Public Document Pack

To: Councillor Malik, Convener; Councillor Reynolds, Vice Convener; Councillor Barney Crockett, the Lord Provost; and Councillors Bell, Cooke, Delaney, Henrickson, MacGregor and Wheeler (Pensions Committee); and Councillor McKelvie, Chairperson; Mr N Stirling, Vice Chairperson; Councillors Allan and Cowe; and Mr I Hodgson, Mr L Knox, Mrs M Lawrence and Mr A Walker (Pension Board).

Town House,
ABERDEEN, 18 March 2021

PENSIONS COMMITTEE AND PENSION BOARD

The Members of the **PENSIONS COMMITTEE AND PENSION BOARD** are requested to meet **remotely on FRIDAY, 26 MARCH 2021 at 10.30am.**

FRASER BELL
CHIEF OFFICER - GOVERNANCE

In accordance with UK and Scottish Government guidance, meetings of this Committee will be held remotely as required. In these circumstances the meetings will be recorded and available on the Committee page on the website.

B U S I N E S S

NOTIFICATION OF URGENT BUSINESS

1.1 There are no items of urgent business at this time

DETERMINATION OF EXEMPT BUSINESS

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

DECLARATIONS OF INTEREST

3.1 Members are requested to intimate any declarations of interest (Pages 5 - 6)

MINUTES OF PREVIOUS MEETINGS

4.1 Minute of Previous Meeting of 11 December 2020 (Pages 7 - 10)

COMMITTEE BUSINESS PLANNER

5.1 Business Planner (Pages 11 - 12)

NOTICES OF MOTION

6.1 There are currently no motions to the Pensions Committee

INTERNAL AND EXTERNAL AUDIT

7.1 North East Scotland Pension Fund Annual Audit Plan 2020/21 - Report by External Audit (Pages 13 - 26)

FINANCE / INVESTMENT

8.1 Budget/Forecast and Projected Spend 2020/21 - PC/MAR21/BUD (Pages 27 - 34)

8.2 Investment Strategy - PCMAR21/REVIEW (Pages 35 - 40)

8.3 2020 Tri-Ennial Valuation Results - PC/MAR21/VAL (Pages 41 - 230)

8.4 Statement of Accounts Action Plan - PC/MAR21/ACCOUNTS (Pages 231 - 234)

GOVERNANCE / COMPLIANCE

9.1 Review of NESPF Compliance with PSPA 2013 and Pension Regulator Requirements - PC/MAR21/GOV (Pages 235 - 240)

9.2 Administration Review - PC/MAR21/ADMIN (Pages 241 - 250)

9.3 Strategy - PC/MAR21/STRAT (Pages 251 - 278)

EXEMPT BUSINESS - NOT FOR PUBLICATION

10.1 Accommodation - PC/MAR21/ACCO (Pages 279 - 298)

10.2 Asset and Investment Manager Performance Report - PC/MAR21/AIMPR (Pages 299 - 328)

EHRIAs related to reports on this agenda can be viewed here
To access the Service Updates for this Committee please click here

Website Address: aberdeencity.gov.uk

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

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DECLARATIONS OF INTEREST

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.

PENSIONS COMMITTEE AND PENSION BOARD

ABERDEEN, 11 December 2020. Minute of Meeting of the PENSIONS COMMITTEE AND PENSION BOARD. Present:- Councillor Malik, Convener; Councillor Reynolds, Vice-Convener; Councillor Barney Crockett, the Lord Provost; and Councillors Bell, Cooke, Delaney (to article 9), Henrickson, MacGregor and Wheeler (Pensions Committee); and Councillor McKelvie, Chairperson; Mr N Stirling, Vice Chairperson; Councillor Allan; Mr I Hodgson, Mr L Knox, Mr K Luke and Mr A Walker (Pension Board).

Also in attendance:- Jonathan Belford, Chief Officer – Finance; Laura Colliss, Pensions Manager; Graham Buntain, Investment Manager; and Colin Morrison, Audit Scotland.

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 9.1 (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 the above-mentioned item 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 OF 29 SEPTEMBER 2020

3. The Committee had before it the minute of its previous meeting of 29 September 2020.

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

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

PENSIONS COMMITTEE AND PENSION BOARD
11 December 2020

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 planner.

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

BUDGET/FORECAST & PROJECTED SPEND 2020/21 - PC/DEC20/BUD

5. The Committee had before it a report by the Chief Officer – Finance which provided details of the Management Expenses Budget/Forecast and Projected Spend 2020/21 for the North East Scotland Pension Fund (NESPF).

The report recommended:-
that the Committee note the update on the NESPF Management Expenses Budget/Forecast and Projected Spend 2020/21, shown in Appendix I.

The Committee resolved:-
to approve the recommendation.

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

TRIENNIAL VALUATION AND FUNDING STRATEGY STATEMENT - PC/DEC20/VAL

6. The Committee had before it a report by the Director of Resources which provided details of the 2020 triennial valuation for the North East Scotland Pension Fund including the proposed assumptions outlined in the Draft Funding Strategy Statement.

The report recommended:-
that Committee –
(a) agree the Funding Approach outlined in the 2020 Funding Strategy Statement including the assumptions used in the calculation of the Fund liabilities for the triennial valuation as at 31 March 2020; and
(b) note the overall whole Fund valuation as at 31 March 2020 (using the proposed assumptions).

The Committee resolved:-
to approve the recommendations.

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

STRATEGIC INFRASTRUCTURE PARTNERSHIP WITH ABERDEEN CITY COUNCIL - PC/DEC/INFRA

7. With reference to article 9 of the minute of its meeting of 15 March 2019, the Committee had before it a report by the Director of Resources following the instruction to the Chief Officer – Finance to explore the opportunities for a strategic partnership between the Council and the North East Scotland Pension Fund (NESPF) for the purposes of supporting local infrastructure investment, and report back on the feasibility.

The report recommended:-
that Committee note the content of the report and agree that the Pension Manager maintain a watching brief on the development of investor ready opportunities in the City Region area.

The Committee resolved:-
to approve the recommendation.

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

STRATEGY - PC/DEC20/STRAT

8. The Committee had before it a report by the Director of Resources which informed the Committee of any changes to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund.

The report provided an update on the Scottish Public Pensions Agency (SPPA) Consultation which sought views on changes to the Local Government Pension Scheme (LGPS) in Scotland in respect of the LGPS statutory underpin protection to remove unlawful discrimination found by the Courts in relation to public service pension scheme ‘transitional protection’ arrangements and included the consultation response prepared by officers for information; the position in relation to Pension Fund Annual Benefit Statements, and that there had been 99.74% compliance for all benefit statements in 19/20 (active, deferred and Councillors) which was a slight decrease from the reported figure of 99.86% in 18/19, although this was attributed to the current challenging circumstances as a result of the pandemic; information on the uptake of the online system instead of paper letters and statements; the on-time completion of the fit out of Marischal Square; the online annual Financial Forum with presentations provided by the Scheme Actuary, Mercer and Fund Officers; and the completion on time of the Aberdeen City Council Transport Buy-In.

The report recommended:-
that Committee note the final outcome of the annual benefit statement project, which was completed successfully, for reassurance (3.9.2 of the report refers).

The Committee resolved:-
to approve the recommendation.

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

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

9. The Committee had before it a report by the Chief Officer - Finance which provided an overview of the investment activity of both the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund for the three month period ending 30 September 2020.

Appended to the report was information in respect of the NESPF and environmental, social and governance (ESG) matters and responsible investment.

The Committee and Board heard from Mr Buntain, Investment Manager, in respect of the detail contained within the report. Mr Buntain highlighted that the ESG appendix now included additional carbon footprint data where this was available.

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

The Committee resolved:
to note the report.

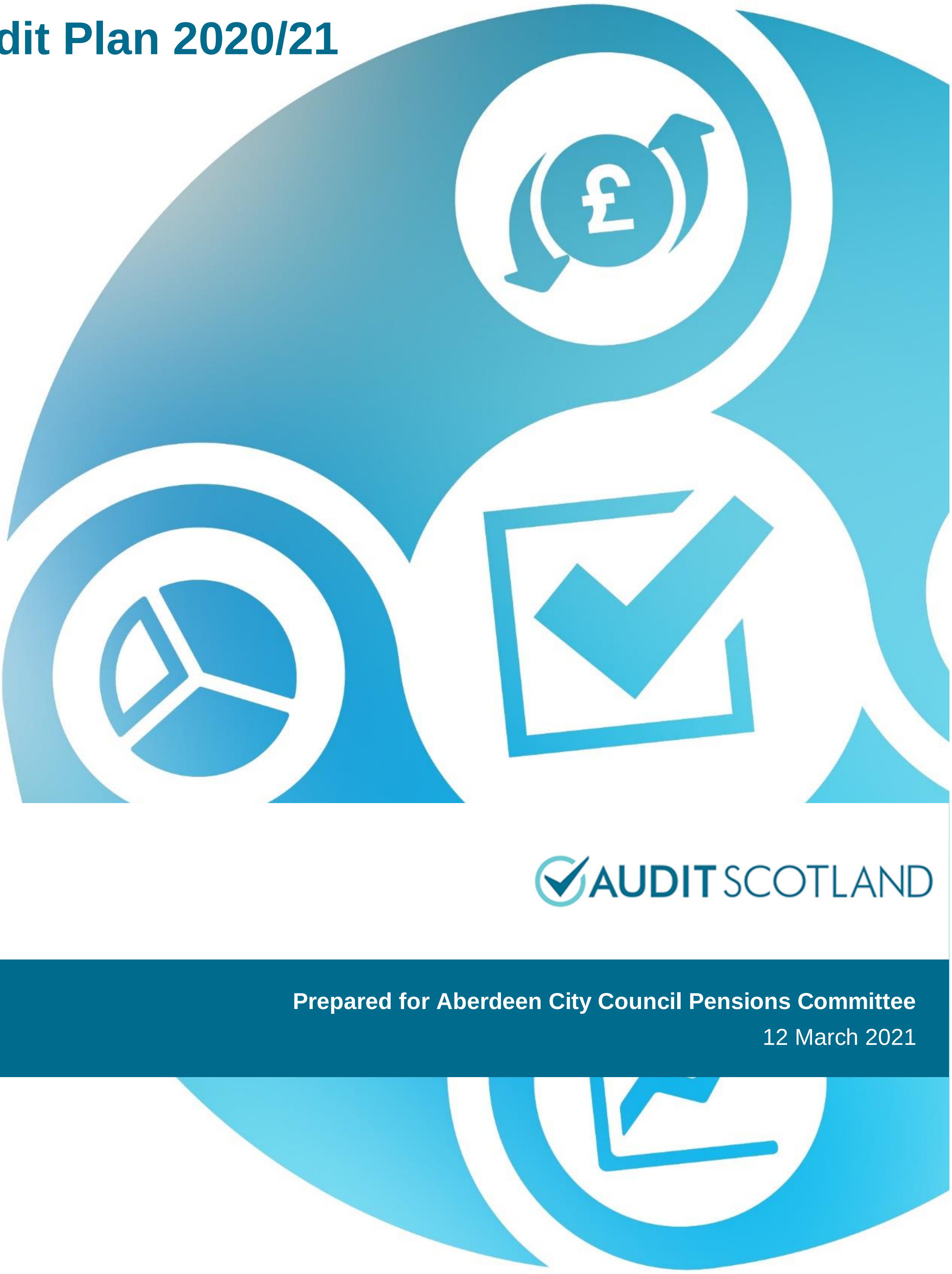
The Board resolved:-
to note the decision of the Committee.
- **COUNCILLOR M. TAUQEER MALIK, Convener**

