments

	2016/17	2017/18
Fixed Interest Securities	**£'000**	**£'000**
UK		
Public Sector Quoted	**7,527**	**1,117**
Pooled Funds – Additional Analysis		
UK		
Fixed Income	33,761	38,126
Unit Trusts	23,364	25,629
Overseas		
Unit Trusts	31,580	33,305
Subtotal Pooled Funds	**88,705**	**97,060**
Cash Deposits	3,638	1,621
Investment Assets Total	**99,870**	**99,798**
Investment Liabilities Total	**0**	**0**
Net Investment Assets	**99,870**	**99,798**

Note 9: Investments Analysed by Fund Manager

Investment Assets	31 March 2017	%	31 March 2018	%
	£'000		£'000	
Schroders	99,550	99.7	99,627	99.8
ACC Loans Fund Deposit	320	0.3	171	0.2
Net Investment Assets	**99,870**	**100.0**	**99,798**	**100.0**

The following investments represent more than 5% of the Net Investment Assets:

Security	Market Value 31 March 2017	% of Net Investment Assets	Market Value 31 March 2018	% of Net Investment Assets
	£'000		£'000	
Blackrock Asset Management UK Aquila Life Currency World Ex UK Equity	14,350	14.4	15,768	15.8
SIF Diversified Completion CLS P Accumulation	10,697	10.7	10,584	10.6
Schroder Investment Management Lux Spec Sits STG Liquidity	4,193	4.2	5,540	5.6
Schroder Matching Plus Synthetic Index Linked Gilt Fund	6,383	6.4	8,352	8.4
SSGA Lux MG GL Treasury Bond Index GBP	11,518	11.5	11,645	11.7
Vanguard Investment Series Global Stock Index FD-INST USD SHS	13,762	13.8	13,879	13.9
Vanguard Investment Series US Investment Grade Cred Index ACC NAV	12,667	12.7	15,045	15.1

Note 10: Stock Lending

Stock Lending is the lending of stock from one investor to another that entitles the lender to continue to receive income generated by the stock plus an additional payment by the borrower.

Collateral is held at a minimum of 105% in respect of each borrower, consisting of UK and Overseas Gilts, UK Equities, Certificates of Deposit and Letters of Credit.

There was no stock lending in operation as at 31 March 2018.

Note 11: Financial and Non-Financial Instruments

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

31 March 2017				31 March 2018		
Designated as Fair Value Through Profit & Loss	Loans and Receivables	Financial Liabilities at Amortised Cost		Designated as Fair Value Through Profit & Loss	Loans and Receivables	Financial Liabilities at Amortised Cost
£'000	£'000	£'000		£'000	£'000	£'000
			Financial Assets			
7,527			Fixed Interest	1,117		
88,705			Pooled	97,060		
	3,638		Cash		1,621	
	530		Debtors		638	
96,232	**4,168**	**0**	**Subtotal**	**98,177**	**2,259**	**0**
			Financial Liabilities			
		(434)	Creditors			(365)
96,232	**4,168**	**(434)**		**98,177**	**2,259**	**(365)**
		99,966	**Financial Instruments Total**			**100,071**
0			**Non-Financial Instruments**	**0**		
96,232	**4,168**	**(434)**		**98,177**	**2,259**	**(365)**
		99,966	**Net Assets of the Fund**			**100,071**

Note 12: Net Gains and Losses on Financial and Non-Financial Instruments

31 March 2017		31 March 2018
£'000	**Financial Assets**	**£'000**
13,949	Fair Value through Profit and Loss	1,962
0	**Financial Liabilities**	0
13,949	**Net Gains and Losses on Financial Instruments**	**1,962**
0	**Non-Financial Instruments**	**0**
13,949	**Net Gains and Losses of the Fund**	**1,962**

Note 13: Valuation of Financial and Non-Financial Instruments carried at Fair Value

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

Level 1

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

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

Level 2

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

Level 3

Financial instruments at level 3 are those where at least one input that could have a significant effect on the instruments valuation is not based on observable market data.

Such instruments would include unquoted equity investments and hedge fund of funds, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investment in private equity are based on valuations provided by the general partners to the private equity funds in which the Aberdeen City Council Transport Fund has invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which follow the valuation principles of IFRS and US GAAP. Valuations are usually undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

The following table provides an analysis of the financial assets and liabilities of the Pension Fund grouped into Levels 1 to 3, based on the level at which the fair values is observable.

Non-Financial instruments have been added to the table for reconciliation to the Net Assets of the Fund.

Note 13A: Fair Value – Basis of Valuation

The basis of the valuation of each class of investment asset is set out below. There have been no changes in the valuation techniques used during the year. All assets have been valued using fair value techniques which represent the highest and best price available at the reporting date.

Description of Asset	Valuation Hierarchy	Basis of Valuation	Observable and Unobservable Inputs	Key Sensitivities affecting the Valuations provided
Market Quoted Investments	Level 1	Published bid market price ruling on the final day of the accounting period	Not required	Not required
Quoted Bonds	Level 1	Fixed interest securities are valued at a market value based on current yields	Not required	Not required
Futures and Options in UK Bonds	Level 1	Published exchange prices at the year-end	Not required	Not required
Exchange Traded Pooled Investments	Level 1	Closing bid value on published exchanges	Not required	Not required
Unquoted Bonds	Level 2	Average of broker prices	Evaluated price feeds	Not required
Forward Foreign Exchange Derivatives	Level 2	Market forward exchange rates at the year-end	Exchange rate risk	Not required
Overseas Bond Options	Level 2	Option pricing model	Annualised volatility of counterpart credit risk	Not required
Pooled Investments – Overseas Unit Trusts and Property Funds	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 Investments – Hedge Funds	Level 3	Closing bid price where bid and offer prices are published.	NAV-based pricing set on a forward pricing basis	Valuations could be affected by material events occurring between

		Closing single price where single price published		the date of the financial statements provided and the pension fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts
Freehold and Leasehold Properties	Level 3	Valued at fair value at the year –end using the investment method of valuation by Paul Willis Bsc (Hons) MRICS of Colliers International in accordance with the *RICS Valuation Professional Standard*	Existing lease terms and rentals Independent market research Nature of tenancies Covenant strength for existing tenants Assumed vacancy levels Estimated rental growth Discount rate	
Unquoted Equity	Level 3	Comparable valuation of similar companies in accordance with *International Private Equity and Venture Capital Valuation Guidelines* (2012)	EBITDA multiple Revenue multiple Discount for lack of marketability Control premium	Valuations could be affected by material events occurring between the date of the financial statements provided and the pension fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts

	Quoted Market Price	Using Observable Inputs	With Significant Unobservable Inputs	
Values at 31 March 2018	**Level 1**	**Level 2**	**Level 3**	**Total**
	£'000	**£'000**	**£'000**	**£'000**
Financial Assets				
Financial Assets at Fair Value through Profit and Loss	98,177	0	0	98,177
Loans and Receivables	2,259	0	0	2,259
Total Financial Assets	**100,436**	**0**	**0**	**100,436**
Financial Liabilities				
Financial Liabilities at Amortised Cost	(365)	0	0	(365)
Total Financial Liabilities	**(365)**	**0**	**0**	**(365)**
Total Financial Instruments	**100,071**	**0**	**0**	**100,071**
Non-Financial Instruments	**0**	**0**	**0**	**0**
Net Assets of the Fund	**100,071**	**0**	**0**	**100,071**

	Quoted Market Price	Using Observable Inputs	With Significant Unobservable Inputs	
Values at 31 March 2017	**Level 1**	**Level 2**	**Level 3**	**Total**
	£'000	**£'000**	**£'000**	**£'000**
Financial Assets				
Financial Assets at Fair Value through Profit and Loss	96,232	0	0	96,232
Loans and Receivables	4,168	0	0	4,168
Total Financial Assets	**100,400**	**0**	**0**	**100,400**
Financial Liabilities				
Financial Liabilities at Amortised Cost	(434)	0	0	(434)
Total Financial Liabilities	**(434)**	**0**	**0**	**(434)**
Total Financial Instruments	**99,966**	**0**	**0**	**99,966**
Non-Financial Instruments	**0**	**0**	**0**	**0**
Net Assets of the Fund	**99,966**	**0**	**0**	**99,966**

Note 13B: Transfers between Levels 1 and 2
There were no transfers between level 1 and 2.

Note 13C: Reconciliation of Fair Value Measurements within Level 3

There are no Fair Value Measurements at Level 3 within the ACC Transport Fund. Therefore, no reconciliation is required.

Note 13D: Sensitivity of Assets Valued at Level 3

There are no assets valued at Level 3 within the ACC Transport Fund. Therefore, no sensitivity analysis is required.

Note 14: Risk arising from Financial and Non-Financial Instruments

The Fund's primary long term risk is that the Fund's 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 Fund and to maximise the opportunity for gains across the whole Fund portfolio.

The 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 Fund manages its liquidity risk, ensuring there is sufficient liquidity to meet the Fund's forecast cash flows.

The Fund manages these investment risks as part of its overall Pension Fund Risk Management Strategy.

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

Market Risk

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

The objective of the 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 industry sectors and individual securities.

Specific risk exposure is limited by applying risk weighted maximum exposures to individual investments.

Other Price Risk – Sensitivity Analysis

Following analysis of historical data and expected investment return movement during the financial year and in consultation with the Fund's Investment Advisor, the Fund has determined that the following movements in market price risk are reasonably possible for the 2017/18 reporting period.

Asset Type	Potential Market Movements (+/-)
Cash	1.0%
UK Bonds	5.6%
Overseas Bonds	5.6%
UK Equities	16.0%
Overseas Equities	20.5%
Pooled - Diversified Growth Funds (DGF)	12.0%

The potential price changes disclosed above are broadly consistent with a one standard deviation movement in the value of the assets. The sensitivities are consistent with the assumptions contained in the Scheme Actuary's most recent review. This analysis assumes that all other variables, in particular foreign currency exchange rates and interest rates, remain the same.

Had the market price of the 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 follows (the prior year comparator is shown below).

Non-Financial instruments have been added to the table for reconciliation to the Net Investment Assets.

Asset Type	Value as at 31 March 2018	Percentage Change	Value on Increase	Value on Decrease
	£'000	**%**	**£'000**	**£'000**
Cash and Cash Equivalents	1,621	1.0	1,637	1,605
Investment Portfolio Assets				
UK Bonds	39,243	5.6	41,441	37,045
UK Equities	15,045	16.0	17,452	12,638
Overseas Equities	33,305	20.5	40,132	26,478
Pooled – DGF	10,584	12.0	11,854	9,314
Total Financial Instruments	**99,798**		**112,516**	**87,080**
Non-Financial Instruments	**0**	N/A	**0**	**0**
Total Assets Available to Pay Benefits	**99,798**		**112,516**	**87,080**

Asset Type	Value as at 31 March 2017	Percentage Change	Value on Increase	Value on Decrease
	£'000	**%**	**£'000**	**£'000**
Cash and Cash Equivalents	3,638	1.1	3,678	3,598
Investment Portfolio Assets				
UK Bonds	41,288	5.5	43,559	39,017
UK Equities	12,667	16.0	14,694	10,640
Overseas Equities	31,580	20.5	38,054	25,106
Pooled – DGF	10,697	12.0	11,981	9,413
Total Financial Instruments	**99,870**		**111,966**	**87,774**
Non-Financial Instruments	**0**	N/A	**0**	**0**
Total Assets Available to Pay Benefits	**99,870**		**111,966**	**87,774**

Interest Rate Risk

The Fund invests in financial assets for the primary purpose of obtaining a return on investments. These investments are subject to interest rate risks which represents the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Fund's interest rate risk is routinely monitored by the Fund in accordance with the Fund's risk management strategy, including monitoring the exposure to interest rates and assessment of actual interest rates against the relevant benchmarks.

The Fund's direct exposure to interest rate movements as at 31 March 2016 and 31 March 2017 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value:

Asset type	As at 31 March 2017	As at 31 March 2018
	£'000	**£'000**
Cash and Cash Equivalents	3,638	1,621
Cash Balances	2	1
Fixed Interest Securities	41,288	39,243
Total	**44,928**	**40,865**

Interest Rate Risk Sensitivity Analysis

The Fund recognises that interest rates can vary and can affect both income to the Fund and the value of the net assets available to pay benefits. A 100 basis point (BPS) movement in interest rates is consistent with the level of sensitivity applied as part of the Fund's risk management strategy. The Fund's long term average rates are expected to move less than 100 basis points from one year to the next and experience suggests that such movements are likely.

The analysis that follows assumes that all other variables, in particular exchange rates, remain constant, and shows the effect in the year on the net assets available to pay benefits of a +/- 100 BPS change in interest rates:

Asset Type	Carrying Amount as at 31 March 2018	Change in Year in the Net Assets Available to Pay Benefits	
		+ 100 BPS	**- 100 BPS**
	£'000	**£'000**	**£'000**
Cash and Cash Equivalents	1,621	1,637	1,605
Cash Balances	1	1	1
Fixed Interest Securities	39,243	39,635	38,851
Total Change in Assets Available	**40,865**	**41,273**	**40,457**

Asset Type	Carrying Amount as at 31 March 2017	Change in Year in the Net Assets Available to Pay Benefits	
		+ 100 BPS	- 100 BPS
	£'000	£'000	£'000
Cash and Cash Equivalents	3,638	3,674	3,602
Cash Balances	2	2	2
Fixed Interest Securities	41,288	41,701	40,875
Total Change in Assets Available	**44,928**	**45,377**	**44,479**

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 Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Fund (£UK). The Fund holds both monetary and non-monetary assets denominated in currencies other than £UK.