	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	**26 March 2021**								
4	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	1.4		
5	Review of NESPF Compliance with PSPA 2013 and Pension Regulator Requirements	To provide Elected Members with a review of NESPF compliance with the Public Service Pensions Act 2013 and the Pensions Regulator requirements during the financial year 2020/21		Mairi Suttie	Finance	Resources	4.1 and 4.2		
6	Investment Strategy Update	To provide an update on the investment strategy of the NESPF		Graham Buntain / Laura Colliss	Finance	Resources	1.1		
7	Administration Review	To provide details of an administration review carried out by the scheme actuary (Mercer) and the North East Scotland Pension Fund (the Fund) to gain efficiencies and improve member outcomes		Gary Gray	Finance	Resources	4.1		
8	External Audit Annual Audit Plan	To present the annual audit plan		Rachel Browne	External Audit	External Audit	2.1		
9	2020 Tri-ennial Valuation Results	To provide details of the triennial valuation as at 31 March 2020 for the NESPF and the ACCTF in advance of the sign off by the scheme actuary in March 2021		Claire Mullen	Finance	Resources	1.1 and 4.1		
10	Statement of Accounts Action Plan	To provide Elected Members with high level information and key dates to the 2020/21 Statement of Accounts including linkages to the plans and timetables of the Council's External Auditors		Laura Colliss	Finance	Resources	3.1		
11	Accommodation	To provide an update to members on the recent relocation of the NESPF		Laura Colliss	Finance	Resources	1		
12	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	1.1 and 5.2		
13	Budget Forecast & Projected Spend	Update on budget and annual spend to date		Michael Scroggie	Finance	Resources	1.3		
14	**25 June 2021**								
15	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	1.4		
16	Investment Strategy Update	To provide an update on the investment strategy of the NESPF if required		Graham Buntain / Laura Colliss	Finance	Resources	5.2		
17	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	5.2		
18	Budget Forecast & Projected Spend	Update on budget and annual spend to date		Michael Scroggie	Finance	Resources	1.3		

	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**
19	Annual Effectiveness Report - Pensions Committee	To present the annual effectiveness report		Stephanie Dunsmuir	Governance	Commissioning	GD 8.5	D	This report will now be presented in December to allow sufficient data to be collected due to the cancellation of some meetings in 2020
20	Internal Audit Annual Report 2020/21	To present the Internal Audit Annual Report for 2020/21		Colin Harvey	Internal Audit	Internal Audit	2.1		
21	Draft NESPF Annual Report & Accounts	To present the draft annual accounts		Laura Colliss	Finance	Resources	3.1		
22	**17 September 2021**								
23	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	1.4		
24	Investment Strategy Update	To provide an update on the investment strategy of the NESPF		Graham Buntain / Laura Colliss	Finance	Resources	5.2		
25	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	5.2		
26	Budget Forecast & Projected Spend	Update on budget and annual spend to date		Michael Scroggie	Finance	Resources	1.3		
27	NESPF Annual Report & Accounts	To present the audited annual accounts and report on the NESPF		Laura Colliss	Finance	Resources	3.1		
28	External Audit Annual Audit Report 2020/21	To present the External Audit Annual Audit Report 2020/21		Rachel Browne	External Audit	External Audit	2.1		
29	**10 December 2021**								
30	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	1.4		
31	Investment Strategy Update	To provide an update on the investment strategy of the NESPF if required		Graham Buntain / Laura Colliss	Finance	Resources	5.2		
32	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	5.2		
33	Budget Forecast & Projected Spend	Update on budget and annual spend to date		Michael Scroggie	Finance	Resources	1.3		

North East Scotland Pension Fund

Annual Audit Plan 2020/21



AUDIT SCOTLAND

Prepared for Aberdeen City Council Pensions Committee

12 March 2021

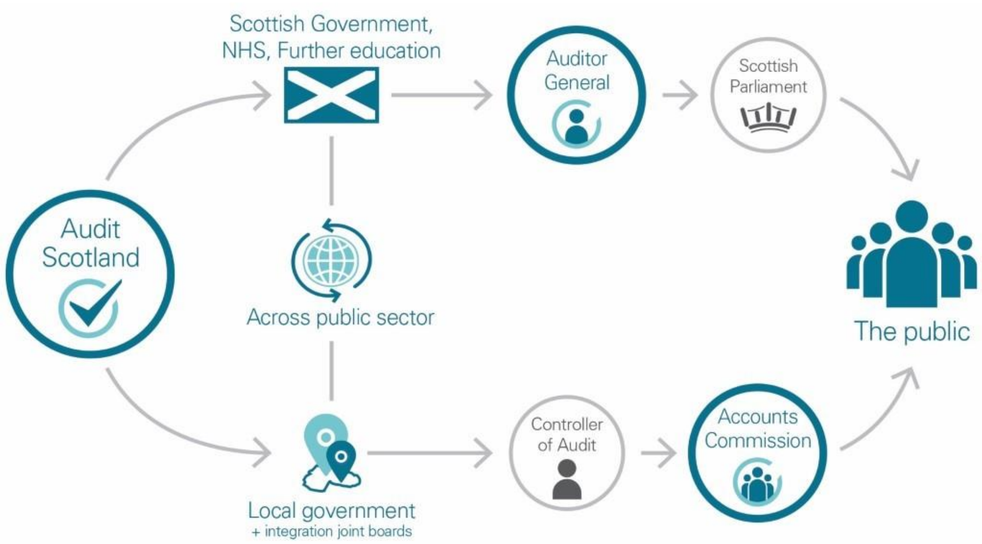
Who we are

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

Audit Scotland's 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

Risks and planned work

1. Our audit of the North East Scotland Pension Fund (the Fund) is carried out in accordance with the Code of Audit Practice, International Standards on Auditing (ISAs), and guidance on planning the audit. This plan contains an overview of the planned scope and timing of our audit. It sets out the work necessary to allow us to provide an independent auditor's report on the financial statements and to meet the wider scope requirements of public sector audit.

2. The wider scope of public audit contributes to assessments and conclusions on financial management, financial sustainability, governance and transparency, and value for money.

3. The public health crisis caused by the coronavirus disease 2019 (Covid-19) pandemic has had a significant and profound effect on every aspect of Scottish society. Public services have been drastically affected, requiring immediate changes to the way they are provided. The impact on public finances has been unprecedented, which has necessitated both the Scottish and UK governments providing substantial additional funding for public services as well as support for individuals, businesses and the economy. It is likely that further financial measures will be needed and that the effects will be felt well into the future.

4. Public audit has an important contribution to the recovery and renewal of public services. The Auditor General for Scotland, the Accounts Commission and Audit Scotland are responding to the risks to public services and finances from Covid-19 across the full range of audit work including annual audits and the programme of performance audits. Audit Scotland views 2020/21 as a transitional year, leading in future to audit timetables which were possible before Covid-19. The well-being of audit teams and the delivery of high-quality audits remain paramount. Maintaining a pragmatic and flexible approach will enable change at short notice as new issues emerge, or if current risks change in significance. Where this impacts on annual audits, an addendum to this annual audit plan may be necessary.

Adding value

5. We aim to add value to the Fund through our external audit work by being constructive and forward looking, by identifying areas for improvement and by recommending and encouraging good practice. In so doing, we intend to help the Fund promote improved standards of governance, better management, and decision making, and more effective use of resources.

Audit risks

6. Building on our knowledge from previous years, discussions with staff, attendance at Pensions Committee meetings and a review of supporting information we have identified a number of significant financial statement and wider dimension audit risks. These risks are detailed in Exhibit 1.

Exhibit 1
2020/21 Significant audit risks

Significant Audit Risk		Source of assurance	Planned audit work
Financial statement risks			
1	**Management override of controls** International Standard on Auditing (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 to change the position disclosed in the financial statements.	Owing to the nature of this risk, assurances from management are not applicable in this instance.	• Detailed testing of journal entries. • Review of accounting estimates. • Focused testing of accruals and prepayments. • Evaluation of significant transactions that are outside the normal course of business.
2	**Estimation, judgements and classification** There is a significant degree of subjectivity in the measurement and classification of certain investments and in the actuarial valuation. North East Scotland Pension Fund investments include investments such as property, unquoted equity and pooled funds, where valuations involve the application of judgement in determining appropriate amounts. 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. The Transport Fund insurance buy-in contract will be subject to an annual actuarial valuation. This subjectivity entails a risk of misstatement in the financial statements.	The majority of investments are listed and traded on public stock exchanges which provide frequent valuations. Unquoted investments are valued by third parties including investment managers and independent valuers who follow detailed professional, accounting and industry guidelines. Use of an experienced and respected actuary to provide actuarial valuations.	• Completion of 'review of the work of an expert' in accordance with ISA 500, for significant unquoted investments. • Confirmation of valuations to valuation reports and/ or other supporting documentation. • Completion of 'review of the work of an expert' in accordance with ISA 500, for the work of the actuary. • Consideration of the report by the consulting actuary to Audit Scotland on actuarial assumptions in use in 2020/21.
3	**Transport Fund Insurance Buy-In Contract** In 2020/21 the Pension Fund entered into an insurance buy-in contract to cover the cost of paying pensioners within the Transport Fund. This is a new arrangement and we will carry out additional audit procedures to	Both parties have very specific contractual responsibilities that are closely monitored. Cashflows will be reconciled and the Scheme Actuary will value the ongoing pensioner liabilities.	• Review of accounting disclosures and management commentary. • Confirmation of valuations to supporting documentation (as noted at no.2 above).

Significant Audit Risk		Source of assurance	Planned audit work
	ensure that it is accounted for correctly.		
Wider dimension risks			
4	**Public scrutiny by those charged with governance** We noted that scrutiny of the annual accounts and audit reports can be limited in comparison to other Pensions Committee reports and would encourage members to strengthen their scrutiny of the annual report and accounts as the Fund's primary vehicle to demonstrate stewardship of public funds. There is a risk of ineffective scrutiny, challenge and transparency on the decision making and on the financial and performance reporting.	The Fund reports and engages with the committee throughout the process via quarterly reporting. The committee has sight of the draft annual accounts and the audited accounts through consultation and meetings, while receiving budget/forecast reports each quarter. Training is provided internally and externally and attendance is encouraged and monitored.	• Review of member training arrangements: training needs assessments, sessions arranged by officers, and sessions attended. • Attendance at Pensions Committee meeting to observe the presentation of annual report and accounts and the scrutiny thereon.

Source: Audit Scotland

7. As set out in ISA 240, there is a presumed risk of fraud in the recognition of income. There is a risk that income may be misstated resulting in a material misstatement in the financial statements. We have rebutted the risk of material misstatement caused by fraud in income recognition in 2020/21 for the following reasons:

- The split of responsibilities between the Fund, its fund managers, its custodian and the bank provide a clear separation of duties reducing the risks relating to investment income.
- Further controls are in place around contribution income which is paid over from employers.

8. In line with Practice Note 10, as most public sector bodies are net expenditure bodies, the risk of fraud is more likely to occur in expenditure. We have rebutted the risk of material misstatement caused by fraud in expenditure in 2020/21 for the following reasons:

- Investments are managed by external investment managers and recorded by the Fund's custodian.
- Pension benefits are the Fund's main expenditure stream. There is no real incentive for the Fund to manipulate the amount of benefits paid.
- Controls are in place to ensure the proper amounts of benefits paid.

9. Although we have rebutted these presumed risks of material misstatement arising from fraud, we will still undertake standard audit procedures around journal testing and cut-off for both income and expenditure.

Reporting arrangements

10. Audit reporting is the visible output for the annual audit. All annual audit plans, and the outputs as detailed in Exhibit 2 and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

11. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

12. At the end of our audit we will provide the Aberdeen City Council Pensions Committee, the Aberdeen City Council Chief Officer – Finance, and the Controller of Audit with an annual audit report containing observations and recommendations on significant matters which have arisen during the audit. We will also issue an independent auditor's report containing our opinion on the financial statements.

Exhibit 2
2020/21 Audit outputs

Audit Output	Target date	Committee Date
Annual Audit Plan	26 March 2021	26 March 2021
Annual Audit Report	17 September 2021	17 September 2021
Independent Auditor's Report	17 September 2021	17 September 2021

Source: Audit Scotland

Audit fee

13. The audit fee for the 2020/21 audit of the Fund is £43,000 (2019/20: £40,880). In determining the audit fee, we have taken account of the risk exposure of the Fund, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited annual accounts, with a complete working papers package on 12 July 2021.

14. Where our audit cannot proceed as planned through, for example, late receipt of unaudited annual accounts or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

Responsibilities

Aberdeen City Council Pensions Committee and Chief Officer - Finance

15. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance that enable them to successfully deliver their objectives.

16. The audit of the annual accounts does not relieve management or the Aberdeen City Council Pensions Committee, as those charged with governance, of their responsibilities.

Appointed auditor

17. Our responsibilities as independent auditors are established by the Local Government (Scotland) Act 1973 and the Code of Audit Practice (including supplementary guidance) and guided by the Financial Reporting Council's Ethical Standard.

18. Auditors in the public sector give an independent opinion on the financial statements and other information within the annual accounts. We also review and report on the arrangements within the audited body to manage its performance and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Annual accounts

19. The audit of the annual accounts, including the financial statements, will be the foundation and source for most of the work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of the Fund and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how the Fund will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free from material misstatement.

20. We will give an opinion on whether the financial statements:

- give a true and fair view of the financial transactions of the Fund during the year ended 31 March 2021 and the amount and disposition as at that date of its assets and liabilities
- have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union, as interpreted and adopted by the Code of Practice on Local Authority Accounting in the UK 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.

Statutory other information in the annual accounts

21. We also review and report on statutory other information published within the annual accounts including the management commentary, annual governance statement and the governance compliance statement. We give an opinion on whether these statements have been compiled in accordance with the appropriate regulations and frameworks in our independent auditor's report.

22. We also review the content of the pension fund annual report for consistency with the financial statements and with our knowledge. We consider whether the information is otherwise materially misstated. We report any uncorrected material misstatements in statutory other information.

Materiality

23. We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinions in the independent auditor's report.

24. We calculate materiality at different levels as described below. The calculated planning materiality values for the Fund are set out in Exhibit 3.

Exhibit 3
Materiality values

Materiality	Main Fund	Transport Fund
Planning materiality – This is the figure we calculate to assess the overall impact of audit adjustments on the financial statements. For 2020/21 it has been set at 1% of gross assets, based on the latest audited accounts, which are the 2019/20 annual accounts.	£44 million	£3.1 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 65% of planning materiality.	£28.5 million	£2 million
Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements more than the 'reporting threshold' amount. This has been calculated at 2.5% of planning materiality (with a maximum of £250,000 as Audit Scotland considers that the Scottish public would perhaps find it unreasonable that an amount beyond this maximum could ever be described as "clearly trivial").	£250 thousand	£80 thousand

Source: Audit Scotland

Lower specific materiality

25. In addition to planning materiality we set lower, specific materiality levels for certain classes of transaction, account balances or disclosures where lesser amounts could influence the decisions of the users of the accounts.

26. We recognise that pension benefits payable to members are of importance to the users of the accounts and we set specific materiality levels as shown in Exhibit 4.

Exhibit 4
Lower specific materiality values

Materiality	Main Fund	Transport Fund
Specific materiality - It has been set at 10% of benefits payable, based on the latest audited accounts, which are the 2019/20 annual accounts.	£15.5 million	£0.9 million
Specific performance materiality – Using our professional judgement we have calculated performance materiality at 65% of the specific materiality.	£10 million	£0.6 million

Source: Audit Scotland

Timetable

27. To support the efficient use of resources it is critical that an annual report and accounts timetable is agreed with us to produce the unaudited accounts. We have included an agreed timetable at Exhibit 5.

Exhibit 5
Annual accounts timetable

Key stage	Date
Consideration of unaudited annual report and accounts by those charged with governance	25 June 2021
Latest submission date of unaudited annual report and accounts with complete working papers package	12 July 2021
Latest date for final clearance meeting with Pensions Manager and Aberdeen City Council Chief Officer - Finance	25 August 2021
Agreement of audited unsigned financial statements Issue of Annual Audit Report including ISA 260 report to those charged with governance	17 September 2021
Independent auditor's report signed	17 September 2021

Source: Audit Scotland

Internal audit

28. Internal audit is provided by the Aberdeenshire Council internal audit service, overseen by the Interim Chief Internal Auditor. As part of our planning process we carried out an annual assessment of the internal audit function to ensure that it operates in accordance with Public Sector Internal Audit Standards (PSIAS).

29. We concluded that internal audit has sound documentation standards and reporting procedures in place and complies with the main requirements of the Public Sector Internal Audit Standards (PSIAS).

Using the work of internal audit

30. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible to avoid duplication.

31. Internal audit's planned 2020/21 audit review for the Fund is Pensions Payroll, to provide assurance that appropriate arrangements are in place to ensure the accuracy and appropriateness of payments made to scheme members. This will include testing of new and on-going pensions, and transfer and termination of pension payments.

32. We do not plan to place formal reliance on internal audit's work for our 2020/21 financial statements audit. The sample sizes within this work will not significantly reduce the level of our audit testing in support of our audit opinion on the financial statements. We consider it more efficient while auditing remotely to carry out testing ourselves rather than placing formal reliance on internal audit's work which requires detailed review of the internal audit file and an element of re-performance. Internal audit's work will give us additional comfort over the pensions payroll.

Audit dimensions

33. Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in Exhibit 6.

Exhibit 6
Audit dimensions

Source: Code of Audit Practice

Financial sustainability

34. As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the Fund's financial sustainability. We define financial sustainability as having medium term (two to five years) and longer term (greater than five years) financial plans in place. We will carry out work and conclude on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of funding arrangements and the investment strategy in place to address any identified funding gaps
- whether there are arrangements in place to demonstrate the affordability and effectiveness of funding and investment decisions.

Financial management

35. Financial management in the context of a pension fund is complex and includes not just investment and funding strategy, but also arrangements for contract management, performance review, budget setting, forecasting and the financial control environment. We will review, conclude and report on:

- the Fund's financial performance and funding levels for the year, including performance against its investment strategy
- whether arrangements are in place to ensure systems of internal control are operating effectively
- the effectiveness of the budgetary control system in communicating accurate and timely financial performance
- how the Fund has assured itself that its financial capacity and skills are appropriate

- whether there are appropriate and effective arrangements in place for the prevention and detection of fraud and corruption.

Governance and transparency

36. 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. The knowledge and skills of Pensions Committee and Pension Board members is key to this process. We will review, conclude and report on:

- the governance disclosures in the annual report and accounts
- whether the Fund can demonstrate that the governance arrangements in place are appropriate and operating effectively
- whether there is effective scrutiny, challenge and transparency on the decision making and on the financial and performance reporting
- the quality and timeliness of financial and performance reporting on the Fund's administration and investments
- consistency of the annual governance statement and the governance compliance statement with the disclosures made in the financial statements.

Value for money

37. Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether the Fund can demonstrate:

- value for money in the use of resources
- there is a clear link between money spent, output and outcomes delivered.
- that outcomes are improving.
- there is sufficient focus on improvement and the pace of it.

Independence and objectivity

38. Auditors appointed by the Accounts Commission or Auditor General for Scotland must comply with the Code of Audit Practice and relevant supporting guidance. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual "fit and proper" declaration for all members of staff. These arrangements are overseen by the Director of Audit Services, who serves as Audit Scotland's Ethics Partner.

39. The engagement lead (i.e. appointed auditor) for the Fund is Gillian Woolman, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of North East Scotland Pension Fund.