The Fund's currency rate risk is routinely monitored by the Fund in accordance with the Fund's risk management strategy, including monitoring the range of exposure to currency fluctuations.

The following table summarises the Fund's currency exposure as at 31 March 2018 and as at the previous period end:

Currency Exposure – Asset Type	Asset Value as at 31 March 2017	Asset Value as at 31 March 2018
	£'000	£'000
Overseas Unit Trusts	31,580	33,305
Total Overseas Assets	**31,580**	**33,305**

Currency Risk – Sensitivity Analysis

Following analysis of historical data in consultation with the Fund's investment advisors, the Fund considers the likely volatility associated with foreign exchange rate movements to be 11.6%.

This analysis assumes that all other variables, in particular interest rates, remain constant.

An 11.6% strengthening/weakening of the pound against the various currencies in which the Fund holds investments would increase/decrease the net assets to pay benefits as follows:

Currency Exposure – Asset Type	Asset Value as at 31 March 2018	Change to Net Assets	Change to Net Assets
		+11.6%	**-11.6%**
	£'000	**£'000**	**£'000**
Overseas Unit Trust	33,305	37,168	29,442
Total Change in Assets Available	**33,305**	**37,168**	**29,442**

Currency Exposure – Asset Type	Asset Value as at 31 March 2017	Change to Net Assets	Change to Net Assets
		+11.7%	**-11.7%**
	£'000	**£'000**	**£'000**
Overseas Unit Trust	31,580	35,275	27,885
Total Change in Assets Available	**31,580**	**35,275**	**27,885**

Credit Risk

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

Deposits are not made with banks and financial institutions unless they are rated independently and meet the Fund's credit criteria. The Local Government Pension Scheme investment regulations have limits as to the maximum percentage of the deposits placed with any one class of financial institution. Money market fund deposits are made through the Funds' Global Custodian and are evaluated according to their internal criteria.

Deposits made to the Aberdeen City Council (ACC) loans fund are administered within the Aberdeen City Council treasury policy.

The Fund believes it has managed its exposure to credit risk, and has had no experience of default or uncollectable deposits. The Fund's cash holding at 31 March 2018 was £1,622,000 and at 31 March 2017 £3,640,000. This was held with the following institutions:

Summary	Rating	Balance as at 31 March 2017	Balance as at 31 March 2018
		£’000	**£’000**
Bank Deposit Accounts			
ACC Loans Fund Deposit	N/A	320	171
BNP Paribas	AAAm	3,318	1,450
Subtotal		**3,638**	**1,621**
Bank Current Accounts			
Clydesdale Bank	BBB+	2	1
Total		**3,640**	**1,622**

Liquidity Risk

Liquidity risk represents the risk that the Fund will not be able to meet its financial obligations as they fall due. The Fund ensures that it has adequate cash resources to meet its commitments. The Fund has immediate access to its cash holdings at all times.

The Fund defines liquid assets as assets that can be converted to cash within three months. Illiquid assets are those assets which will take longer than three months to convert in to cash. As at 31 March 2018 the value of illiquid assets was £0 which represented 0% of the total fund assets (31 March 2017 £0 which represented 0% of the total fund assets).

Note 15: Breakdown of Long Term and Current Assets and Liabilities

	31 March 2017	31 March 2018
	£'000	**£'000**
Long Term Assets	**350**	**324**
Employees' Contributions due	3	2
Employer's Contributions due	16	11
Sundry Debtors	159	300
	178	**313**
Bank	2	1
Total Current Assets	**180**	**314**
Total Long Term and Current Assets	**530**	**638**

Analysis of Assets (Debtors Only)*	**31 March 2017**	**31 March 2018**
	£'000	**£'000**
Central Government Bodies	350	324
Total Long Term Assets	**350**	**324**
Central Government Bodies	31	48
Other Entities and Individuals	147	265
Total Current Assets*	**178**	**313**
Total Long Term and Current Assets	**528**	**637**

*The above is an analysis of Debtors only and does not include the Bank

	31 March 2017	**31 March 2018**
Current Liabilities	**£'000**	**£'000**
Sundry Creditors	305	232
Benefits Payable	129	133
Total Current Liabilities	**434**	**365**

Analysis of Liabilities	**31 March 2017**	**31 March 2018**
	£'000	**£'000**
Other Entities and Individuals	434	365
Total Current Liabilities	**434**	**365**

Note 16: Related Party Transactions

Aberdeen City Council provides administration services for the Pension Funds, the costs of which are reimbursed by the Funds.

The cost of these services for the Aberdeen City Council Transport Fund was £42,941 (2016/17 - £37,567).

Prior to the remittance of excess cash to the Investment fund managers, surplus cash is invested as a temporary loan with the Council. At the year end this amounted to £171,000 (2016/17 - £320,000) for the Aberdeen City Council Transport Fund.

Interest was received from the Council of £674 (2016/17 - £1,265) for the Aberdeen City Council Transport Fund.

Note 17: Key Management Personnel

Certain employees of Aberdeen City Council hold key positions in the financial management of the Aberdeen City Council Transport Fund. However they are not members of the Aberdeen City Council Transport Fund.

Note 18: Investment Principles

A summary of the Statement of Investment Principles is available on the Pension Fund's website www.nespf.org.uk. A full version of the Statement of Investment Principles is available on request from Director of Resources, Aberdeen City Council, Resources, Level 1 West, Business Hub 7, Marischal College, Broad Street, Aberdeen, AB10 1AB.

The Statement of Investment Principles is reviewed on an annual basis by the Pensions Committee and in the light of any change to the investment strategy of the Pension Funds.

Note 19: Critical Judgements in applying Accounting Policies

Assumptions made about the future and other major sources of estimation uncertainty.

The items in the net asset statement at 31 March 2018 for which there is a significant risk of material adjustment in the forthcoming financial year are shown below:

Item	Uncertainties	Effect if Actual Results Differ from Assumption
Actuarial present value of 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.	The methodology used by the Scheme Actuary is in line with accepted guidelines. Further to the Fund's liability being calculated every three years, an update of the funding position is calculated by the Scheme Actuary every 3 months. Further information can be found in note 1.

Note 20: Events after the Balance Sheet Date

The draft Statement of Accounts was authorised for issue by the Director of Resources on 22 June 2018, and the audited accounts were issued by the Chief Officer - Finance on 14 September 2018. Events taking place after this date are not reflected in the Annual Accounts or Notes. Where events taking place before this date provided information about conditions existing at 31 March 2018, the figures in the Annual Accounts and Notes have been adjusted in all material respects to reflect the impact of this information. No such adjustments have been required.

At the time of publication there were no material post balance sheet event to report, the Fund continues to implement the approved De-Risking Investment Strategy.

Global Custody services post year end are provided by HSBC following transition from BNPP on the 2 April 2018.

Independent Auditor’s Report

Independent auditor’s report to the members of Aberdeen City Council as administering authority for the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund and to the Accounts Commission

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 120 of the Code of Audit Practice approved by the Accounts Commission, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Report on the audit of the financial statements

Opinion on financial statements

I certify that I have audited the financial statements in the annual report of the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund (the Funds) for the year ended 31 March 2018 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Fund Accounts, the Net Assets Statements and Notes to the Pension Fund Accounts, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 (the 2017/18 Code).

In my opinion the accompanying financial statements:

- give a true and fair view in accordance with applicable law and the 2017/18 Code of the financial transactions of the funds during the year ended 31 March 2018 and of the amount and disposition at that date of their assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2017/18 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Basis for opinion

I conducted my audit in accordance with applicable law and International Standards on Auditing (UK) (ISAs (UK)). My responsibilities under those standards are further described in the auditor’s responsibilities for the audit of the financial statements section of my report. I am independent of the fund in accordance with the ethical requirements that are relevant to my audit of the financial statements in the UK including the Financial Reporting Council’s Ethical Standard, and I have fulfilled my other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Conclusions relating to going concern basis of accounting

I have nothing to report in respect of the following matters in relation to which the ISAs (UK) require me to report to you where:

- the use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Chief Officer - Finance has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the funds' ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Responsibilities of the Chief Officer - Finance and Aberdeen City Council Pensions Committee for the financial statements

As explained more fully in the Statement of Responsibilities, the Chief Officer - Finance is responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Chief Officer - Finance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Chief Officer - Finance is responsible for assessing the funds' ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless deemed inappropriate.

The Aberdeen City Council, Pensions Committee is responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit of the financial statements

My objectives are to achieve reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of the auditor's responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website www.frc.org.uk/auditorsresponsibilities. This description forms part of my auditor's report.

Other information in the annual report

The Chief Officer - Finance is responsible for the other information in the annual report. The other information comprises the information other than the financial statements and my auditor's report thereon. My opinion on the financial statements does not cover the other information and I do not express any form of assurance conclusion thereon except on matters prescribed by the Accounts Commission to the extent explicitly stated later in this report.

In connection with my audit of the financial statements, my responsibility is to read all the other information in the annual report and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit or otherwise appears to be materially misstated. If I identify such material inconsistencies or apparent material misstatements, I am required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

Report on other requirements

Opinions on matters prescribed by the Accounts Commission

In my opinion, based on the work undertaken in the course of the audit

- the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with statutory guidance issued under the Local Government in Scotland Act 2003;
- the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016); and
- the information given in the Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations 2014.

Matters on which I am required to report by exception

I am required by the Accounts Commission to report to you if, in my opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- I have not received all the information and explanations I require for my audit.

I have nothing to report in respect of these matters.

Gillian Woolman MA FCA CPFA
Audit Director
Audit Scotland
4th Floor
102 West Port
Edinburgh
EH3 9DN

14 September 2018

Appendix 1- Statement by the Consulting Actuary

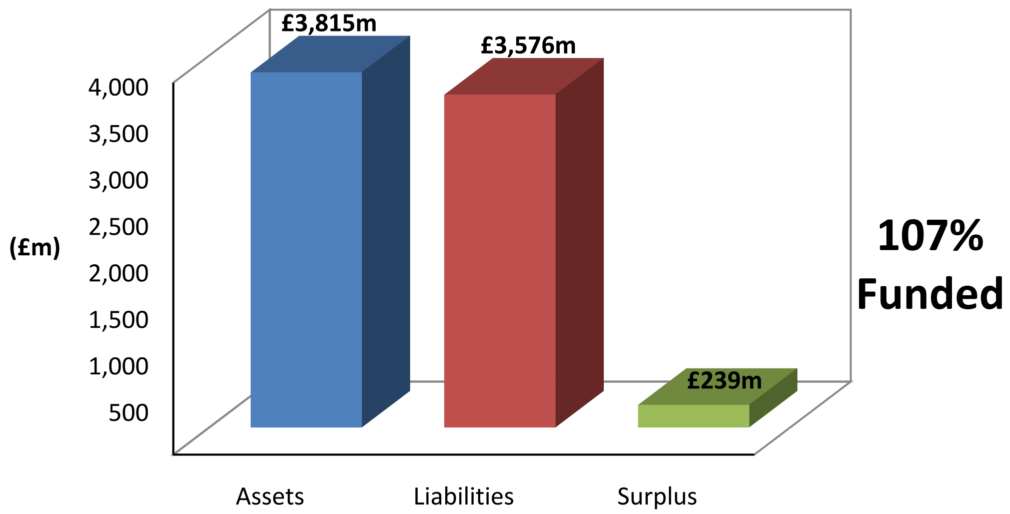
Accounts for the year ended 31 March 2018 - Statement by the Consulting Actuary

This statement has been provided to meet the requirements under Regulation 55 (1)(d) of The Local Government Pension Scheme (Scotland) Regulations 2014.

North East Scotland Pension Fund

An actuarial valuation of the North East Scotland Pension Fund was carried out as at 31 March 2017 to determine the contribution rates with effect from 1 April 2018 to 31 March 2021.

On the basis of the assumptions adopted, the Fund's assets of £3,815 million represented 107% of the Fund's past service liabilities of £3,576 million (the "Funding Target") at the valuation date. The surplus at the valuation was therefore £239 million.



The valuation also showed that a Primary contribution rate of 22.0% of pensionable pay per annum was required from employers. The Primary rate is calculated as being sufficient, together with contributions paid by members, to meet all liabilities arising in respect of service after the valuation date.

The funding objective as set out in the Funding Strategy Statement (FSS) is to achieve and then maintain a solvency funding level of 100% of liabilities (the solvency funding target). In line with the FSS, where a surplus exists at the effective date of the valuation a plan will be put in place which allows contribution offsets to refund any surplus.

The FSS sets out the process for determining the spread period in respect of each employer (or the recovery period for those employers with a deficit in the Fund). At this actuarial valuation the average spread/recovery period adopted is approximately 24 years, and the total initial surplus reclaimed on a whole fund level (the "Secondary rate" for 2018/19) is approximately £12.8 million per annum.

Further details regarding the results of the valuation are contained in the formal report on the actuarial valuation dated 28 March 2018.