Quality control

40. International Standard on Quality Control 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

41. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice (and relevant supporting guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews and internal quality reviews. The Institute of Chartered Accountants of Scotland (ICAS) have also been commissioned to carry out external quality reviews of our work.

42. As part of our commitment to quality and continuous improvement Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time and this may be directed to the engagement lead.

North East Scotland Pension Fund

Annual Audit Plan 2020/21

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ABERDEEN CITY COUNCIL

COMMITTEE	Pensions Committee
DATE	26 March 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	Budget/Forecast & Projected Spend 2020/21
REPORT NUMBER	PC/MAR21/BUD
DIRECTOR	Steven Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHOR	Michael Scroggie
TERMS OF REFERENCE	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 and Projected Spend 2020/21 for the North East Scotland Pension Fund (NESPF).

2. RECOMMENDATION

2.1 That the Committee note the update on the NESPF Management Expenses Budget/Forecast and Projected Spend 2020/21, shown in Appendix I.

3. BACKGROUND/MAIN ISSUES

3.1 BUDGET/FORECAST AND PROJECTED SPEND 2020/21

3.1.1 Appendix I shows the NESPF Budget 2020/21. The budget includes a re-alignment of cost headings that 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 few 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 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 in this report.

6. MANAGEMENT OF RISK

6.1 There are no direct risk implications arising from the recommendation in this report.

7. OUTCOMES

7.1 This report does not impact on the Council Delivery Plan.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

North East Scotland Pension Fund (NESPF) Annual Report & Accounts (2019/20) and Fund Governance Policy Statement

10. APPENDICES

Appendix I, Budget/Forecast and Projected Spend 2020/21

11. REPORT AUTHOR CONTACT DETAILS

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Appendix I – 2020/21 BUDGET/FORECAST AND PROJECTED SPEND

The Budget and Projected Spend for NESPF Administration Expenses are shown below:

	Notes	Full Year Budget 2020/21	Budget to 31/12/20	Actual Spend to 31/12/20	Accrual to 31/12/20	Amended Spend to 31/12/20	Over or (Under) to 31/12/20	Proj Annual Spend 2020/21	Proj Over or (Under) Spend 2020/21
		£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Administrative Staff Costs	1	1,567	1,175	305	646	951	(224)	1,267	(300)
Information Technology		455	341	309	23	332	(9)	452	(3)
Supplies & Services		129	97	35	58	93	(4)	125	(4)
Accommodation		251	188	2	165	167	(21)	247	(4)
Printing & Publications		20	15	7	0	7	(8)	20	0
Administration Expenses Total		**2,422**	**1,816**	**658**	**892**	**1,550**	**(266)**	**2,111**	**(311)**

Note (Spend Variance ± 5%):

1. Under spend – Vacancies pending recruitment process and no staff travel costs during lockdown.

Appendix I – 2020/21 BUDGET/FORECAST AND PROJECTED SPEND (continued)

The Budget and Projected Spend for NESPF Oversight & Governance Expenses are shown below:

	Notes	Full Year Budget 2020/21	Budget to 31/12/20	Actual Spend to 31/12/20	Accrual to 31/12/20	Amended Spend to 31/12/20	Over or (Under) to 31/12/20	Proj Annual Spend 2020/21	Proj Over or (Under) Spend 2020/21
		£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Investment Staff Costs	1	301	226	44	90	134	(92)	178	(123)
Pension Fund Committee	2	15	11	0	1	1	(10)	2	(13)
Pension Board	3	10	7	0	1	1	(6)	2	(8)
External Audit Fee		41	31	0	31	31	0	41	0
Internal Audit Fee		6	5	0	4	4	(1)	6	0
Actuarial Fees	4	182	137	157	90	247	110	370	188
General Expenses	5	130	97	113	0	113	16	175	45
Oversight & Governance Expenses Total		**685**	**514**	**314**	**217**	**531**	**158**	**774**	**89**

Note (Spend Variance ± 5%):

1. Under spend – see previous note.
2. Under spend – Saving based upon the annual training event held in London not proceeding.
3. Under spend – Saving based upon the annual training even held in London not proceeding.
4. Over spend – Project Dallas nearing completion allowing Actuarial activity to increase and re-focus on main fund.
5. Over spend – Various Investment advice e.g. reviews of Property, Strategy, etc. Increased LGPC annual subscription levy.

Appendix I – 2020/21 BUDGET/FORECAST AND PROJECTED SPEND (continued)

The Forecast and Projected Spend for NESPF Investment Management Expenses are shown below:

	Notes	Full Year Forecast 2020/21	Forecast to 31/12/20	Actual Spend to 31/12/20	Accrual to 31/12/20	Amended Spend to 31/12/20	Over or (Under) to 31/12/20	Proj Annual Spend 2020/21	Proj Over or (Under) Spend 2020/21
		£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Investment Management	1	10.782	8,086	2,632	6,598	9,230	1,144	12,108	1,326
Performance Fees		6,335	4,751	0	4,751	4,751	0	6,335	0
Direct Property Expenses	2	774	581	468	0	468	(113)	624	(150)
Transaction Costs	3	475	356	626	261	887	531	1,182	707
Custody Fees	4	125	94	80	21	101	7	133	8
Investment Management Expenses Total		**18,491**	**13,868**	**3,806**	**11,631**	**15,437**	**1,569**	**20,382**	**1,891**

Note (Spend ± 5%):

1. Investment Management costs as at the reporting date are projected for the remaining part of the year. However, costs associated with private equity are not calculated until the year end. Therefore, uncertainty in projecting these costs carries the risk of over/under stating the spend for the year. It is anticipated that there will be an over spend.
2. The Forecast for 2020/21 is based upon the Fund Manager's estimation for the year. Costs as at reporting date are projected for the remaining part of the year. Albeit a useful guide, using past transaction activity as a basis for projecting costs carries the risk of

over/under stating the spend for the year. If current transaction activity continues then it is anticipated that there will be an under spend.

3.Transaction Costs are reported by the Custodian (HSBC) as at the reporting date then projected for the remaining part of the year. Albeit a useful guide, using past transaction activity as a basis for projecting costs carries the risk of over/under stating the spend for the year. If current transaction activity continues then it is anticipated that there will be an over spend.

3(a). Transaction Costs are reported by the Custodian (HSBC).

Analysis of Transaction Costs for the period 1 April 2020 to 31 December 2020:

	Commission (£)	Expenses (£)	Tax (£)	Total (£)
Equities	216,250.92	1,451.74	609,449.83	827,152.49
Pooled – Unit Trust	0.00	59,614.46	0.00	59,614.46
Grand Total (£)	**216,250.92**	**61,066.20**	**609,449.83**	**886,766.95**

4. Over Spend – Non budgeted Class Action Fee.

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.

Agenda Item 8.2

ABERDEEN CITY COUNCIL

COMMITTEE	Pensions Committee
DATE	26 March 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	Investment Strategy Review 2021
REPORT NUMBER	PC/MAR21/REVIEW
DIRECTOR	Steven Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHORS	Graham Buntain and Laura Colliss
TERMS OF REFERENCE	1.1

1. PURPOSE OF REPORT

1.1 This report details the outcome of the investment strategy review which has been prepared by officers following the outcome of the 2020 Actuarial Valuation. This report sets out the details of the Fund's current investment strategy and makes a number of recommendations on taking the strategy forward.

2. RECOMMENDATION

2.1 That the Committee approve the proposed investment strategy as set out in section 3.5 of the report.

3. BACKGROUND

3.1 The Fund's established practice is to complete a review of its investment strategy following the outcome of each triennial actuarial valuation.

The aim of the investment strategy is:

- To restore any Fund deficit position through investment returns and agreed contributions to achieve 100% funding but also consider what investment policy the Fund would have when fully funded.

- To provide a framework for identifying changes required over the coming period to continue and maintain the appropriate funding level.

3.2 **Actuarial Valuation 2020 & Funding Strategy Statement**

Valuation Date	31 March 2014 £'s	31 March 2017 £'s	31 March 2020 £'s
Asset Value	2,834	3,815	4,405
Liabilities	3,025	3,562	4,276

Surplus/(Deficit)	(191)	253	129
Funding Level	**94%**	**107%**	**103%**

Actuarial Valuation

3.2.1 As shown in the above table, the Fund has a strong funding level, outperforming the target funding level of 100%. Having reached this position it is now very important that the Fund implements a balanced investment strategy that locks in this funding level and protects this position going forward; whilst recognising the Fund is still an open Fund.

Funding Strategy Statement

3.2.2 The Local Government Pension Scheme (Scotland) Regulations 2018 (as amended) (the '2018 Regulations') and the Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014 (the '2014 Transitional Regulations') (collectively 'the Regulations') provide the statutory framework from which the administering authority is required to prepare a Funding Strategy Statement (FSS).

3.2.3 Funding is the making of advance provision to meet the cost of accruing benefit promises. Decisions taken regarding the approach to funding will therefore determine the rate or pace at which this advance provision is made. Although the Regulations specify the fundamental principles on which funding contributions should be assessed, implementation of the funding strategy is the responsibility of the administering authority, acting on the professional advice provided by the scheme actuary.

3.2.4 The administering authority's long term objective is for the Fund to achieve a 100% solvency level over a reasonable time period and then maintain sufficient assets in order for it to pay all benefits arising as they fall due.

3.2.5 The purpose of the Funding Strategy Statement is therefore:

- to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward by taking a prudent longer-term view of funding those liabilities;
- to establish contributions at a level to 'secure the solvency' of the Pension Fund and the 'long term cost efficiency'; and
- to have regard to the desirability of maintaining as nearly constant a primary rate of contribution as possible.

3.2.6 The intention is for this strategy to be both cohesive and comprehensive for the Fund as a whole, recognising that there will be conflicting objectives which need to be balanced and reconciled. Whilst the position of individual employers must be reflected in the statement, it must remain a single strategy for the administering authority to implement and maintain.

3.2.7 Delivery of the Funding Strategy is through a combination of scheme contributions (both member and employer) and the Fund's investment Strategy.

3.2.8 This report sets out the Fund's current investment strategy and proposal for its development over the next valuation period.

3.3 **Investment Strategy**

3.3.1 Despite the time spent by Pension Funds on the appointment, review and selection of fund managers, investment strategy and the development of the strategic benchmark (Alpha) accounts for around 80 - 90% of the performance of a pension fund's assets.

3.3.2 Investment strategy should be determined in order to meet the Fund's particular requirements, with specific reference to the funding position and liability profile, and to the Fund objectives. It need not reflect a standard 'mould' or 'model'; rather it should be based on sound rationale specific to the Fund's own circumstances. In theory every fund should have a different asset allocation policy.

3.3.3 It is not possible to construct a portfolio of investments which produces a stream of income exactly matching the expected liability outgo. However, it is possible to construct a portfolio which more closely matches the liabilities and represents the minimum risk investment position. Such a portfolio would consist of a mixture of long-term index-linked and fixed interest gilts.

3.3.4 Investment of the Schemes' assets in line with the minimum risk portfolio would minimise fluctuations in the Schemes' ongoing funding level between successive actuarial valuations.

3.3.5 Departure from a minimum risk investment strategy, in particular to include equity investments, gives the prospect that out-performance by the assets will stabilise the contribution requirements and move towards/maintain the funding target (100%). The funding target might in practice therefore be achieved by a range of combinations of funding plan, investment strategy and investment performance.

3.3.6 The current FSS incorporated the following global strategy asset allocation as appropriate to meet the long term objective of achieving/maintaining 100% funding:

<u>Growth Assets 57.5% (range +/- 5%)</u>
Global Equities 45%
Diversified Growth 7.5%
Limited Partnerships 5%

<u>Income/Protection Assets 42.5% (range +/- 5%)</u>
Bonds/Credit 15%
Direct Property 10%
Infrastructure 10%
Index Linked 5%

Other 2.5%

3.4 **2020 Investment Strategy Review**

3.4.1 During the above review a number of topics were considered including:

a) Re-balancing the Equity profile and overweight
b) The role of each mandate as a contribution towards Investment Strategy
c) Private Equity maturity
d) De-risking and adding Inflation protection
e) Income requirements
f) Environmental, Social & Governance issues

3.4.2 Changes made since the last review of the Fund include;

a) Further investments in Direct Lending, Credit and Infrastructure

3.5 **Investment Strategy 2021**

3.5.1 Having taken all the above into consideration which importantly includes the current funding position of 103% the Fund should look to achieve its rebalancing target and lock in recent gains.

3.5.2 To achieve this, the Fund needs to reduce its growth asset allocation and increase its income/protection allocation. This can be done by reducing Global Equities and increasing Bonds/Credit and Infrastructure assets.

3.5.3 The proposed move between Growth and Income/Protection will be phased over time taking into account trigger points and market conditions. In the first instance Officers recommend the following change:

Current Strategic Benchmark	**Proposed Strategic Benchmark**
Growth Assets 57.5% (+/- 5%)	**Growth Assets 55.0% (+/- 5%)**
Global Equities 45%	Global Equities 50%
Diversified Growth Funds 7.5%	
Limited Partnerships 5%	Limited Partnerships 5%
Income/Protection Assets 42.5% (+/- 5%)	**Income/Protection Assets 45.0% (+/- 5%)**
Bonds/Credit 15%	Bonds/Credit 22.5%
Property 10%	Property 10%
Infrastructure 10%	Infrastructure 10%
Index Linked 5%	
Other 2.5%	Other 2.5%

4. FINANCIAL IMPLICATIONS

4.1 The performance of the Fund over the long term impacts on the Fund's 'funding level' and therefore the ability to meet its long term liabilities.

5. LEGAL IMPLICATIONS

5.1 As noted in Paragraph 3.2 the strategy is in line with the legal requirements stipulated in the Regulations. Failure to comply with Regulations would lead to action by the Pensions Regulator.

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. The risk set out in 5.1 is managed through the Risk Register. The Regulations require an administering authority to prepare, maintain and publish a Funding Strategy Statement.

7. OUTCOMES

7.1 The report does not impact on the Council's Delivery Plan.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

None

10. APPENDICES

None

11. REPORT AUTHOR CONTACT DETAILS

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ABERDEEN CITY COUNCIL

COMMITTEE	Pensions Committee
DATE	26 March 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	2020 Tri-ennial Valuation Results
REPORT NUMBER	PC/MAR21/VAL
DIRECTOR	Steven Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHOR	Claire Mullen
TERMS OF REFERENCE	1.1 and 4.1

1. PURPOSE OF REPORT

1.1 The purpose of this report is to give the Pensions Committee details of the triennial valuation as at 31 March 2020 for the North East Scotland Pension Fund (NESPF) and the Aberdeen City Council Transport Fund (ACCTF) in advance of the sign off by the scheme actuary in March 2021.

2. RECOMMENDATIONS

That the Committee: -

2.1 approve the final Funding Strategy Statement for both the NESPF and the ACCTF which outlines the assumptions used in the calculation of the Fund liabilities for the triennial valuation as at 31 March 2020; and

2.2 note the Actuarial Valuation Reports which outline the overall results of the valuation including the funding levels for the NESPF and the ACCTF which will be the published following the sign off by the scheme actuary.

3. BACKGROUND

3.1 The triennial valuation exercise for the NESPF and the ACCTF as at 31 March 2020 has been undertaken throughout this financial year and is required to be completed and signed off by the scheme actuary Mercer by 31 March 2021.

Funding Strategy Statements (FSS)

3.2 The draft NESPF FSS was brought to Committee in December 2020 and the final version of this report along with the ACCTF FSS are now available in appendix I and appendix III for approval. These documents outline the methodology and assumptions used to determine the value of the liabilities held within the Funds.

3.3 The FSS also outlines the Funds approach to employer admission, terminations as well as assessment of covenant risk with a view to maintaining the overall solvency of the Funds.

Actuarial Valuation Reports

3.4 The actuarial valuation reports available in appendix II and appendix IV certify the outcome of the valuation exercise. This report will be available to all stakeholders and will be provided to the Scottish Government in accordance with the regulatory requirements.

3.5 The overall funding level of the NESPF is to be certified as 103%.

3.6 The funding level for the ACCTF is determined to be 114% following the completion of the merge with Strathclyde Pension Fund No.3 and the completion of the buy-in exercise. Further commentary is also provided in the report as a result of the buy-in exercise that was transacted in November 2020.

3.7 The contribution certificates attached to the valuation reports outline the individual employer contribution rate requirement for the duration of the inter-valuation exercise. The contribution rates are determined using each participating employers funding levels with a view to maintaining the solvency of the overall Fund.

4. FINANCIAL IMPLICATIONS

4.1 Meeting the liabilities of the Fund is the responsibility of the participating employers. As part of the valuation process the employer contribution requirements for all individual employers for the years 2021/22 to 2023/24 are determined using the approved assumptions.

4.2 Determining the assumptions with the appropriate level of certainty/prudency will impact on the contribution requirements for each employer based on their own liabilities and funding levels.

5. LEGAL IMPLICATIONS

5.1 In accordance with the LGPS (Scotland) Regulations 2018 the valuation is to be completed and signed off by the scheme actuary by 31 March 2021. Failure to comply would result in action being taken by the Pensions Regulator.

6. MANAGEMENT OF RISK

6.1 The Pension Fund maintains its own Risk Management Policy and regularly updates its Risk Register in line with change. This is reported quarterly to the Pensions Committee. There is a risk of failure to carry out and agree the valuation within statutory timeframes, however this risk is managed through the Risk Register.

7. OUTCOMES

7.1 This report does not impact the Council Delivery Plan.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

None

10. APPENDICES

Appendix I, NESPF Funding Strategy Statement
Appendix II, NESPF Actuarial Valuation Report
Appendix III, ACCTF Funding Strategy Statement
Appendix IV, ACCTF Actuarial Valuation Report

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North East Scotland Pension Fund

Funding Strategy Statement

February 2021

Aberdeen City Council

This Funding Strategy Statement has been prepared by Aberdeen City Council (the Administering Authority) to set out the funding strategy for the North East Scotland Pension Fund (the “Fund”), in accordance with Regulation 56 of the Local Government Pension Scheme (Scotland) Regulations 2014 (as amended) and guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA)

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Executive Summary

Ensuring that the North East Scotland Pension Fund (the "Fund") has sufficient assets to meet its pension liabilities in the long term is the fiduciary responsibility of the Administering Authority (Aberdeen City Council). The Funding Strategy adopted by the North East Scotland Pension Fund will therefore be critical in achieving this.

The purpose of this Funding Strategy Statement ("FSS") is to set out a clear and transparent funding strategy that will identify how each Fund employer's pension liabilities are to be met going forward.

The details contained in this Funding Strategy Statement will have a financial and operational impact on all participating employers in the North East Scotland Pension Fund.

It is imperative therefore that each existing or potential employer is aware of the details contained in this statement.

Given this, and in accordance with governing legislation, all interested parties connected with the North East Scotland Pension Fund have been consulted and given opportunity to comment prior to this Funding Strategy Statement being finalised and adopted. This statement takes into consideration all comments and feedback received.

MEETING THE FUND'S SOLVENCY OBJECTIVE

The Administering Authority's long term objective is for the Fund to achieve and maintain a 100% solvency level over a reasonable time period. Contributions are set in relation to this objective which means that once 100% solvency is achieved, if assumptions are borne out in practice, there would be sufficient assets to pay all benefits earned up to the valuation date as they fall due.

However, because financial and market conditions/outlook change between valuations, the assumptions used at one valuation may need to be amended at the next to meet the primary objectives. This in turn means that contributions will be subject to change from one valuation to another. This objective is considered on an employer specific level when setting individual contribution rates so each employer has the same fundamental objective in relation to their liabilities.

The general principle adopted by the Fund is that the assumptions used, taken as a whole, will be chosen sufficiently prudently for this objective to be reasonably achieved in the long term at each valuation.

The funding strategy set out in this document has been developed alongside the Fund's investment strategy on an integrated basis taking into account the overall financial and demographic risks inherent in the Fund to meet the objective for all employers over different periods. The funding strategy includes appropriate margins to allow for the possibility of adverse events (e.g. material reduction in investment returns, economic downturn and higher inflation outlook) leading to a worsening of the funding position which would normally lead to volatility of contribution rates at future valuations if these margins were not included. This prudence is required by the Regulations and guidance issued by professional bodies and Government agencies to assist the Fund in meeting its primary solvency objective. Individual employer results will also have regard to their covenant strength and the investment strategy applied to the asset shares of those employers.

LONG TERM COST EFFICIENCY

Each employer's contributions are set at such a level to achieve full solvency in a reasonable timeframe. Solvency is defined as a level where the Fund's liabilities i.e. benefit payments can be reasonably met as they arise.