In practice, each individual employer's position is assessed separately and the contributions required are set out in the report. In addition to the certified contribution rates, payments to cover additional liabilities arising from early retirements will be made to the Fund by the employers.

The funding plan adopted in assessing the contributions for each individual employer is in accordance with the FSS. Any different approaches adopted, e.g. with regard to the implementation of contribution increases and surplus offset periods, are as determined through the FSS consultation process.

The valuation was carried out using the projected unit actuarial method and the main actuarial assumptions used for assessing the Funding Target and the Primary rate of contribution were as follows:

	For both past and future service liabilities (Funding Target and Primary rate of contribution)
Rate of return on investments (discount rate)	4.15% per annum
Rate of pay increases (long term)*	3.9% per annum
Rate of increases in pensions in payment (in excess of GMP)/deferment	2.4% per annum
Rate of CPI Inflation/CARE benefit revaluation	2.4% per annum

* allowance was also made for short-term public sector pay restraint over a 3 year period.

The assets were assessed at market value.

The next triennial actuarial valuation of the Fund is due as at 31 March 2020. Based on the results of this valuation, the contribution rates payable by the individual employers will be revised with effect from 1 April 2021.

Actuarial Present Value of Promised Retirement Benefits for the Purposes of IAS 26

IAS 26 requires the present value of the Fund's promised retirement benefits to be disclosed, and for this purpose the actuarial assumptions and methodology used should be based on IAS 19 rather than the assumptions and methodology used for funding purposes.

To assess the value of the benefits on this basis, we have used the following financial assumptions as at 31 March 2018 (the 31 March 2017 assumptions are included for comparison):

	31 March 2017	31 March 2018
Rate of return on investments (discount rate)	2.5% per annum	2.6% per annum
Rate of pay increases*	3.8% per annum	3.6% per annum
Rate of increases in pensions in payment (in excess of GMP)/deferment	2.3% per annum	2.2% per annum
Rate of CPI Inflation/CARE benefit revaluation	2.3% per annum	2.1% per annum

* includes a corresponding allowance to that made in the latest formal actuarial valuation for short-term public sector pay restraint (2014 valuation for the 31 March 2017 figure, 2017 valuation for the 31 March 2018 figure).

The demographic assumptions are the same as those used for funding purposes. Full details of these assumptions are set out in the formal report on the actuarial valuation dated 28 March 2018 (the 2014 valuation assumptions were used for the 31 March 2017 figures).

During the year, corporate bond yields rose slightly, resulting in a higher discount rate being used for IAS 26 purposes at the year-end than at the beginning of the year (2.6% p.a. versus 2.5% p.a.). The expected long-term rate of CPI inflation decreased during the year, from 2.3% p.a. to 2.1%. Both of these factors combined served to decrease the liabilities over the year.

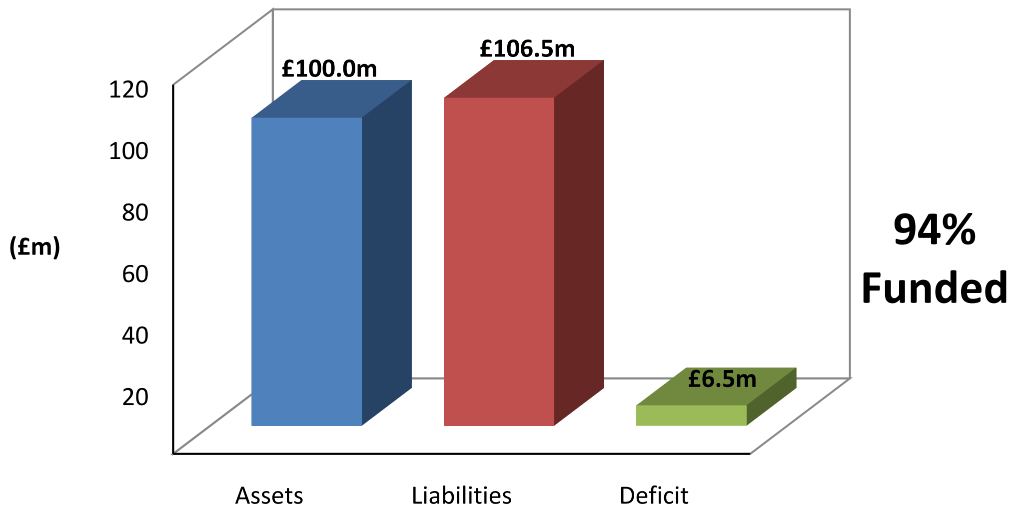
The value of the Fund's promised retirement benefits for the purposes of IAS 26 as at 31 March 2017 was estimated as £4,718 million. Interest over the year increased the liabilities by c£119 million, and allowing for net benefits accrued/paid over the period then increased the liabilities by c£81 million (after allowing for any increase in liabilities arising as a result of early retirements/augmentations). There was then a decrease in liabilities of £26 million made up of "actuarial gains" (mostly changes in the actuarial assumptions used, primarily the discount rate and assumed rate of future CPI as referred to above, offset to some degree by the results of the 2017 valuation).

The net effect of all the above is that the estimated total value of the Fund's promised retirement benefits as at 31 March 2018 is therefore £4,892 million.

Aberdeen City Council Transport Fund

An actuarial valuation of the Aberdeen City Council Transport Fund was carried out as at 31 March 2017 to determine the contribution rates with effect from 1 April 2018 to 31 March 2021.

On the basis of the assumptions adopted, the Fund's assets of £100 million represented 94% of the Fund's past service liabilities of £106.5 million (the "Funding Target") at the valuation date. The deficit at the valuation was therefore £6.5 million.



The valuation also showed that a Primary contribution rate of 58.5% of pensionable pay per annum was required from the employer. The Primary rate is calculated as being sufficient, together with contributions paid by members, to meet all liabilities arising in respect of service after the valuation date.

The funding objective as set out in the Funding Strategy Statement (FSS) is to achieve a solvency funding level of 100% of liabilities (the solvency funding target) over a reasonable time period and then maintain sufficient assets in order for it to pay all benefits arising as they fall due. In line with the FSS, where a shortfall exists at the effective date of the valuation a deficit recovery plan will be put in place which requires additional contributions to correct the shortfall.

The FSS sets out the process for determining the recovery plan. At this valuation, the Administering Authority and First Aberdeen Limited have agreed that First Aberdeen Limited will maintain the same level of current contributions as those agreed at the 2014 valuation which are 33% of pensionable pay plus £1.5m p.a. At present, therefore, part of the £1.5m annual payment is being used to finance the costs in relation to future service. This means that the amount to recover the shortfall is approximately £1.1m p.a. On this basis the deficit would be expected to be removed in about 5 years.

Further details regarding the results of the valuation are contained in the formal report on the actuarial valuation dated 28 March 2018.

The valuation was carried out using the attained age actuarial method and the main actuarial assumptions used for assessing the Funding Target and the Primary rate of contribution were as follows:

	For both past and future service liabilities (Funding Target and Primary rate of contribution)
Rate of return on investments (discount rate)	1.6% per annum
Rate of pay increases (short term)	2.9% per annum to 31 March 2018
Rate of pay increases (long term)	3.4% per annum
Rate of increases in pensions in payment (in excess of GMP)/deferment	2.9% per annum
Rate of CPI Inflation/CARE benefit revaluation	2.9% per annum

The assets were assessed at market value.

The next triennial actuarial valuation of the Fund is due as at 31 March 2020. Based on the results of this valuation, the contribution rate payable will be revised with effect from 1 April 2021.

Actuarial Present Value of Promised Retirement Benefits for the Purposes of IAS 26

IAS 26 requires the present value of the Fund's promised retirement benefits to be disclosed, and for this purpose the actuarial assumptions and methodology used should be based on IAS 19 rather than the assumptions and methodology used for funding purposes.

To assess the value of the benefits on this basis, we have used the following financial assumptions as at 31 March 2018 (the 31 March 2017 assumptions are included for comparison):

	31 March 2017	31 March 2018
Rate of return on investments (discount rate)	2.5% per annum	2.6% per annum
Rate of pay increases*	4.3% per annum	2.6% per annum
Rate of increases in pensions in payment (in excess of GMP)/deferment	2.3% per annum	2.2% per annum
Rate of CPI Inflation/CARE benefit revaluation	2.3% per annum	2.1% per annum

* includes a corresponding allowance to that made in the latest formal actuarial valuation for short-term public sector pay restraint (2014 valuation for the 31 March 2017 figure, 2017 valuation for the 31 March 2018 figure).

The demographic assumptions are the same as those used for funding purposes. Full details of these assumptions are set out in the formal report on the actuarial valuation dated 28 March 2018 (the 2014 valuation assumptions were used for the 31 March 2017 figures).

During the year, corporate bond yields rose slightly, resulting in a higher discount rate being used for IAS 26 purposes at the year-end than at the beginning of the year (2.6% p.a. versus 2.5% p.a.). The expected long-term rate of CPI inflation decreased during the year, from 2.3% p.a. to 2.1%. The real (long term) salary growth above inflation has also reduced from 2.0% p.a. to 0.5% p.a. These factors combined served to decrease the liabilities over the year.

The value of the Fund's promised retirement benefits for the purposes of IAS 26 as at 31 March 2017 was estimated as £85.6 million. Interest over the year increased the liabilities by c£2.1 million, though allowing for net benefits accrued/paid over the period then decreased the liabilities by c£3.4 million (after allowing for any increase in liabilities arising as a result of early retirements/augmentations). There was then a further decrease in liabilities of £6.3 million made up of "actuarial gains" (mostly changes in the actuarial assumptions used, primarily the discount rate and assumed rate of future CPI as referred to above, offset to some extent by the results of the 2017 valuation).

The net effect of all the above is that the estimated total value of the Fund's promised retirement benefits as at 31 March 2018 is therefore £78.0 million.

Paul Middleman
Fellow of the Institute and Faculty of Actuaries
Mercer Limited

May 2018

Appendix 2 – Schedule of Employers

North East Scotland Pension Fund

1.	Aberdeen City Council (Administering Authority)	Scheduled
2.	Aberdeenshire Council	Scheduled
3.	The Moray Council	Scheduled
4.	Scottish Water	Scheduled
5.	Grampian Valuation Joint Board	Scheduled
6.	Scottish Fire and Rescue Service	Scheduled
7.	Scottish Police Authority	Scheduled
8.	North East Scotland College	Scheduled
9.	Moray College	Scheduled
10.	Visit Scotland	Scheduled
11.	NESTRANS	Scheduled
12.	Robertson Facilities Management (Shire)	Transferee
13.	Bon Accord Care Ltd	Transferee
14.	Bon Accord Support Services Ltd	Transferee
15.	Aberdeen Heat & Power	Transferee
16.	Station House Media Unit	Transferee
17.	Aberdeen Sports Village	Transferee
18.	Sport Aberdeen	Transferee
19.	Robertson Facilities Management (City)	Transferee
20.	Forth & Oban Ltd	Transferee
21.	Alcohol and Drugs Action	Transferee
22.	Idverde UK	Transferee
23.	Visit Aberdeenshire	Transferee
24.	Citymoves Dance Agency	Transferee
25.	Xerox (UK) Ltd	Transferee
26.	Forth and Oban Ltd (Shire)	Transferee
27.	Aberdeen Endowments Trust	Admitted
28.	North East Sensory Services	Admitted
29.	Aberlour Child Care Trust	Admitted
30.	Fraserburgh Harbour Commissioners	Admitted
31.	Peterhead Port Authority	Admitted
32.	Robert Gordon University	Admitted
33.	Robert Gordon's College	Admitted
34.	Aberdeen Cyrenians	Admitted
35.	Mental Health Aberdeen	Admitted
36.	Fersands & Fountain Community Project	Admitted
37.	SCARF	Admitted
38.	Inspire	Admitted
39.	Archway	Admitted
40.	Middlefield Community Project	Admitted
41.	Gordon Rural Action	Admitted
42.	St Machar Parent Support Project	Admitted
43.	Printfield Community Project	Admitted
44.	HomeStart Aberdeen	Admitted
45.	Aberdeen Foyer	Admitted
46.	HomeStart (NEA)	Admitted
47.	Pathways	Admitted

48. Outdoor Access Trust for Scotland	Admitted
49. Osprey Housing	Admitted
50. Aberdeen Performing Arts	Admitted
51. Aberdeen International Youth Festival	Admitted
52. Sanctuary Housing	Admitted
53. Sanctuary Scotland	Admitted
54. Scottish Lighthouse Museum	Admitted

Aberdeen City Council Transport Fund

1. First Aberdeen	Scheduled

ABERDEEN CITY COUNCIL

COMMITTEE	PENSIONS COMMITTEE
DATE	14 SEPTEMBER 2018
REPORT TITLE	BUDGET/FORECAST 2018/19
REPORT NUMBER	PC/SEPT18/BUD
DIRECTOR	STEVEN WHYTE
CHIEF OFFICER	JONATHAN BELFORD
REPORT AUTHOR	MICHAEL SCROGGIE
TERMS OF REFERENCE	PENSIONS COMMITTEE 1.3

1. PURPOSE OF REPORT

1.1 The purpose of this report is to give the Pensions Committee details of the Management Expenses Budget/Forecast 2018/19 for the North East Scotland Pension Fund (NESPF).