Employer contributions are also set in order to achieve long term cost efficiency. Long term cost-efficiency requires that any funding plan must provide equity between different generations of taxpayers. This means that the contributions must not be set at a level that is likely to give rise to additional costs in the future which fall on later generations of taxpayers or put too high a burden on current taxpayers. The funding parameters and assumptions e.g. deficit recovery period must have regard to this requirement which means a level of prudence is needed. Furthermore, the FSS must have regard to the desirability of maintaining as nearly constant a primary rate of contribution as possible.

When formulating the funding strategy, the Administering Authority has taken into account these key objectives and also considered the implications of the requirements under Section 13(4)(c) of the Public Service Pensions Act 2013. As part of these requirements the Government Actuary's Department (GAD) must, following an actuarial valuation, report on whether the rate of employer contributions to the Fund is set at an appropriate level to ensure its "solvency" and "long term cost efficiency" of the Local Government Pension Scheme (Scotland) (the "LGPS") so far as relating to the Fund.

SURPLUS/DEFICIT SPREAD PERIOD AND CONTRIBUTIONS

As the solvency level of the Fund is 103% at the valuation date i.e. the assets of the Fund are greater than the liabilities, the surplus can potentially be used to reduce ongoing contribution requirements. However, the funding position at individual employer level will vary and for some employers a deficit recovery plan needs to be implemented such that additional contributions are paid into the Fund to meet the shortfall.

Deficit contributions paid to the Fund / surplus run off in respect of each employer will generally be expressed as a percentage of pensionable pay and it is the Fund's objective that any funding deficit is eliminated as quickly as the participating employers can reasonably afford given other competing cost pressures and based on the Administering Authority's view of the employer's covenant and risk to the Fund. For employers in deficit, this may result in some flexibility in recovery periods by employer which would be at the sole discretion of the Administering Authority. The recovery periods will be set by the Fund, although employers will be free to pay above the minimum contribution certified if they wish or to select any shorter deficit recovery period if they wish. Employers may also elect to make prepayments of deficit contributions which could result in a cash saving over the valuation certificate period. For employers in surplus, this will be removed at a rate which depends on the circumstances of each employer. This will depend on the financial covenant and if the employer may potentially exit the Fund in the near future. In some cases this may mean the employer pays the primary contribution rate unadjusted.

Where a deficit exists, the maximum period that it should be recovered over is 19 years, which in the long term provides equity between different generations of taxpayers whilst ensuring the deficit payments are eliminating a sufficient proportion of the capital element of the deficit, thereby reducing the interest cost. This will be periodically reviewed depending on the maturity profile of the Scheme. Similar principles apply to employers in surplus. However, where an employer is expected to exit the Fund, then in normal circumstances, any surplus/deficit would be spread over the remaining period to exit. Full details are set out in this FSS.

The period for recovering any deficit will vary by employer and this is covered in further detail in Section 5.

Where there is a material increase in contributions required at this valuation the employer will be able to 'phase in' their contributions over a period of 3 years in a pattern agreed with the Administering Authority and depending on the affordability of contributions as assessed considering the covenant of an employer, with effect from 1 April 2021.

The government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. A consultation was issued in July 2020, which confirms that the remedy will have the effect of removing the current age criteria applied to the underpin implemented in 2015 for the LGPS, which would then apply to all members who were active as at 1 April 2012. The relevant estimated costs of the remedy have been quantified and notified to employers on this basis. The final funding position and certified contributions for each employer include the estimated costs of the McCloud remedy.

ACTUARIAL ASSUMPTIONS

The actuarial assumptions used for assessing the funding position of the Fund and the individual employers, the "Primary" contribution rate, and any contribution variations due to underlying surpluses or deficits (i.e. the "Secondary" rate) are set out in an Appendix to this FSS.

The discount rate in excess of CPI inflation (the "real discount rate") has been derived from the expected return on the Fund's assets based on the long term strategy set out in its Statement of Investment Principles (SIP). When assessing the appropriate prudent discount rate, consideration has been given to the level of expected asset returns in excess of CPI inflation (i.e. the rate at which the benefits in the LGPS generally increase each year). It is proposed at this valuation the real return over CPI inflation for determining the past service liabilities is 1.25% per annum and 1.50% per annum for determining the future service ("Primary") contribution rates. This compares to 1.75% per annum (past and future) at the last valuation.

The assumption for the long term expected future real returns has fallen since the last valuation. This is principally due to a combination of expectations: the returns on the Fund's assets and the level of inflation in the long term. This is also taken into account by the Actuary when proposing the assumptions and at this valuation means that the level of prudence has been reduced. The assumption has therefore been adjusted so that in the Actuary's opinion, when allowing for the resultant employer contributions emerging from the valuation, the Fund can reasonably be expected to meet the Solvency and Long Term Cost Efficiency objectives.

Where warranted by an employer's circumstances, the Administering Authority retains the discretion to apply an adjusted discount rate to reflect the termination assumptions for that employer if it were to exit the Fund to protect the Fund as a whole. Such cases will be determined by the Section 95 Officer and reported to the Committee.

Within the next valuation cycle, the Fund will consider the merits of implementing a choice of investment strategies to offer to employers, which would exhibit lower investment risk than the current whole fund strategy. This may be appropriate for employers who are deemed to have a weaker covenant than others in the Fund or those who wish to target a lower risk strategy (e.g. if planning for termination). The demographic assumptions are based on the Fund Actuary's bespoke analysis for the Fund, also taking into account the experience of the wider LGPS where relevant.

EMPLOYER ASSET SHARES

The Fund is a multi-employer pension scheme that is not formally unitised and so individual employer asset shares are calculated at each actuarial valuation. This means it is necessary to make some approximations in the timing of cashflows and allocation of investment returns when deriving each employer's asset share.

At each review, cashflows into and out of the Fund relating to each employer, any movement of members between employers within the Fund, along with investment return earned on the asset share, are allowed for when calculating asset shares at each valuation. In addition, the asset shares maybe restated for changes in data or other policies.

Other adjustments are also made on account of the funding positions of orphan bodies which fall to be met by all other active employers in the Fund.

FUND POLICIES

In addition to the information/approaches required by overarching guidance and Regulation, this statement also summarises the Fund's practice and policies in a number of key areas:

1. Covenant assessment and monitoring

An employer's financial covenant underpins its legal obligation and crucially the ability to meet its financial responsibilities to the Fund now and in the future. The strength of covenant to the Fund effectively underwrites the risks to which the Fund is exposed. These risks include underfunding, longevity, investment and market forces.

The strength of employer covenant can be subject to substantial variation over relatively short periods of time and, as such, regular monitoring and assessment is vital to the overall risk management and governance of the Fund. The employers' covenants will be assessed and monitored objectively in a proportionate manner, and an employer's ability to meet its obligations in the short and long term will be considered when determining its funding strategy.

After the valuation, the Fund will continue to monitor employers' covenants in conjunction with their funding positions over the inter-valuation period. This will enable the Fund to anticipate and pre-empt any material issues arising and thus adopt a proactive approach in partnership with the employer. More details are provided in Appendix C to this statement.

2. Admitting employers to the Fund

Various types of employers are permitted to join the LGPS under certain circumstances, and the conditions upon which their entry to the Fund is based and the approach taken is set out in Appendix B. Examples of new employers include:

- Scheme Employers
- Designated bodies - those that are permitted to join if they pass a resolution
- Admission bodies - usually arising as a result of an outsourcing or a transfer to an entity that provides some form of public service and their funding primarily derives from local or Scottish Government.

The key objective for the Fund is to only admit employers where the risk to the Fund is mitigated as far as possible. Certain employers may be required to provide a guarantee or alternative security before entry will be allowed, in accordance with the Regulations and Fund policies.

3. Termination policy for employers exiting the Fund

When an employer ceases to participate within the Fund, it becomes an exiting employer under the Regulations. The Fund is then required to obtain an actuarial valuation of that employer's liabilities in respect of the benefits of the exiting employer's current and former employees, along with a termination contribution certificate. At the discretion of the Administering Authority, suspension notices may be agreed to in certain circumstances – see Termination Policy for further details.

Where there is **no guarantor** who would subsume the liabilities of the exiting employer, the Fund's policy is that a discount rate linked to a minimum risk basis and a more prudent longevity assumption is used for assessing liabilities on termination. With the exception of where a suspension notice has been issued, any exit payments due should be paid immediately although instalment plans will be considered by the Administering Authority on a case by case basis. Any exit credits (surplus assets over liabilities) will be paid from the Fund to the exiting employer following certification by the Actuary. The Administering Authority also reserves the right to modify this approach on a case by case basis if circumstances warrant it.

Where there is a **guarantor** who would subsume the assets and liabilities of the outgoing employer the policy is that any deficit or surplus would normally be subsumed into the guarantor and taken into account at the following valuation. This is subject to agreement from all interested parties who will need to consider any separate contractual agreements that have been put in place between the exiting employer and the guarantor. In some instances an exit debt may be payable by an outgoing employer before the assets and liabilities are subsumed by the guarantor. In the case of a service which has been outsourced, this will be determined by the commercial contract and arrangements which exist between the guarantor and the outgoing employer. Where the outgoing employer is responsible for an exit debt, an exit credit may be payable to the outgoing employer if a surplus of assets over liabilities exists on termination of an admission agreement. This would be based on a determination by the Administering Authority. Please see the termination policy for full details.

1 Introduction

The Local Government Pension Scheme (Scotland) Regulations 2018 (as amended) ("the 2018 Regulations"), the Local Government Pension Scheme (Transitional) Regulations 2014 ("the 2014 Transitional Regulations") (collectively; "the Regulations") provide the statutory framework from which the Administering Authority is required to prepare a Funding Strategy Statement (FSS). The key requirements for preparing the FSS can be summarised as follows:

- After consultation with all relevant interested parties involved with the North East Scotland Pension Fund (the "Fund"), the Administering Authority will prepare and publish their funding strategy;
- In preparing the FSS, the Administering Authority must have regard to:
  - the guidance issued by CIPFA for this purpose; and
  - the Statement of Investment Principles (SIP) for the Fund published under Regulation 12 of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 (as amended);
- The FSS must be revised and published whenever there is a material change in either the policy set out in the FSS or the SIP.

Benefits

The benefits provided by the Fund are specified in the governing legislation contained in the Regulations referred to above. Benefits payable under the Fund are guaranteed by statute and thereby the pensions promise is secure for members. The FSS addresses the issue of managing the need to fund those benefits over the long term, whilst at the same time facilitating scrutiny and accountability through improved transparency and disclosure.