2. RECOMMENDATION

That the Committee: -

2.1 Approve the NESPF Management Expenses Budget/Forecast 2018/19, shown in Appendix I.

3. BACKGROUND/MAIN ISSUES

3.1 BUDGET/FORECAST 2018/19

3.1.1 Appendix I shows the Council's Budget 2018/19 for the NESPF, which is consistent with that reported to Full Council in March 2018. The re-alignment of cost headings follows guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) for Pension Funds. Additional NESPF Budget is added for costs outwith the Council's Budget and for those costs directly paid for by the Fund.

3.1.2 Administrative Expenses – all staff costs of the pension administration team are charged direct to the Fund quarterly. Associated management, accommodation and other overheads are apportioned to this activity and charged annually as expenses to the Fund.

3.1.3 Oversight and Governance Expenses – all staff costs associated with oversight and governance are charged direct to the Fund quarterly. Associated management costs are apportioned to this activity and charged annually as expenses to the Fund.

3.1.4 Investment Management Expenses – Fees of the external investment managers and custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or decrease as the market value of these investments change. Fund Managers charge their fees quarterly in arrears. In addition, the Fund has negotiated performance related fees with a number of its investment managers. If applicable, performance fees are charged annually at the year end. The unpredictability of market forces for these elements makes forecasting extremely difficult with any degree of accuracy.

3.1.5 The Chartered Institute of Public Finance and Accountancy (CIPFA) has reviewed and revised their guidance to Pension Funds on Accounting for Scheme Management Costs. As a result, the Fund no longer accounts for indirect limited partnership fees.

3.1.6 Transaction Costs and Direct Property Expenses are included within the section 'Investment Management Expenses'. Other investment related expenses (e.g. investment advice and litigation, etc.) are included within the section 'Oversight & Governance Expenses'.

3.2 GOVERNANCE

3.2.1 The Pension Fund projected costs for salaries and direct costs are included in monthly monitoring reports to the Service and Corporate Management Teams. The Chief Officer-Finance reports to the Pensions Committee on a quarterly monthly basis.

4. FINANCIAL IMPLICATIONS

4.1 All Pension Fund costs are paid for by the Fund.

5. LEGAL IMPLICATIONS

5.1 There are no direct legal implications arising from the recommendation of this report.

6. MANAGEMENT OF RISK

6.1 There are no direct risk implications arising from the recommendation of this report.

7. OUTCOMES

7.1 This report does not impact either the Local Outcome Improvement Plan or the Target Operating Model.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Equality & Human Rights Impact Assessment	Not required
Privacy Impact Assessment	Not required
Duty of Due Regard / Fairer Scotland Duty	Not applicable

9. BACKGROUND PAPERS

North East Scotland Pension Fund (NESPF) Annual Report & Accounts (2017/18) and Fund Governance Policy Statement.

10. APPENDICES

Appendix I, Budget/Forecast 2018/19

11. REPORT AUTHOR CONTACT DETAILS

Michael Scroggie
Accounting Manager
MScroggie@nespf.org.uk
01224 264178

This page is intentionally left blank

Appendix I – 2018/19 BUDGET/FORECAST

The Budget/Forecast for the NESPF is shown below:

	Notes	ACC Full Year Budget 2018-19	Additional Budget	NESPF Full Year Budget 2018-19
		£'000	**£'000**	**£'000**
Administrative Staff Costs		1,238	43	1,281
Support Services Inc IT		162	497	659
Printing & Publications		13	10	23
Administration Expenses Total		**1,413**	**550**	**1,963**
Investment Staff Costs		189	0	189
Pensions Committee		2	9	11
Pension Board		2	2	4
External Audit Fee		0	40	40
Internal Audit Fee		10	0	10
Actuarial Fees		0	112	112
General Expenses		0	106	106
Oversight & Governance Expenses Total		**203**	**269**	**472**
Investment Management Fees		0	12,097	12,097
Performance Fees		0	5,536	5,536
Direct Operating Property Expenses		0	250	250
Transaction Costs		0	2,000	2,000
Custody Fees		0	145	145
Investment Management Expenses Total		**0**	**20,028**	**20,028**
Management Expenses Grand Total		**1,616**	**20,847**	**22,463**

Important to Note

Appendix I is a forecast of costs for Investment Management Expenses rather than a traditional budget. This is due to the level of estimation involved and the extent of the unknown, especially given that Investment Management and Performance Fees are based upon an unpredictable Market Value. This terminology has been adopted following discussions with the CIPFA Pensions Network.

ABERDEEN CITY COUNCIL

COMMITTEE	PENSIONS COMMITTEE
DATE	14 SEPTEMBER 2018
REPORT TITLE	STRATEGY
REPORT NUMBER	PC/SEPT18/STRAT
DIRECTOR	STEVEN WHYTE
CHIEF OFFICER	JONATHAN BELFORD
REPORT AUTHOR	LAURA COLLISS
TERMS OF REFERENCE	PENSIONS COMMITTEE 1-5

1. PURPOSE OF REPORT

1.1 To inform the Committee and provide recommendations to changes to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund.

2. RECOMMENDATION

That the Committee: -

2.1 Note the four proposed options in respect of the Scottish Local Government Pension Scheme Structure Review and agree a response to be submitted by the Chief Officer - Finance on behalf of the Fund and stakeholders (item 3.9.7).

3. BACKGROUND

3.1 In line with the structural review of the Pension Fund, six specific areas were identified to fully address the strategic management of the Fund;

- Investment
- Accounting
- Benefit Administration
- Technical
- Governance
- Employer Relations

3.2 The roles and responsibilities within these areas have been very clearly defined to ensure accountability across the Pension Fund.

3.3 The Pensions Committee will be comprehensively informed via this report as to the current position and any variances to the Funds strategy and recommendations. To support this report service updates covering the six strategic areas will also be available via the secure website (http://www.nespf.org.uk/TheFund/Governance/fundgovernance.aspx) and email.

3.4 Also available on the Pension Fund website are all the Policy documents that govern the Pension Fund including its various strategies.

3.5 **INVESTMENT**

3.5.1 *Asset & Investment Manager Performance Report*

Separate Report, provided

3.5.2 **Local Authority Pension Fund Forum (LAPFF)**

Copies of the latest e-bulletins, quarterly engagement and annual reports are available at http://www.lapfforum.org

3.6 **ACCOUNTING**

3.6.1 Audited Aberdeen City Council Pension Fund (known as the North East Scotland Pension Fund) Annual Report & Accounts

Budget/Forecast 2018/19 Report

Separate Reports, provided

3.7 **BENEFIT ADMINISTRATION**

3.7.1 **LGPS Regulations Update**

The LGPS (Scotland) Regulations 2018 came into force on 1 June 2018 and in doing so, revoked the 2014 Regulations. However concerns were raised by Scottish Funds around inconsistences and potential issues with the new Regulations. The main concern being that the Regulations, by revoking the 2014 Regulations, have the unintended effect of revoking rights and liabilities accrued under the 2014 Regulations i.e. for members who left prior to 1 June 2018, which then impacts on the Fund’s ability to carry out its administrative functions such as processing retirement benefits. Amendment Regulations are due to be issued as a matter of urgency but in the meantime a Letter of Comfort has been provided by Scottish Ministers to allow normal business to continue.

3.8 **TECHNICAL**

3.8.1 *Appendix I*, Pensions Administration Strategy Update

3.9 <u>**GOVERNANCE**</u>

3.9.1 **Scheme Advisory Board**

Copies of the latest bulletins and meetings available at http://lgpsab.scot

3.9.2 **Annual Benefit Statements**

3.9.3 The North East Scotland Pension Fund has a statutory requirement to issue all active and deferred members with annual benefit statement information by 31 August each year. The Fund reported 99.76% compliance in terms of the 2016/17 active benefit statements and 93.06% in respect of deferred benefit statements.

3.9.4 Deferred annual benefit statements for 2017/18 were issued to members online through the Fund's secure Member Self Service (MSS) facility, with an option for members to 'opt in' to continue receiving paper statements.

3.9.5 Active benefit statements are on schedule to be issued week commencing 20 August 2018, with a planned move to online statements from 2018/19. A final outcome report will be taken to the next Committee meeting.

3.9.6 **Pension Fund Staffing Update**

Two posts within the Pensions Section, Senior Pensions Officer-Training & Development and Pensions Officer-Employer Relationship, have been advertised internally within the Council and interviews are scheduled to take place shortly. Recruitment of an additional Pensions Officer on the ER team was approved by the Committee in March 2017 to help meet the ever increasing workload demands on the team. Recruitment to the SPO-Training & Development post will fill a vacancy left by the retirement of the previous post holder.

3.9.7 **Scheme Structure Review Update**

3.9.8 A consultation was launched on the Scottish LGPS structure review in June, to invite employers and employee representative groups to give their views on how the SLGPS should best be structured to service it's members and sponsors going forward. The consultation will close on 7 December 2018.

3.9.10 The consultation sets out 4 possible options:

- Keep the status quo (11 separate Funds)
- Promote cooperation in investing and administration between the 11 Funds
- Pool investments between the 11 Funds
- Merge the 11 Funds into one or more new Funds

3.9.11 Responses to the consultation will be evaluated by the Scottish Scheme Advisory Board and presented to Scottish Government Ministers in 2019 before a final decision is made.

3.9.12 Further information on the proposed options and background reports are available at https://lgpsab.scot

Appendix II, Consultation Report
Appendix III, Consultation Response Form

3.10 **EMPLOYER RELATIONSHIP**

3.10.1 **Annual Administration Forum**

The annual administration forum was held at the Beach Ballroom on 4 July 2018. Feedback from the event was extremely positive, with both the workshops and presentations being well received. In total 22 of the Fund's participating employers attended. Topics covered included retirement, data protection, pensionable pay and communications.

3.10.2 **Year End/Valuation Process Update**

All Scheme employers are required to submit an annual year-end data return by 30 April and this deadline was met again this year (with the exception of just 1 employer). The year-end process for 2017/18 was completed in just 32 days (down from 55 in 2016/17 and 63 in 2015/16). The Fund continues to expand its online data exchange services, with all employers required to submit electronic monthly submissions which helps improve data quality and reduce year-end processes for both individual employers and the Fund.

The Employer Relationship Team processes and reconciles each year-end data return. Approximately 25,000 active member records were updated, between April and July 2018, with employee and employer contributions as well as salary information and CARE pay for the year.

4. FINANCIAL IMPLICATIONS

4.1 The performance of the Fund over the long term can impact on the Fund's funding level and therefore the ability to meet its long-term liabilities.

5. LEGAL IMPLICATIONS

5.1 There are no direct legal implications arising from the recommendation in this report.

6. MANAGEMENT OF RISK

6.1 The Pension Fund regularly updates its Risk Register in line with change and is reported quarterly to the Pensions Committee.

Appendix IV, Copy of Risk Register (August 2018)

7. OUTCOMES

Design Principles of Target Operating Model	
	Impact of Report
Governance	This report links to the 'governance' design principle by ensuring transparency and by providing the necessary information to allow informed decisions to be made and implemented, including performance and improvement measures.
Workforce	This report links to the 'workforce' design principle as the report details the six separate areas of the Fund, each with clear roles and responsibilities, ensuring accountability across the Fund. The Fund structure is kept under review to ensure we can continue to meet immediate obligations as well as being able to anticipate and meet longer term needs.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Equality & Human Rights Impact Assessment	Not required
Privacy Impact Assessment	Not required
Duty of Due Regard / Fairer Scotland Duty	Not applicable

9. BACKGROUND PAPERS

None

10. APPENDICES

Appendix I, PAS Update Quarter 1 Report 2018/19
Appendix II, Consultation Report
Appendix III, Consultation Response Form

Appendix IV, Copy of Risk Register August 2018

11. REPORT AUTHOR CONTACT DETAILS

Laura Colliss
Pensions Manager
LColliss@nespf.org.uk
01224 264158

North East Scotland
PENSION FUND

Pension Administration Strategy

Quarterly Reporting |June 2018

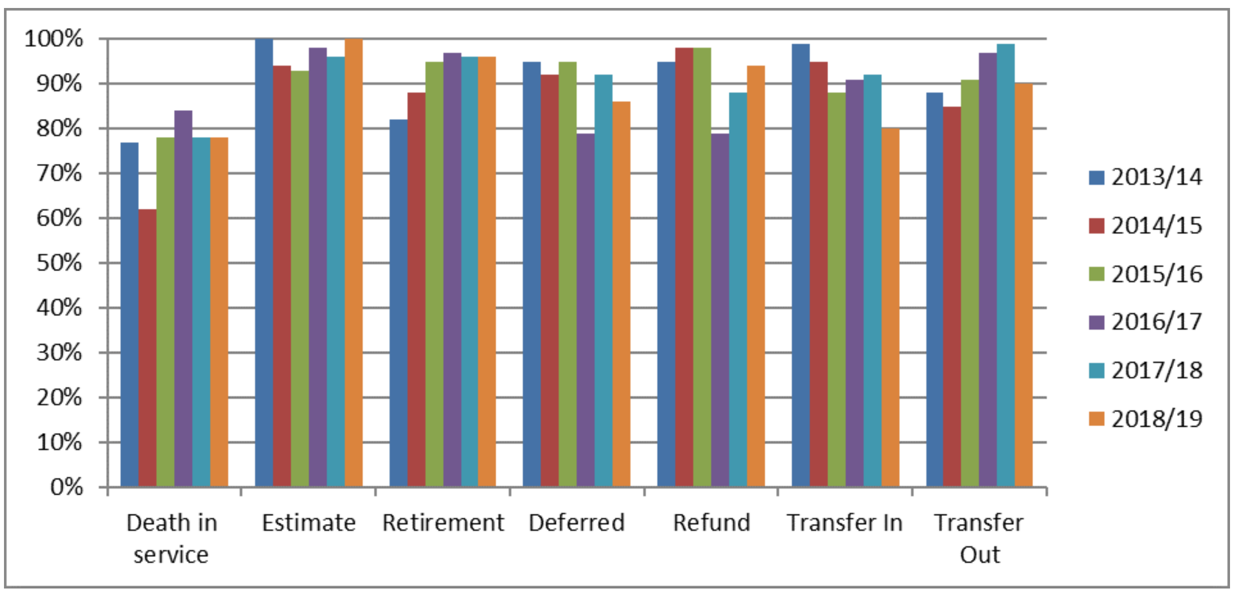
1. NESPF performance to 30 June

1.1 Key administration tasks

Measuring performance is essential to evidence the efforts made by both the Pension Fund and Scheme employers to comply with statutory requirements and deliver a high quality pension administration service. The Pension Fund aims to provide the information below within the agreed timescales shown.

Administration Task	Target	Amount	Achieved	Percentage
Notification of death in service	5 days	9	7	78%
Notification of retirement estimate	10 days	252	252	100%
Notification of retirement benefits	10 days	477	459	96%
Notification of deferred benefits	10 days	78	67	86%
Notification of refund	10 days	258	243	94%
Notification of transfer in value	10 days	30	24	80%
Notification of transfer out value	10 days	115	103	90%

1.2 Previous years comparison



2. Employer performance to 30 June

2.1 Policy on discretions received (85%)

Each Scheme emloyer is required under regulation 58 of the Local Government Pension Scheme (Scotland) Regulations 2014 to prepare a written statement of its policy on how it will exercise various discretions provided by the Scheme. This 'discretions policy' must be kept under review by employers and revised as necessary.

Employers			
Aberdeen City Council	Aberdeen Cyrenians	Aberdeen Endowments Trust	Aberdeen Foyer
Aberdeen Heat and Power	Aberdeen Performing Arts	Aberdeen Sports Village	AIYF
Aberdeenshire Council	Aberlour	Archway	Bon Accord Care
Bon Accord Support	Outdoor Access Trust for Scotland	Fersands and Fountain	First Aberdeen
Forth & Oban (City)	Fraserburgh Harbour	Grampian Valuation Joint Board	Home Start Aberdeen
Inspire	Mental Health Aberdeen	Middlefield Community Project	Moray College
NESTRANS	North East Scotland College	North East Sensory Services	Osprey Housing
Pathways	Peterhead Port Authority	Printfield Community Project	Robert Gordons College
Robert Gordon University	Sanctuary Scotland	Scottish Fire and Rescue	Scotland's Lighthouse Museum
Scottish Police Authority	Scottish Water	Sport Aberdeen	St Machar Parent Support Project
Station House Media Unit	The Moray Council	Visit Scotland	Xerox

2.2 Signed PLO statements received (46%)

Following the revision of the NESPF Pension Administration Strategy in April 2018 each Scheme employer must designate a named individual to act as a Pension Liaison Officer, the main contact with regard to any aspect of administering the Local Government Pension Scheme (LGPS).

Pension Liaison Officers			
Aberdeen City Council	Aberdeen Cyrenians	Aberdeen Endowments Trust	Aberdeen Foyer
Aberdeen Heat and Power	Aberlour Childcare Trust	Alcohol & Drugs Action	Archway
Bon Accord Care	Bon Accord Support	Outdoor Access Trust for Scotland	Fraserburgh Harbour
Middlefield Community Project	Moray College	North East Scotland College	North East Sensory Services
Pathways	Peterhead Port Authority	Printfield Community Project	Robert Gordons College
Scottish Fire and Rescue	Scottish Water	Sport Aberdeen	St Machar Parent Support Project
Visit Aberdeenshire	Xerox		

2.3 Quantity of data received (240,042)

All Scheme employers are now required to provide monthly data using I-Connect, by way of a monthly file extracted from the payroll system or by completing electronic forms for individual members.

I-Connect events processed	Total
Starters (new start and opt in)	1062
Amendments (address, personal details, hours and absence)	8878
Leavers (exit and opt out)	874
Contributions (employee, employer and additional)	77599
Salary	75825
Cumulative CARE pay	74438
Works address	1366

2.4 Quality of data received

The quality of data received from Scheme employers is assessed and checked by the Employer Relationship Team (ERT). Red, Amber and Green flags will be used to assess the quality of the data. The Pension Fund will seek, at the earliest opportunity, to work closely with Scheme employers in identifying areas of unsatisfactory performance, and provide the necessary training and development for improvement.

Since the introduction of the requirement to provide monthly information in this format the quality of the data received through i-Connect has been of a very high standard. This allows the Fund to provide accurate and up to date information to members, meet the requirements of The Pension Regulator and improved the accuracy of the financial information held for the valuation of the Fund.

Green	I-Connect events processed and validated by ERT
Amber	I-Connect events processed however missing or incorrect data identified by ERT
Red	I-Connect events not processed
Blank	Data not provided (as at June 2018)

Employer	Submission	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
Aberdeen City Council	Extract File												
Aberdeenshire Council	Extract File												
Bon Accord Care	Extract File												
Bon Accord Support	Extract File												
Grampian Valuation Joint Board	Extract File												
Moray Council	Extract File												
NESTRANS	Extract File												
Police Scotland (Aberdeen)	Extract File												
Robert Gordon University	Extract File												
Moray College	Extract File												
Scottish Water	Extract File												
Scottish Fire and Rescue Service	Extract File												
Sport Aberdeen	Extract File												
Aberdeen Endowments Trust	Online Return												
Aberdeen Cyrenians	Online Return												
Aberdeen Foyer	Online Return												
Aberdeen Heat and Power	Online Return												
Aberdeen Performing Arts	Online Return												
Aberdeen Sports Village	Online Return												
Aberlour Child Care Trust	Online Return												
Aberdeen International Youth Festival	Online Return												
Archway	Online Return												
City Moves Dance Agency	Online Return												

Alcohol & Drugs Action	Online Return												
Fersands and Fountain	Online Return												
First Aberdeen	Online Return												
Forth and Oban (City)	Online Return												
Forth and Oban (Shire)	Online Return												
Fraserburgh Harbour	Online Return												
Homestart Aberdeen	Online Return												
Homestart NEA	Online Return												
ID Verde	Online Return												
Inspire	Online Return												
Mental Health Aberdeen	Online Return												
Middlefield Community Project	Online Return												
North East Sensory Services	Online Return												
Osprey Housing	Online Return												
Outdoor Access Trust Scotland	Online Return												
Pathways	Online Return												
Peterhead Port Authority	Online Return												
Printfield Community Project	Online Return												
Police Scotland (Glasgow)	Online Return												
Robert Gordon College	Online Return												
Robertson FM City	Online Return												
Robertson FM Shire	Online Return												
Sanctuary Scotland	Online Return												
SCARF	Online Return												
Scotlands Lighthouse Museum	Online Return												
St Machar Parent Support Project	Online Return												
Station House Media Unit	Online Return												
Visit Scotland	Online Return												
Xerox	Online Return												
North East Scotland College	ALCARE												

Consultation on the

Review of the Structure of the Scottish Local Government Pension Fund

Carried out by the Pensions Institute

on behalf of the Scottish Local Government Pension Scheme Advisory Board

June 2018

Contents

About the Pensions Institute

Hosted by Cass Business School at the University of London, the Pensions Institute (www.pensions-institute.org) is the first and only UK academic research centre focused entirely on pensions research. Our purpose is to serve as an essential forum for pensions data and research, with particular emphasis on the UK system.

About the Scheme Advisory Board

Established under the Public Service Pensions Act 2013, the Scheme Advisory Board's role is to provide advice to the Scottish Government on the desirability of changes to the design of the Scottish Local Government Pension Scheme and the implication of other policy issues.

Cabinet Secretary's foreword

I am delighted to support the launch of the Scottish Local Government Pension Scheme Advisory Board's consultation on a structural review of the Local Government Pension Scheme (LGPS) pension funds in Scotland.

LGPS fund authorities invest in a wide variety of projects including local housing and infrastructure, however investment in Scotland's infrastructure is only a small part of the investment strategy of the Scottish fund authorities. The Scottish Government is ambitious for greater investment by local government funds in Scotland's infrastructure.

There are currently excellent examples of fund authorities collaborating on infrastructure projects in Scotland. We look to LGPS fund authorities to improve their already positive impact on the economy thereby contributing further to sustainable economic growth, creating more jobs and supporting the delivery of key capital infrastructure needs in Scotland, such as transport projects and housing.

A key part of the Scheme Advisory Board's role is to provide advice about the effective and efficient administration and management of the Scheme. So I asked the board to investigate the collaboration between fund authorities to invest in Scottish infrastructure, whilst maintaining overall investment performance to ensure that the interests of LGPS members' are protected.

The Scheme Advisory Board commissioned reports from pension consultants Mercers and Iain Clacher of the University of Leeds on possible future structures for the funds. The reports highlight that the new governance arrangements require a greater focus on cost transparency and performance. The academic evidence on costs and fees also seems to support the premise that there are cost savings available with economies of scale for both the administration and investment of pension funds.

I welcome the Scheme Advisory Board's consultation, which provides four clear options for the future structure of pension funds in Scotland. I encourage you to participate fully in this important debate which could have a wide-ranging impact on the people of Scotland.

Derek Mackay MSP

Cabinet Secretary for Finance and the Constitution

Executive summary

This consultation seeks to establish the views of employers and employee representative groups on whether outcomes for the members and sponsors of the Scottish Local Government Pension Scheme (SLGPS) can be improved by altering the structure of the scheme.

The consultation asks these stakeholders to compare the advantages and disadvantages of the current scheme structure against three options that, by differing degrees, consolidate the functions of the scheme's 11 constituent funds by collaboration, pooling and merger.

The main question is whether the sustainability of the scheme, and thus members interests, can be improved by reducing the investment management costs of the system with the trade-off of potentially diminishing local governance and oversight.

Investment management costs are the single biggest line item of expenditure in the system and small reductions in fees can lead to significantly improved net investment performance for funds over the long run. But how do these quantitative gains compare to the qualitative losses of local control?

This central question also gives rise to subsidiary questions. Consolidation has the potential to improve the ability of funds to invest. Larger scale in funds could improve governance, the range of investments available to funds and the management of operating risks – each with the potential to enhance performance.

But at the same time, the roles of people working locally in funds could be diminished, with their responsibilities concentrated in a smaller set of larger funds. Changes to the current structure would generate set up costs and require careful implementation to ensure accountability was maintained.

The purpose of the consultation is to get feedback on four possible options, ranging from maintaining the *status quo* to full consolidation into one or more larger funds. Responses gathered in this consultation will be evaluated and presented to Scottish Government Ministers in 2019 for a decision on a future course of action.

Although this consultation asks questions about a potential future structure for the SLGPS, these questions were also relevant when designing the current system. This consultation asks whether the trade-off – between scaling up to reduce investment costs or retaining governance locally – inherent in the current system of 11 funds is the best interest of members and sponsors or should be revisited.

Introduction

This consultation invites employers and employee representative groups to give their views on how the Scottish Local Government Pension Scheme (SLGPS) should best be structured to serve its members and sponsors.

SLGPS is Scotland's largest pension scheme with currently more than 406,000 members who are employees, former employees and pensioners. It has members in local government, education, the police, the voluntary sector, environment agencies and private contractors. The scheme is composed of 11 individual funds with assets totalling around £42bn and liabilities to members of £55bn.[1] Each fund serves a different group of employer organisations, the largest fund is Strathclyde with £19.7bn in assets and 210,000 members; Orkney Islands is the smallest, with assets of £335m and 3,663 members.[2]

Research by the Scheme Advisory Board, a statutory organisation set up to advise SLGPS and the Scottish Government, shows that the scheme faces a number of significant challenges and, as a result, the current structure of the scheme with its 11 funds should be reviewed.

A selection of these challenges include: the deficit; investment management costs and their transparency; investment performance; volatile investment markets; low interest rates; a maturing scheme membership; and the consequences of implementing investment preferences in respect of certain assets, such as fossil fuels and infrastructure.

Based on this research, the Scheme Advisory Board has identified four options that compare the advantages and disadvantages of retaining the current structure of the scheme without change or, by degrees, consolidating the scheme's 11 constituent funds:

1. Retain the current structure with 11 funds.
2. Promote cooperation in investing and administration between the 11 funds.
3. Pool investments between the 11 funds.
4. Merge the 11 funds into one or more new funds.

The purpose of this consultation – requested by the Scottish Government Cabinet Secretary for Finance and Constitution, Derek Mackay MSP – is to ask employers and employee representative groups for their views on each of these options.

Responses gathered in this consultation will be evaluated by the Scheme Advisory Board and presented to Scottish Government Ministers in 2019 to inform any future course of action. As well as this consultation, Ministers will also take into consideration a

[1] The SLGPS also includes five additional funds including transport funds and the Scottish Homes Pension Fund which are managed by the 11 administering authorities.