The Fund is a defined benefit arrangement with principally final salary related benefits earned by contributing members up to 1 April 2015 and Career Averaged Revalued Earnings ("CARE") benefits earned thereafter. There is also a "50:50 Scheme Option", where members can elect to accrue 50% of the full scheme benefits in relation to the member only and pay 50% of the normal member contribution.

Employer Contributions

The required levels of employee contributions are specified in the Regulations. Employer contributions are determined in accordance with the Regulations (which require that an actuarial valuation is completed every three years by the actuary, including a rates and adjustments certificate specifying the "primary" and "secondary" rate of the employer's contribution).

Primary Rate

The "Primary rate" for an employer is the contribution rate required to meet the cost of the future accrual of benefits, including ancillary death in service and ill health benefits together with administration costs. It is expressed as a percentage of pensionable pay, ignoring any past service surplus or deficit, but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer's covenant.

The Primary rate for the whole Fund is the weighted average (by payroll) of the individual employers' Primary rates.

Secondary Rate

The "Secondary rate" is an adjustment to the Primary rate to reflect any past service deficit or surplus, to arrive at the total rate of contribution each employer is required to pay. The Secondary rate may be expressed as a percentage adjustment to the Primary rate, and/or a cash adjustment in each of the three years beginning 1 April in the year following the actuarial valuation.

The Secondary rate is specified in the rates and adjustments certificate.

For any employer, the rate they are actually required to pay is the sum of the Primary and Secondary rates.

Secondary rates for the whole Fund in each of the three years shall also be disclosed. These will be the calculated weighted average based on the whole Fund payroll in respect of percentage rates and the total amount in respect of cash adjustments.

2

Purpose of FSS in Policy Terms

Funding is the making of advance provision to meet the cost of accruing benefit promises. Decisions taken regarding the approach to funding will therefore determine the rate or pace at which this advance provision is made. Although the Regulations specify the fundamental principles on which funding contributions should be assessed, implementation of the funding strategy is the responsibility of the Administering Authority, acting on the professional advice provided by the actuary.

The Administering Authority's long term objective is for the Fund to achieve a 100% solvency level over a reasonable time period and then maintain sufficient assets in order for it to pay all benefits arising as they fall due.

The purpose of this Funding Strategy Statement is therefore:

- to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward by taking a prudent longer-term view of funding those liabilities;
- to establish contributions at a level to "secure the solvency" of the pension fund and the "long term cost efficiency",
- to have regard to the <u>desirability</u> of maintaining as nearly constant a <u>primary rate</u> of contribution as possible.

The intention is for this strategy to be both cohesive and comprehensive for the Fund as a whole, recognising that there will be conflicting objectives which need to be balanced and reconciled. Whilst the position of individual employers must be reflected in the statement, it must remain a single strategy for the Administering Authority to implement and maintain.

3

Aims and Purpose of the Fund

The aims of the Fund are to:

- manage employers' liabilities effectively and ensure that sufficient resources are available to meet all liabilities as they fall due
- enable employer contribution rates to be kept at a reasonable and affordable cost to the taxpayers, scheduled, resolution and admitted bodies, while achieving and maintaining Fund solvency and long term cost efficiency, which should be assessed in light of the profile of the Fund now and in the future due to sector changes
- maximise the returns from investments within reasonable risk parameters taking into account the above aims.

The purpose of the Fund is to:

- receive monies in respect of contributions, transfer values and investment income, and
- pay out monies in respect of Fund benefits, transfer values, exit credits, costs, charges and expenses as defined in the Regulations.

4

Responsibilities of the Key Parties

The efficient and effective management of the Fund can only be achieved if all parties exercise their statutory duties and responsibilities conscientiously and diligently. The key parties for the purposes of the FSS are the Administering Authority (and, in particular the Pensions Committee), the individual employers and the Fund Actuary and details of their roles are set out below. Other parties required to play their part in the fund management process are bankers, custodians, investment managers, auditors and legal, investment and governance advisors, along with the Local Pensions Board created under the Public Service Pensions Act 2013.

Key parties to the FSS

The **Administering Authority** should:

- operate the pension fund
- collect employer and employee contributions, investment income and other amounts due to the pension scheme as stipulated in the Regulations
- pay from the pension fund the relevant entitlements as stipulated in the Regulations
- invest surplus monies in accordance with the Regulations
- ensure that cash is available to meet liabilities as and when they fall due
- take measures as set out in the Regulations to safeguard the fund against the consequences of employer default
- manage the valuation process in consultation with the Fund's actuary
- prepare and maintain a FSS and an SIP, both after proper consultation with interested parties, and
- monitor all aspects of the Fund's performance and funding, amending the FSS/SIP as necessary
- effectively manage any potential conflicts of interest arising from its dual role as both Fund administrator and a fund employer, and
- establish, support and monitor a Local Pension Board (LPB) as required by the Public Service Pensions Act 2013, the Regulations and the Pensions Regulator's relevant Code of Practice.

The **Individual Employer** should:

- deduct contributions from employees' pay correctly after determining the appropriate employee contribution rate (in accordance with the Regulations)

- pay all contributions, including their own as determined by the actuary, promptly by the due date
- develop a policy on certain discretions and exercise those discretions as permitted within the regulatory framework
- make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of Fund benefits, early retirement strain
- have regard to the Pensions Regulator's focus on data quality and comply with any requirement set by the Administering Authority in this context
- notify the Administering Authority promptly of any changes to membership which may affect future funding.
- understand the pensions impacts of any changes to their organisational structure and service delivery model, and
- understand that the quality of the data provided to the Fund will directly impact on the assessment of the liabilities and contributions. In particular, any deficiencies in the data would normally result in the employer paying higher contributions than otherwise would be the case if the data was of high quality.

The **Fund Actuary** should:

- prepare valuations including the setting of employers' contribution rates at a level to ensure fund solvency after agreeing assumptions with the Administering Authority and having regard to their FSS and the Regulations
- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters such as pension strain costs, ill health retirement costs etc.
- provide advice and valuations on the termination of admission agreements including in relation to exit credit payments
- provide advice to the Administering Authority on bonds and other forms of security against the financial effect on the Fund of employer default
- assist the Administering Authority in assessing whether employer contributions need to be revised between valuations as required by the Regulations
- advise on funding strategy, the preparation of the FSS and the inter-relationship between the FSS and the SIP, and
- ensure the Administering Authority is aware of any professional guidance or other professional requirements which may be of relevance to the Fund Actuary's role in advising the Fund.

5 Solvency Funding Target

Securing the “solvency” and “long term cost efficiency” is a regulatory requirement. To meet these requirements, the Administering Authority’s long term funding objective is for the Fund to achieve and then maintain sufficient assets to cover 100% of projected accrued liabilities (the “funding target”) assessed on an ongoing past service basis including allowance for projected final pay where appropriate. In the long term, an employer’s total contribution rate would ultimately revert to its Primary rate of contribution.

Solvency and Long Term Efficiency

Each employer’s contributions are set at such a level to achieve full solvency in a reasonable timeframe. Solvency is defined as a level where the Fund’s liabilities i.e. benefit payments can be reasonably met as they arise.

Employer contributions are also set in order to achieve long term cost efficiency. Long term cost-efficiency implies that contributions must not be set at a level that is likely to give rise to additional costs in the future. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the appropriate time.

When formulating the funding strategy the Administering Authority has taken into account these key objectives and also considered the implications of the requirements under Section 13(4)(c) of the Public Service Pensions Act 2013. As part of these requirements the Government Actuary’s Department (GAD) must, following an actuarial valuation, report on whether the rate of employer contributions to the Fund is set at an appropriate level to ensure the “solvency” of the pension fund and “long term cost efficiency" of the LGPS so far as relating to the Fund.

Determination of the solvency Funding Target and Recovery Plan

The principal method and assumptions to be used in the calculation of the funding target are set out in **Appendix A**. The principles underlying the Employer Recovery Plans are set out below. This covers the recovery of deficits and the run off of any surplus assets over liabilities where applicable.

Underlying these assumptions are the following two tenets:

- that the Fund is expected to continue for the foreseeable future; and
- favourable investment performance can play a valuable role in achieving adequate funding over the longer term.

This allows the Fund to take a longer term view when assessing the contribution requirements for certain employers.

In considering this the Administering Authority, based on the advice of the Fund Actuary, will consider if this results in a reasonable likelihood that the funding plan will be successful potentially taking into account any changes in funding after the valuation date up to the finalisation of the valuation by 31 March 2021 at the latest.

As part of each valuation separate employer contribution rates are assessed by the Fund Actuary for each participating employer or group of employers. These rates are assessed taking into account the experience and circumstances of each employer, following a principle of no cross-subsidy between the distinct employers and employer groups in the Fund.

Individual employer contributions will be expressed and certified as two separate elements:

- the **Primary rate**: a percentage of pensionable payroll in respect of the cost of the future accrual of benefits and ancillary death in service and ill health benefits
- the **Secondary rate**: a percentage of pensionable payroll over 2021/24 in respect of an employer's surplus or deficit

For any employer, the total contributions they are actually required to pay in any one year is the sum of the Primary and Secondary rates (subject to an overall minimum of zero). Both elements are subject to further review from April 2024 based on the results of the 2023 actuarial valuation.

Spreading of Surplus / recovery of Deficit contributions

It is the Fund's objective that, where a deficit exists, it is eliminated as quickly as the participating employers can reasonably afford based on the Administering Authority's view of the employer's covenant and risk to the Fund.

In the case of a deficit, recovery periods will be set by the Fund on a consistent basis across employer categories where possible and communicated as part of the discussions with employers. This will determine the minimum contribution requirement and employers will be free to select any shorter deficit recovery period and higher contributions if they wish, including the option of prepaying the deficit contributions in one lump sum either on an annual basis or a one-off payment. This will be reflected in the monetary amount requested via a reduction in overall deficit contributions payable. The Administering Authority does retain ultimate discretion in applying these principles for individual employers on grounds of affordability and covenant strength.

The key principles when considering surplus/deficit spreading are as follows:

- The Fund does not believe it appropriate for contribution reductions to apply compared to the existing funding plan where deficits remain unless there is compelling reason to do so.

- Subject to consideration of affordability, where a deficit exists, as a general rule the deficit recovery period will reduce by at least 3 years for employers at this valuation when compared to the preceding valuation. This is to target full solvency over a similar (or shorter) time horizon. This is to maintain (as far as possible) equity between different generations of taxpayers and to protect the Fund against the potential for an unrecoverable deficit. The deficit recovery period will be set to at least cover the expected interest costs (actual interest costs will vary in line with investment performance) on the deficit. Where an employer is expected to exit the Fund then in normal circumstances, any deficit would be recovered over the remaining period to exit. Where an employer is closed to new entrants then, as a general rule, the spread period should be no more than the average expected future working lifetime of the active membership.