[2] All figures dated 31 March 2017.

governance review of public sector pensions being undertaken by the Scottish Public Service Pensions Agency.

This consultation report contains detailed background on how the options were developed including web links to the original research reports; presents arguments for each option; and provides questions that LGPS employers and employee representative bodies should answer to present their views.

The consultation is being managed by Pensions Institute, an academic research organisation hosted by the University of London, on behalf of the Scheme Advisory Board.

How to participate

This consultation is open to LGPS employers and employee representative groups only. To have their views heard, these organisations should respond to the questions in the form accompanying this report and return it via email to the Pensions Institute at consultation@pensions-institute.org no later than Friday, 7 December 2018.

As it is not practical to engage with scheme members directly, respondents who are employee representative bodies are encouraged to canvass the views of their members in order to present their views to this consultation.

Employers who are also administering authorities are additionally invited to give their views from their perspective as authorities. The consultation will attempt to contact all employer members of the SLGPS but the 11 administering authorities should also encourage their admitted bodies to take part in the consultation.

This consultation is being conducted in electronic form only, so responses must be emailed; hard copy posted or delivered responses cannot be received. Any queries about the consultation should be addressed to Matthew Roy, Fellow, Pensions Institute at matthew.roy@pensions-institute.org.

Background to the consultation

1. A review of the structure of the SLGPS was agreed with stakeholders and the Scottish Government Ministers when the changes to the scheme and the new Scheme Advisory Board were introduced in 2015. The Scheme Advisory Board (SAB) proposed carrying out this review beginning in 2016.

2. SAB's proposal was approved by the Scottish Government Cabinet Secretary for Finance and Constitution.

3. Several studies were used to inform this review and make up the background to this consultation. These are summarised in Appendix 1.

4. In February 2017, SAB produced its own review report. This report is informed by the findings of research in Appendix 1 as well as a working party set up by the board comprising employers, trades unions and fund advisers. It also includes two new pieces of research commissioned by SAB from Mercer in 2016 and Iain Clacher at Leeds University Business School in 2017 and these are included as annexes to SAB's review report.

   The report can be found at SAB's website lgpsab.scot/consultation2018.

5. In summary, the report sets out four options for the future structure of the local government pension scheme in Scotland:

   1) Retain the current structure with 11 funds

   2) Promote cooperation in investing and administration between the 11 funds

   3) Pool investments between the 11 funds

   4) Merge the 11 funds into one or more new funds

6. The four options were presented to Scottish Government Ministers in May 2017. In January 2018, SAB received a letter from Derek Mackay MSP, Cabinet Secretary for Finance and the Constitution seeking a consultation with SLGPS employers and employee membership bodies on the four options.

7. The next section presents a summary of the arguments detailed in SAB's review report.

Summary arguments for and against the four options

8. The Scheme Advisory Board's 2017 report sets out four main options for the local government pension scheme and this consultation focuses on four criteria in relation to each option:

— Cost of investing: This is the biggest outlay by each fund in SLGPS and research suggest even small reductions in investing costs and, in particular, investment manager fees could have a significant impact on fund performance.

— Governance: Numerous studies show that improving governance produces significantly better outcomes over the long-term and that most pension funds in both the private and public sectors have room to improve in this area.

— Operating risks: Are believed to vary significantly among public and private sector pension funds depending on the effectiveness of the governance processes of each fund and the quality of the executive resources available to individual funds.

— Infrastructure investment: There is an increasing political desire that SLGPS funds be able to invest pension assets in infrastructure should they decide it to be in the interest of members and employers.

9. Below are summarised the advantages and disadvantages of each option in relation to these criteria and the questions asked in the consultation. The full arguments across a wider range of criteria can be found in SAB's review report. Detailed summaries of the arguments for each option are also presented in Appendix 2 of this report.

Option 1: Retain the current structure with 11 funds

10. The first option for the SLGPS is to do nothing and to maintain the status quo by retaining the current structure with 11 funds.

Cost of investing

11. Evaluating the costs of investing in the 11 funds is currently hindered by the funds' different approaches to reporting and a lack of transparency in investment fees. But from an investment perspective, maintaining the current structure is likely to mean that inefficiencies will remain across the SLGPS as most of the funds will not achieve the benefits of scale that have been documented across a number of countries including the UK. These benefits include improved bargaining power and reduced duplication of efforts in administration, governance, spending on advisors and fund management.

12. The consequence of this is that the scheme will continue to cost more per member for some employers than others. Over the long-run, such cost inefficiencies could be considerable and hence require higher contribution rates putting further pressure on local government and employer budgets.

Governance

13. The current structure of the SLGPS is complex and funds have responded by adopting a variety of different processes for managing investment mandates, investment fund performance and investment costs. As a whole, larger funds have greater resources and capacity to establish and manage these processes than smaller funds.

14. However, a potential advantage in maintaining the current structure would be to retain local oversight and strategy. This local connection may be more difficult to retain if centralised asset pools or merged funds were to be created, as are explored in the options below.

Operating risks

15. There is significant variation in the resources funds have to manage governance processes under the current structure. Smaller funds tend to have less executive support than larger funds. Funds run by only a few individuals may face 'key-person' risk where the incapacity or absence of a single individual hampers the operation of the fund.

Infrastructure

16. Funds have different capacities to invest in infrastructure under the current structure. Larger funds are better able to make investments in infrastructure projects, while small funds acting on their own may not have the resources or expertise to invest in these assets.

<u>Question 1:</u>

Please use the attached form when answering these questions and explain your responses.

a) Cost of investing:

- How well informed do you feel about the investment costs in your fund? What information do you rely on to specify and measure these?

- How well does the current system manage investment costs?

- How would you improve the measurement and management of investment costs in the current system?

b) Governance:

- How well informed do you feel about the governance of your fund? What information do you rely on to measure this?

- How well is the current system governed?

- How would you improve governance of the current system?

- How important is it to maintain a local connection with respect to oversight and strategy?
- How would you determine if the benefits of a local connection in governance outweigh the benefits of scale?

c) Operating risks:

- How well informed do feel about the operating risks of your fund? What information do you rely on to specify and measure these?
- How well are operating risks managed in the current system?
- How would you improve the measurement and management of operating risks in the current system?

d) Infrastructure:

- How well informed do you feel about your fund's investments in infrastructure? What information do you rely on?
- How do you rate the current system's ability to invest in infrastructure?
- How would you increase investment in infrastructure in the current system?

e) Do you have any additional comments about this option?

Option 2: Promote cooperation in investing and administration between the 11 funds

17. The second option for the SLGPS is to retain the current structure with 11 funds but promote cooperation in investing and administration between different funds. Cooperation encompasses co-investment, and shared services, where funds agree to share functions in order to achieve cost savings through economies of scale.

Cost of investing

18. Cooperation between funds when hiring investing managers could lead to efficiency gains. One example of this is the investment collaboration between the Lothian and Falkirk funds. This agreement allowed Falkirk to leverage expertise and scale by jointly investing with the larger Lothian fund.

19. The Lothian-Falkirk example suggests that groups of funds could collaborate to lower costs by clubbing together when appointing managers to invest in particular asset classes. In this model, funds would invest in UK equities or other asset classes as one large block rather than as separate mandates across a number of funds.

20. But coordinating such joint procurement decisions in an informal environment may be challenging. Since any party is free to leave the arrangement, any cost savings may not be long lasting.

Governance

21. Under the cooperation option, the current structure of governance would continue. Investment mandates would be directed by the Pension Committee of each fund and each fund would retain local oversight and strategy. As such, cooperation between the funds would be limited in scope by the rules for investing followed by each Pension Committee.

22. Each collaboration arrangement would then require a new subordinate governance process. In the example of Lothian and Falkirk, the Pension Committees of each fund must agree to coordinate when they delegate investment mandates.

23. Although cooperation would require some sharing of control, and more complex governance, it would still retain some local oversight and strategy.

Operating risks

24. Promoting cooperation arrangements would not resolve issues that smaller funds may have with executive support. They would add new layers of complexity which must be managed. The need for funds to coordinate activities has the potential to reduce the effectiveness and responsiveness of the individual investment decisions of each fund, particularly if this slows down the investing process.

Infrastructure

25. In the Lothian-Falkirk example, both funds have been able to jointly invest substantial in infrastructure projects. But it is unclear how well collaboration agreements would scale to include more joint fund investors. Several funds may wish to club together to invest in large scale projects as each fund individually is likely to have only a small

allocation available to infrastructure as an asset class. It is unclear if funds could bear the transaction costs and resources this 'clubbing together' process would require or if it could be concluded swiftly enough.

Question 2:

Please use the attached form when answering these questions and explain your responses.

a) Cost of investing:

- What impact do you think promoting agreements between funds would have on investment costs?
- What would be the positive impacts?
- What would be the negative impacts?

b) Governance:

- What impact do you think promoting agreements between funds would have on governance?
- What would be the positive impacts?
- What would be the negative impacts?

c) Operating risks:

- What impact do you think promoting agreements between funds would have on operating risks?
- What would be the positive impacts?
- What would be the negative impacts?

d) Infrastructure:

- What impact do you think promoting agreements between funds would have on funds' ability to invest in infrastructure?
- What would be the positive impacts?
- What would be the negative impacts?

e) Do you have any additional comments about this option?

Option 3: Pool investments between the 11 funds

26. The third option covers asset pooling where the assets of distinct pension schemes are consolidated into one or more asset pools to be managed centrally on behalf of the different schemes. Schemes retain their governance, administration and back office functions and continue to appoint and manage many of their advisers. This process would be analogous to the pooling of LGPS assets that is ongoing in England and Wales.

27. Asset pooling would be a significant shift to the way in which the SLGPS manages its investments. From an investment perspective, if there were to be a single aggregated pool, it would have circa £42bn of assets under management more than double the size of the largest fund currently, Strathclyde at £19.7bn in assets.

28. Although funds would be pooled, assets and liabilities would still be allocated by the employer in the same way as the current arrangements. This ensures that employers would still be liable for the pension obligations that they have accrued, for any deficit that they are liable for currently, and for any new benefits that are promised.

Cost of investing

29. Asset pooling has the potential to generate significant cost savings from scale over the long-term. For instance, the larger scale of asset pools could enable the majority of the investment activities of funds participating in each pool to be brought in house, which is likely to create significant cost efficiencies over time as well as allowing for a more sophisticated and dynamic investment strategy.

30. A significant challenge in successfully pooling assets is achieving scale to cover set-up costs, ongoing operating expenses and governance costs. In the short-term, pooling would generate large initial transitional and set up costs, potentially including the requirement to seek FCA authorisation for the new asset pools.

Governance

31. From a governance perspective, under asset pooling each fund’s Pensions Committee would likely retain responsibility for determining the asset allocation for their investments, making funding decisions and ensuring funds were managed in accordance with applicable laws and regulations. However, the day-to-day management of the investments would be delegated to the pool.

32. Each fund would also retain its Pension Board as stipulated in The Public Service Pensions Act 2013, with its existing employer and employee representation, as well as its role to provide advice on the administration and management of the pool.

Operating risks

33. Pooling assets would significantly boost the executive resources available to manage governance process related to day-to-day investing. But investment management risks would become concentrated in the new asset pools. It would be critical to establish clear lines of responsibility to ensure there is accountability for decisions made when managing the pool and to retain local oversight and strategy.

Infrastructure

34. By grouping investments together under single mandates, pooling is expected to significantly boost the capability of the SLGPS to invest in infrastructure. Combined in pools, the buying power of each individual fund's allocation to infrastructure could be exercised collectively, in a coordinated way.

Question 3

Please use the attached form when answering these questions and explain your responses.

a) Cost of investing:

- What impact do you think pooling investments between funds would have on the cost of investing?
- What would be the positive impacts?
- What would be the negative impacts?
- If asset pooling were possible, under what circumstances should a fund consider joining an asset pool?
- Under which circumstances should the SLGPS consider directing funds to pool?

b) Governance:

- What impact do you think pooling investments between funds would have on governance?
- What would be the positive impacts?
- What would be the negative impacts?

c) Operating risks:

- What impact do you think pooling investments between funds would have on operating risks?
- What would be the positive impacts?
- What would be the negative impacts?

d) Infrastructure:

- What impact do you think pooling investments between funds would have on funds' ability to invest in infrastructure?
- What would be the positive impacts?
- What would be the negative impacts?

e) Do you have any additional comments about this option?

Option 4: Merge the funds into one or more new funds

35. The fourth scenario is for funds in the SLGPS to merge, with assets, liabilities and administrative functions being managed by one or more larger funds.

36. Merging pension funds poses a number of challenges. Although funds merge, their assets and liabilities still have to be allocated by the employer, as employers would remain liable for the pension obligations that they have accrued, for any deficit that they are liable for currently, and for any new benefits that are promised.

Cost of investing

37. Fund mergers have the potential to generate significant cost savings from scale over the long-term in the same way that asset pooling does. For instance, the larger scale of funds could enable the majority of the investment activities of merged funds to be brought in-house, which could create significant cost efficiencies over time as well as allowing for a more sophisticated and dynamic investment strategy.

38. Fund mergers may provide additional improvements to the cost of investing over and above pooling. As well as day-to-day investment management, other back office functions would also be combined to lower costs. Larger scale asset pools may also make available additional investment risk management strategies, such as interest rate hedging.

39. In the short-term, merging would generate large initial transitional and set-up costs.

Governance

40. The full merger of SLGPS funds would likely have the most far-reaching consequences for governance. Governance would likely no longer be a local government function and could be the responsibility of one or more central government bodies. Although there would be local government representation on the Pensions Boards of the merged funds, the treasury function of the local authority is no longer likely to have direct involvement in any pension fund matters.

41. The dual board-committee structure could persist or be replaced by different arrangements such as a lead authority or a joint board.

Risk management

42. Mergers, like the asset pooling option, would significantly boost the executive resources available to manage governance process related to day-to-day investing, but additionally bring more executive support to bear in merged back office and administrative support functions.

43. As in asset pooling, it would be critical to establish clear lines of responsibility to ensure there is accountability for decisions made when managing merged funds.

Infrastructure

44. By grouping investments together under single mandates, mergers, like pooling are expected to significantly boost the capability of the SLGPS to invest in infrastructure.

Combined in merged funds, the buying power of each individual fund's allocation to infrastructure could be exercised collectively, in a coordinated way.

Question 4

Please use the attached form when answering these questions and explain your responses.

a) Cost of investing:

- What impact do you think mergers between funds would have on the cost of investing?
- What would be the positive impacts?
- What would be the negative impacts?
- If merging were possible, under what circumstances should a fund consider a merger?
- Under what circumstances should the SLGPS consider directing funds to merge?

b) Governance:

- What impact do you think mergers between funds would have on governance?
- What would be the positive impacts?
- What would be the negative impacts?

c) Operating risks:

- What impact do you think mergers between funds would have on operating risks?
- What would be the positive impacts?
- What would be the negative impacts?

d) Infrastructure:

- What impact do you think mergers between funds would have on funds' ability to invest in infrastructure?
- What would be the positive impacts?
- What would be the negative impacts?

e) Do you have any additional comments about this option?

Question 5

Please use the attached form when answering these questions and explain your responses.

a) Which option does your organisation prefer? Please explain your preference.

b) What other options should be considered for the future structure of the LGPS?

c) What would be the advantages and disadvantages of these other option for funds' investment costs, governance, operating risks and ability to invest in infrastructure?

d) Are there any other comments you would like to make?

Appendix 1: Reports of previous pension scheme reviews

Deloitte report

A copy of the Deloitte report can be found SAB's website lgpsab.scot/consultation2018.

In 2011, Deloitte presented research on the merits of combining the investment and administration functions of the SLGPS. This research was conducted as part of a Pathfinder Project to identify potential cost savings and operational efficiencies in SLGPS by adopting shared services. Participants in the research included the Improvement Service, Scottish Government, Convention of Scottish Local Authorities (COSLA), the 11 funds and the Scottish Public Pensions Agency.

The 2011 report considered a number of models including retaining the current structure and merging into one, two or three larger host funds. While Deloitte identified a number of key risks in the current structure, they concluded that the savings in investment management fees would not be significant enough to justify, in cost terms alone, merging funds. They reached a similar conclusion in relation to an improvement in investment performance. They did recommend less active investment management and pointed to the benefits, particularly for small and medium sized schemes, of shared technical advice.

In relation to administrative costs, the report found that costs per member in Scotland compared favourably with funds in England and Wales. However, based on the experience of shared services between Cumbria and Lancashire, Deloitte recommended further consideration of a single operating model and a common administration system – rather than formal administrative mergers.

APG report

A copy of the APG review can be found at SAB's website lgpsab.scot/consultation2018.

In light of increasing awareness about investment fees and performance, UNISON commissioned the Dutch pension group, APG, to undertake a similar review of LGPS pension funds across the UK, including Scotland. APG evaluated data on 101 funds over 2001–09 and modelled the impact of fund mergers.

APG concluded that investment expenses and administration costs decline when the size of fund increases and that larger funds consistently achieved higher investment returns. They also drew upon international studies that show substantial positive economies of scale in asset management.

APG's simulation for one fund in Scotland indicated average annual savings in investment management costs of £7m. They also concluded that improved investment performance could have led to £772m of additional assets for Scottish funds.

Audit Scotland report

A copy of the Audit Scotland report can be found at SAB's website:
lgpsab.scot/consultation2018
or the Audit Scotland website:
www.audit-scotland.gov.uk/report/the-cost-of-public-sector-pensions-in-scotland

In 2011, Audit Scotland reported on the cost of public sector pensions in Scotland. The focus of this review was on the costs of benefits and associated contributions. Audit Scotland summarised the advantages and disadvantages, which essentially come down to economies of scale and expertise as against transition costs and the impact on local governance.

Cost transparency code and FCA market study

Information about the cost transparency code for the local government pension scheme in England and Wales can be found on the scheme's website:
lgpsboard.org/index.php/structure-reform/cost-transparency

Information about the FCA's market study into asset management can be found at the authority's website:
www.fca.org.uk/publications/market-studies/asset-management-market-study%20

In 2015, the Financial Conduct Authority (FCA) launched an asset management market study to understand how asset managers compete to deliver value to both retail and institutional investors. The FCA found weak price competition with evidence of sustained, high profits over a number of years.

The local government pension scheme in England and Wales launched a Code of Transparency to improve investment fee transparency and consistency. The voluntary code sets standards for reporting on fees paid to asset managers and was adopted by SLGPS in 2016.

Appendix 2: Overview of advantages and disadvantages for the four options

Criteria	OPTION 1 Retain the current structure with 11 funds	OPTION 2: Promote cooperation in investing & administration between the 11 funds	OPTION 3: Pool investments between the 11 funds	OPTION 4: Merge the funds into one or more new funds
GOVERNANCE	**PROS** Maintains local decision making and connection with respect to oversight and strategy.	**PROS**	**PROS** There is not, at least at a high level, an issue of localism vs centralisation that emerges from merging/pooling; it is simply a question of investing in the most cost effective way to secure member benefits. Professionalise decision making and governance. Some representation of local authorities on a Pensions Committee, which would set broad asset allocation, risk budgets, and risk-adjusted performance criteria for the investment of the assets. Funds may be more focused on the performance and accountability of an investment pool and it is likely that they would exert a high degree of scrutiny on the performance of the pooled assets. Additional gains from better risk-management functions under the ethos that good governance should drive outcomes and not just wrap round a predetermined solution or structure. More arms-length from administering and reduced conflicts of interest.	**PROS** Reduces number of Pension Boards. A fund as large as a pooled Scottish LGPS would be able to attract and recruit the best people.

Criteria	OPTION 1 Retain the current structure with 11 funds	OPTION 2: Promote cooperation in investing & administration between the 11 funds	OPTION 3: Pool investments between the 11 funds	OPTION 4: Merge the funds into one or more new funds
	CONS Potential conflicts between Fund and Administering Authority e.g. in multi-employer fund, setting contribution rates. Duplication across funds in terms of administrative, governance, advisory, and fund management costs, and lack of scale in most of the Scottish LGPS funds. Large number of stakeholders and decision makers including committees and pension boards. Specialist staff recruitment (especially for investment) can be difficult due to terms and conditions of councils and/or for more rural funds. Lack of internal resource and staff in smaller funds have other duties to perform that can be impacted by broader council developments.	**CONS**	**CONS** Increase in consolidation of governance thus reducing local governance. A significant shift towards a more central structure such as asset pooling could remove existing functions such as trustees etc. Such change will take time and cost money, both of these factors have to be accepted and the costs and benefits of the envisaged structure would have to be clear and accepted by a wide range of stakeholders. Moreover, the gains to any long-term strategic shift in the operation of the Scottish LGPS are likely to emerge over a number of years rather than immediately or in the short-term.	**CONS** Governance would no longer be a local government function and would be the responsibility of a quango. Potential disconnect between the employer and the scheme leading to lower local engagement.

Criteria	OPTION 1 Retain the current structure with 11 funds	OPTION 2: Promote cooperation in investing & administration between the 11 funds	OPTION 3: Pool investments between the 11 funds	OPTION 4: Merge the funds into one or more new funds
INVESTMENT	**PROS** Bespoke investment strategy and implementation for each fund. Potential to collectively negotiate with existing managers to reduce fees.	**PROS** Joint procurement of investment managers or other services could lead to some efficiency gains. Potential to leverage some of the internal expertise and scale within the larger funds. Some cost efficiencies could be gained if broad mandates e.g. UK passive equities were to be invested as one large block rather than as separate mandates across a number of funds	**PROS** Significant cost savings resulting from scale. Ability to move towards greater internal management. Professionalisation of investment – FCA authorisation likely to be required. Resolves MIFID II issues. Enable the in-housing of the majority of the investment activities of the fund, which is likely to create significant cost efficiencies as well as allowing for a more dynamic investment strategy. -Increased employment as a result. Ability to invest in new asset classes/opportunities. A more transparent and uniform governance model with potential to improve returns. Collective proactive stewardship opportunities to capture the 'engagement premium' which could add up to 2 to 4% in the first year to returns. Smaller funds gain access to new investment opportunities.	**PROS** Likely that significant cost savings could be generated if there was to be a significant scaling up of pension fund assets as this increases the bargaining power of the SLGPS. Increased sustainability of SLGPS

Criteria	OPTION 1 **Retain the current structure with 11 funds**	OPTION 2: **Promote cooperation in investing & administration between the 11 funds**	OPTION 3: **Pool investments between the 11 funds**	OPTION 4: **Merge the funds into one or more new funds**
	CONS Inefficiencies will persist and not allowing benefits of scale thus risking future sustainability. Investment mandates, performance targets, and an understanding of costs and fees are unlikely to be optimal. While likely that improved disclosure via better data collection (now underway) will help improve this situation in the coming years, it does not necessarily shift the dynamic between funds and fund managers, as there is only a small increase in bargaining power. Pension funds, in all likelihood, would remain price takers. Limited options for bespoke employer investment strategies. Smaller funds lack influence unable to take an active role as a shareholder. Smaller schemes face key-person risks. MIFID II, and FCA classification of local authorities, could have major impact on investment options available.	**CONS** Relies on Pension Committees and officers being more coordinated / or compromising. Potentially a slow process. Sustainability risk e.g. if one fund decides to terminate agreement. Potential issues relating to unauthorised investment advice due to lack of FCA authorisation. Opportunity of gains limited by virtue of extant governance structures. Does not resolve MIFID II issues. Potential for smaller funds gaining access to new opportunities.	**CONS** Complexity and costs of establishing FCA authorised pool. Could be time consuming to establish. Lose local connection with funds. E&W models untested as yet so there is no track record to assess benefits.	**CONS**

Criteria	OPTION 1 **Retain the current structure with 11 funds**	OPTION 2: **Promote cooperation in investing & administration between the 11 funds**	OPTION 3: **Pool investments between the 11 funds**	OPTION 4: **Merge the funds into one or more new funds**
FUNDING	**PROS**	**PROS** Greater consistencies of funding approach, depending on service to be shared. Potential for consistent approach to employer covenant and offering different funding options including offering different investment strategies.	**PROS** Funds retain funding decisions. May provide wider range of options for different investment/funding strategies.	**PROS** Employer liabilities remain identifiable thus avoiding concerns with regard to cross-subsidy or netting of gain/losses at the time of merging funds. May provide wider range of options for different investment/funding strategies. Consistent funding approach within each new fund. (See funding challenges section in Annex 5). This could include the approach to employer covenants and the potential to offer different investment/funding options. Resolves the funding inconsistencies and the issue of risk of cessation faced by employers who are admitted to more than one fund. May be an opportunity to separate the liabilities of certain employers from others and put in place different funding arrangements, potentially reducing the exposure of the other employers in the funds. For example, certain groups of employers could be grouped for funding purposes and bespoke admission agreements/guarantees put in place e.g. third sector/charities or colleges. Improves long term sustainability of the SSLGPS.

Criteria	OPTION 1 **Retain the current structure with 11 funds**	OPTION 2: **Promote cooperation in investing & administration between the 11 funds**	OPTION 3: **Pool investments between the 11 funds**	OPTION 4: **Merge the funds into one or more new funds**
FUNDING	**CONS** Difficult to see the funding position of the Scottish LGPS as a whole. Employers who are admitted to more than one fund have inconsistent funding approaches and risk of triggering cessations. Duplication/inconsistent approach to employer covenant. Limited options for bespoke employer funding strategies.	**CONS** Limited opportunity for improvement and the cons associated with the status quo option would remain.	**CONS** Funds retain funding decisions and inconsistencies persist.	**CONS** Potential lack of customisation of assumptions for different employers.
PENSION ADMINISTRATION	**PROS** More local/ bespoke service.	**PROS** (As per merging funds, depending on the collaboration).	**PROS**	**PROS** Improved economies of scale. Consistent service for all members and employers. Removes duplication. IT system rationalisation and standardisation.

Criteria	OPTION 1 Retain the current structure with 11 funds	OPTION 2: Promote cooperation in investing & administration between the 11 funds	OPTION 3: Pool investments between the 11 funds	OPTION 4: Merge the funds into one or more new funds
	CONS Costs in some schemes will remain higher than they need to be. Inefficiencies in data submission for employers admitted to more than one fund. Inconsistent service for members, particularly evident where employers are admitted to more than one fund. Duplication of effort. Key-person risks.	**CONS** (As per merging funds, depending on the collaboration).	**CONS** As per status quo.	**CONS** Potential loss of local service / local jobs.
INFRASTRUCTURE (note that Investment comments above generally apply)	**PROS** Local funds retain decision making on the type of infrastructure investment.	**PROS** Potential to leverage expertise within existing funds.	**PROS** Scale facilitates direct and co-investments in large infrastructure projects and at lower cost.	**PROS**
	CONS Smaller funds don't have expertise to implement. Safeguards need to be put in place to prevent governmental or local issues driving investment to projects where there is no financial return to the pension fund.	**CONS** Safeguards need to be put in place to prevent governmental or local issues driving investment to projects where there is no financial return to the pension fund.	**CONS**	

Review of the Structure of the Scottish Local Government Pension Scheme

CONSULTATION RESPONSE FORM

Instructions
Responses in this form should be drafted in conjunction with the accompanying consultation report. To respond, please complete the **respondent details** and as many of the **consultation questions** your organisation wishes to complete and return the form via email to the Pensions Institute at consultation@pensions-intitute.org no later than **Friday, 7 December 2018**.

This consultation is being conducted in electronic form only, so **responses must be emailed**; hard copy posted or delivered responses cannot be received. Any queries about the consultation should be addressed to Matthew Roy, Fellow, Pensions Institute at matthew.roy@pensions-institute.org.

RESPONDENT DETAILS

Name of responding organisation(s) Please list the full name of each organisation participating in this response.	**Organisation type** Is your organisation an administering authority, employer, or employee group? Please record for each responding organisation.
full names of responding organisations	type of organisation

Authors Please list any people that wish to be recorded as authors of this response, including name, job title and organisation.	**Consent** Please confirm each author consents to their information being retained for analysing the consultation responses by writing 'confirm' by their name.
names, job tiles and organisation of authors	consents

Date Please date the response.	date

Covering information
If you wish to include covering information with your response, please include the text here. The text can wrap onto additional pages if needed.

covering text

The consultation questions follow.

CONSULTATION QUESTIONS

Question 1: Retain the current structure with 11 funds

The text can wrap onto additional pages.

a) Cost of investing:

- *How well informed do you feel about the investment costs in your fund? What information do you rely on to specify and measure these?*
- *How well does the current system manage investment costs?*
- *How would you improve the measurement and management of investment costs in the current system?*

b) Governance:

- *How well informed do you feel about the governance of your fund? What information do you rely on to measure this?*
- *How well is the current system governed?*
- *How would you improve governance of the current system?*
- *How important is it to maintain a local connection with respect to oversight and strategy?*

How would you determine if the benefits of a local connection in governance outweigh the benefits of scale?

c) Operating risks:

- *How well informed do feel about the operating risks of your fund? What information do you rely on to specify and measure these?*
- *How well are operating risks managed in the current system?*
- *How would you improve the measurement and management of operating risks in the current system?*

d) Infrastructure:

- *How well informed do you feel about your fund's investments in infrastructure? What information do you rely on?*
- *How do you rate the current system's ability to invest in infrastructure?*
- *How would you increase investment in infrastructure in the current system?*

e) Do you have any additional comments about this option?

Question 2: Promote cooperation in investing and administration between the 11 funds

The text can wrap onto additional pages.

a) Cost of investing:

- *What impact do you think promoting agreements between funds would have on investment costs?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

b) Governance:

- *What impact do you think promoting agreements between funds would have on governance?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

c) Operating risks:

- *What impact do you think promoting agreements between funds would have on operating risks?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

d) Infrastructure:

- *What impact do you think promoting agreements between funds would have on funds' ability to invest in infrastructure?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

e) Do you have any additional comments about this option?

Question 3: Pool investments between the 11 funds

The text can wrap onto additional pages.

a) Cost of investing:

- *What impact do you think pooling investments between funds would have on the cost of investing?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*
- *If asset pooling were possible, under what circumstances should a fund consider joining an asset pool?*
- *Under which circumstances should the SLGPS consider directing funds to pool?*

b) Governance:

- *What impact do you think pooling investments between funds would have on governance?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

c) Operating risks:

- *What impact do you think pooling investments between funds would have on operating risks?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

d) Infrastructure:

- *What impact do you think pooling investments between funds would have on funds' ability to invest in infrastructure?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

Do you have any additional comments about this option?

Question 4: Merge the funds into one or more new funds

The text can wrap onto additional pages.

a) Cost of investing:

- *What impact do you think mergers between funds would have on the cost of investing?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*
- *If merging were possible, under what circumstances should a fund consider a merger?*
- *Under what circumstances should the SLGPS consider directing funds to merge?*

b) Governance:

- *What impact do you think mergers between funds would have on governance?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

c) Operating risks:

- *What impact do you think mergers between funds would have on operating risks?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

d) Infrastructure:

- *What impact do you think mergers between funds would have on funds' ability to invest in infrastructure?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

e) Do you have any additional comments about this option?

Question 5: Preferred and additional options

The text can wrap onto additional pages.

a) **Which option does your organisation prefer? Please explain your preference.**
b) **What other options should be considered for the future structure of the LGPS?**
c) **What would be the advantages and disadvantages of these other option for funds' investment costs, governance, operating risks and ability to invest in infrastructure?**
d) **Are there any other comments you would like to make?**

The consultation questions end.

This page is intentionally left blank

1. In line with best practice and the Pensions Regulator (tPR) Code of Practice, NESPF maintains a risk register to ensure the risks the Fund faces are properly understood and risk mitigation actions are in place.
2. The risk register is review and updated quarterly, with reporting to the Pensions Committee.

3. RAG Summary as at August 2018

Catastophic	9, 18	1, 16, 21	6			
Critical		4, 19, 20	8, 15, 25	14, 24		
Marginal	17	2, 5, 13, 29	7, 11, 12, 22, 23	3, 10, 28		26
Negligle						
Impact / Likelihood	**Almost impossible**	**Very Low**	**Low**	**Significant**	**High**	**Extremely High**

Pension Fund Risk Register

No	Risk Description	Effect/Consequences	Current Controls	Current Risk			Risk Movement	Current Status/Progress
				Impact	Likelihood	Score		
Pension Fund Level								
1	Lack of effective Risk Management	Failure to identify and respond to risks will impact on service delivery capabilities	Pension Fund Risk Register is reviewed and updated quarterly	4	2	**8**	↔	Ongoing
2	Poor Governance	Lack of a robust and effective governance framework and suitable policies/procedures could create a regulatory compliance issue, lead to poor service delivery and reputational risk	The Fund has in place an annual review of its governance statement and supporting policies and procedures, ensuring both regulatory and Council objectives compliance	2	2	**4**	↔	Ongoing - annual review reported to Committee
3	Lack of Performance Measures	Failure to monitor performance across the Fund will provide a lack of transparancy on delivering an efficient and effective service	The Fund has in place both statutory and local KPI's	2	4	**8**	↔	The Fund particpates in national benchmarking exercises and has internal measures which are reported to Committee
4	Failure of Pensions Committee and Pension Board to operate effectively	Failure to ensure effective joint working will result in non-compliance with regulatory requirements, inability to make decisions or policies, reputational risk	Annual review of Committee and Board, in consultation with both	3	2	**6**	↔	Annual Report to Committee and Board on effectiveness and training (March 2018)
5	Operational disaster, unable to access the workplace	Loss of service delivery, staff downtime	Disaster Recovery Policy in place, incorporated into ACC	2	2	**4**	↔	Ongoing - review underway and Pension Fund Team to be made fully aware once complete
6	Failure to recruit and develop staff	Service delivery and succession planning at risk	Individual staff training plans reviewed annually, ongoing review of staffing requirements	4	3	**12**	↔	Several vacant posts to be filled
7	Pay and price inflation valuation assumptions either higher or lower	Potential Increase in employer contribution rates	Funding updates reported to Committee quarterly	2	3	**6**	↔	Information provided by FMS
Governance								
8	Failure to comply with LGPS Regulations, Pensions Act, HMRC and other overriding legislation	Audit criticism, legal challenge, reputational risk, financial loss/penalties	Six monthly compliance review and annual report to Committee	3	3	**9**	↔	Ongoing - reported to Committee (March 2018)

9	Failure to comply with FOI requests	Audit criticism, legal challege, reputational risk	Internal controls in place to ensure deadlines adhered to, Pension Fund Manager responsible for all FOI requests	4	1	**4**	↔	Ongoing
10	Conflicts of Interest	Audit criticism, legal challenge, reputational risk	Regular discussions between CO-Finance and Pension Fund Manager. Areas of risk and conflict declared at Pensions Committee and Pension Board meetings, conflicts register to record and monitor	2	4	**8**	↔	Ongoing
Benefit Adminstration								
11	Requirement to complete GMP reconcilliation	Failure to ensure future member benefits are calculated correctly, audit critism and financial loss	Appointment of GMP Project Team	2	3	**6**	↔	Ongoing
12	Fraud/Negligence	Overpayment/unauthorised payments, system corruption, audit criticism, legal challenge, reputational risk	Pension payments signed off by a SPO-Benefits, segreagation of duties for staff authorising/submitting lump sum payments. Admin to Pay to be implemented in 2018.	2	3	**6**	↔	Ongoing - regular reporting to Committee in place.
13	Overpayments of pension benefits	Audit criticism, legal challege, reputational risk	Pension payments signed off by a SPO-Benefits, segreagation of duties for staff authorising/submitting lump sum payments	2	2	**4**	↔	Ongoing
Investments								
14	Insufficient assets to meet the Fund's long term liabilities	Increase in employer contribution rates and investment risk, audit criticism, legal challege, reputational risk, financial loss	Quarterly assessment of investment performance and funding updates, tri-ennial valuation and investment strategy review	3	4	**12**	↔	Ongoing
15	Failure to monitor investment managers and assets	Audit criticism, legal challenge and reputational risk	Quarterly assessment of asset performance and regular meetings with managers	3	3	**9**	↔	Ongoing

16	Failure of work stock markets	Increase in employer contribution rates, financial loss	Diversification of scheme assets, tri-ennial valuation and investment strategy review	4	2	**8**	↔	Ongoing - revised investment strategy to Committee (March 2018)
17	Negligence/fraud/default by investment managers	Financial loss, reputational damage	Due diligence on appointment and appropriate clause in legal agreements, fund management monitoring, SAS 70 reports	2	1	**2**	↔	Ongoing
18	Failure of Global Custodian	Loss of assets or control of assets	Regular meetings with custodian, receipt of SAS 70 reports and monitoring	4	1	**4**	↔	Ongong - new custodian appointed April 2018
Accounting								
19	Poor financial reporting	Qualified accounts	Comprehensive policies and procedures in place	3	2	**6**	↔	Ongoing
20	Annual review of Code of Practice and any other overriding regulations	Qualified accounts	Review of Code, attending CIPFA meetings/reviews	3	2	**6**	↔	Ongoing
Technical								
21	Failure to secure and manage personal data in line with Data Protection requirements	Audit criticism, legal challege, reputational risk, financial penalties	Internal control and procedures for management of data, project group set up to implement GDPR & assess current processes.	4	2	**8**	↔	Ongoing - revised policies and procedures implementated from May 2018 for GDPR
22	Failure of the Fund's administration system	Staff downtime, loss of service delivery	The administration system is hosted externally with back-up in separate location	2	3	**6**	↔	Quarterly report is provided to Pension Fund Manager on any hosted system errors/resolutions
23	Failure to carry out effective member tracing	Incorrect pension payments made, incorrect assesstment of actuarial liabilities	Tracing Service in place (ATMOS)	2	3	**6**	↔	Ongoing
Employer Relationship								
24	Failure to monitor employer covenant	Orphaned liabilities could fall on remaining employers	Continued implementation of Employer Covenant Policy	3	4	**12**	↔	Ongoing
25	Changes in early retirement strategies by employers	Pressure on cash flows	ERT to manage through Employer Covenant Policy and discretions	3	3	**9**	↔	Ongoing
26	Employers leaving Scheme/closing to new members	Orphaned liabilites could fall to remaining employers	ERT to manage through Employer Covenant Policy	2	6	**12**	↔	Ongoing

27	Longevity	Increase in employer contribution rates	Actuarial valuation every 3 years which undertakes scheme specific analysis including review of life expectancy/mortality assumptions	2	2	4		Ongoing - revised Investment Strategy and FSS to Committee following tri-ennial valuation (March 2018)
28	Employer contributions not received, collected or recorded accurately	Orphaned liabilites could fall to remaining employers	Accounting Team escalate any issues to Governance/ERT Team, with escalation to tPR if persists. Breaches Policy and Register in place	2	4	**8**		Ongoing
29	Failure to maintain member records; data incomplete or inaccurate	Incorrect pension payments made, incorrect assessment of actuarial liabilities	All employers required to submit monthly data which is reconcilled by the ERT	2	2	4		Quarterly PAS reporting to Committee

This page is intentionally left blank

Exempt information as described in paragraph(s) 6 of Schedule 7A
of the Local Government (Scotland) Act 1973.

Document is Restricted

This page is intentionally left blank

Exempt information as described in paragraph(s) 6 of Schedule 7A
of the Local Government (Scotland) Act 1973.

Document is Restricted

This page is intentionally left blank