- Employers will have the freedom to pay above the minimum contributions if they so wish. Subject to affordability considerations and other factors, a bespoke period may be applied in respect of particular employers where the Administering Authority considers this to be warranted. The average recovery period adopted by all employers will be set out within the Actuary's report. Employers will be notified of their individual deficit recovery period as part of the provision of their individual valuation results.

- Where an employer is in surplus this will be run off over a period determined by the Administering Authority on the advice of the Actuary. This will depend on the nature of employer, allowing for the financial covenant strength and reasonable affordability of contributions. The objective is to maintain stability of total contributions at this and future valuations. Where an employer is expected to exit the Fund then in normal circumstances, the surplus would be spread over the remaining period to exit.

- In determining the actual recovery period to apply for any particular employer or employer grouping, the Administering Authority may take into account some or all of the following factors:
    - The size of the funding shortfall / surplus;
    - The business plans of the employer;

  - o The assessment of the financial covenant of the Employer, and security of future income streams;
  - o Any contingent security available to the Fund or offered by the Employer such as guarantor or bond arrangements, charge over assets, etc.

  The objective is to recover any deficit or remove any surplus over a reasonable timeframe, and this will be periodically reviewed.

- Where increases (or decreases) in employer contributions are required from 1 April 2021, following completion of the 2020 actuarial valuation, the increase (or decrease) from the rates of contribution payable in the year 2021/22 may be implemented in steps, over a maximum period of 3 years, depending on affordability of contributions as determined by the administering authority However, where a surplus exists or where there has been a reduction in contributions paid in respect of an employer's deficit at the valuation, the Fund would not consider it appropriate for any increase in contributions paid in respect of future accrual of benefits to be implemented in steps.

- As part of the process of agreeing funding plans with individual employers, the Administering Authority will consider the use of contingent assets and other tools such as bonds or guarantees that could assist employing bodies in managing the cost of their liabilities or could provide the Fund with greater security against outstanding liabilities.

- It is acknowledged by the Administering Authority that, whilst posing a relatively low risk to the Fund as a whole, a number of smaller employers may be faced with significant contribution increases that could seriously affect their ability to function in the future. The Administering Authority therefore would be willing to use its discretion to accept an evidence-based affordable level of contributions for the organisation for the three years 2021/2024. Any application of this option is at the ultimate discretion of the Fund officers and Section 95 officer in order to effectively manage risk across the Fund. It will only be considered after the provision of the appropriate evidence as part of the covenant assessment and also the appropriate professional advice.

- For those bodies identified as having a weaker covenant, the Administering Authority will need to balance the level of risk plus the solvency requirements of the Fund with the sustainability of the organisation when agreeing funding plans.

- Notwithstanding the above principles, the Administering Authority, in consultation with the actuary, has also had to consider whether any exceptional arrangements should apply in particular cases.

Employers Exiting the Fund

- Employers must notify the Fund as soon as they become aware of their planned exit date. Where appropriate, or at the request of the Scheme Employer, the Fund will review their certified contribution in order to target a fully funded position at exit. Consideration will be given to any cap and collar arrangements when reviewing contribution rates.

- On the cessation of an employer's participation in the Fund, in accordance with the Regulations, the Fund Actuary will be asked to make a termination assessment. In such circumstances:

The policy for employers **who have a guarantor** participating in the Fund:

Where an employer with a guarantor leaves the Fund, the valuation of the termination payment will be calculated using the funding assumptions used for the assessment of the Solvency Funding Target, as set out in Appendix A.

The residual assets and liabilities and hence any surplus or deficit will normally transfer back to the guarantor but in circumstances where an exiting employer is expected to still be responsible for the termination position, an exit payment/exit credit may be payable from/to the exiting employer.

This is subject to agreement from all interested parties who will need to consider any separate contractual agreements that have been put in place between the exiting employer and the guarantor. If all parties do not agree, then the surplus will be paid directly to the exiting employer following cessation (despite any other agreements that may be in place).

Further details are set out in the Termination Policy in Appendix B.

The policy for employers who **do not have a guarantor** participating in the Fund:

Where an employer with no guarantor leaves the Fund and leaves liabilities with the Fund which the Fund must meet without recourse to that employer, the valuation of the termination payment (or Exit credit) will be calculated using a discount rate based on a minimum risk investment strategy and a more prudent life expectancy assumption.

- In the case of a surplus, the Fund pays the exit credit to the exiting employer following completion of the termination process.

- In the case of a deficit, the Fund would require the exiting employer to pay the termination deficit to the Fund as a lump sum cash payment (unless agreed otherwise by the Administering Authority at their sole discretion) following completion of the termination process.

  The Administering Authority has can vary the treatment on a case by case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary. The termination policy is summarised set out in Appendix B.

Funding for Non-Ill Health Early Retirement Costs

Employers are required to meet all costs of early retirement strain by capital payments into the Fund as determined on the advice of the Actuary.

6

Link to Investment Policy and the Statement of Investment Principles (SIP)

The results of the 2020 valuation show the liabilities to be 103% covered by the current assets.

In assessing the value of the Fund's liabilities in the valuation, allowance has been made for growth asset out-performance as described below, taking into account the investment strategy adopted by the Fund, as set out in the SIP.

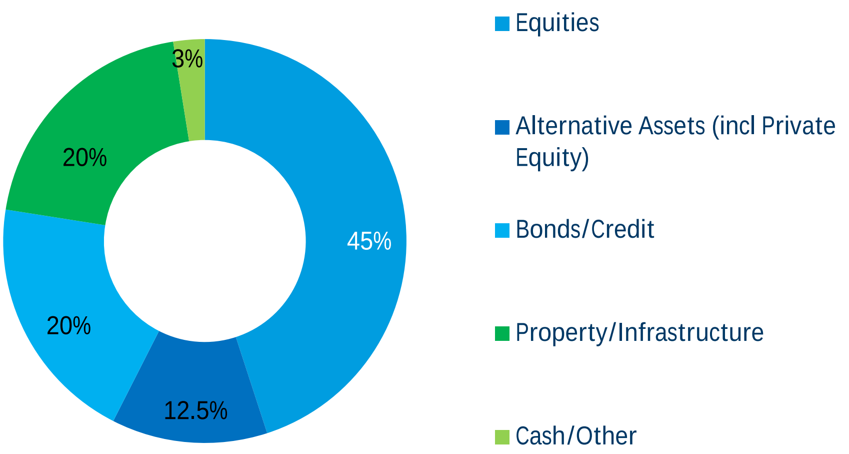
It is not possible to construct a portfolio of investments which produces a stream of income exactly matching the expected liability outgo. However, it is possible to construct a portfolio which represents the "minimum risk" investment position which would deliver a very high certainty of real returns above assumed CPI inflation. Such a portfolio would consist mainly of a mixture of long-term index-linked, fixed interest gilts and possible "swaps".

Investment of the Fund's assets in line with the minimum risk portfolio would minimise fluctuations in the Fund's ongoing funding level between successive actuarial valuations.

If, at the valuation date, the Fund had been invested in this portfolio, then in carrying out the valuation it would not be appropriate to make any allowance for out-performance of the Fund investments or any adjustment to market implied inflation assumption due to supply/demand distortions in the bond markets. This would result in real return versus CPI inflation of minus 1.4% per annum at the valuation date. On this basis of assessment, the assessed value of the Fund's liabilities at the valuation would have been significantly higher, resulting in a funding level of 62%. This is a measure of the level of reliance on future investment returns i.e. level of investment risk being taken.

Departure from a minimum risk investment strategy, in particular to include growth assets such as equities, gives a better prospect that the assets will, over time, deliver returns in excess of CPI inflation and reduce the contribution requirements. The target solvency position of having sufficient assets to meet the Fund's pension obligations might in practice therefore be achieved by a range of combinations of funding plan, investment strategy and investment performance.

The overall strategic asset allocation is set out in the Statement of Investment Principles and the current strategy is set out below:



Based on the investment strategy above and the Actuary's assessment of the return expectations for each asset class, this leads to an overall best estimate average expected return of 1.95% per annum in excess of CPI inflation as at the valuation date. For the purposes of setting funding strategy however, the Administering Authority believes that it is appropriate to take a margin for prudence on these return expectations. This margin, however, has been reduced to take account of the risk management strategies implemented to reduce the volatility of returns within the investment strategy.

A measure of overall prudence to protect against adverse experience in the future is to consider the funding level if it was assessed on a "best estimate" basis for all the principal assumptions (mainly the investment return and life expectancy). The actuary has assessed this funding level as 115%. This level of prudence is built in to allow the Fund to address adverse events whilst maintain stability (within reasonable parameters) in employer contributions where appropriate.

Within the next valuation cycle, the Fund will consider the merits of implementing a choice of investment strategies to offer to employers, which would exhibit a lower risk/return profile than the current whole fund strategy. This may be appropriate for employers who are deemed to have a weaker covenant than others in the Fund or those who wish to target a lower risk strategy (e.g. if planning for termination).

7

Identification of Risks and Counter-Measures

The funding of defined benefits is by its nature uncertain. Funding of the Fund is based on both financial and demographic assumptions. These assumptions are specified in the actuarial valuation report. When actual experience is not in line with the assumptions adopted a surplus or shortfall will emerge at the next actuarial assessment and will require a subsequent contribution adjustment to bring the funding back into line with the target.

The Administering Authority has been advised by the Fund Actuary that the greatest risk to the funding level is the investment risk inherent in the predominantly equity based strategy, so that actual asset out-performance between successive valuations could diverge significantly from that assumed in the long term. The Actuary's formal valuation report includes a quantification of the key risks in terms of the effect on the funding position.

Financial

The financial risks are as follows:-

- Investment markets fail to perform in line with expectations
- Any risk management policies fail to perform in line with expectations
- Market outlook moves at variance with assumptions
- Investment Fund Managers fail to achieve performance targets over the longer term
- Asset re-allocations in volatile markets may lock in past losses
- Pay and price inflation significantly more or less than anticipated
- An employer ceasing to exist without prior notification, resulting in a large exit credit requirement from the Fund impacting on cashflow requirements.

Any increase in employer contribution rates (as a result of these risks), may in turn impact on the service delivery of that employer and their financial position.

In practice the extent to which these risks can be reduced is limited. However, the Fund's asset allocation is kept under constant review and the performance of the investment managers is regularly monitored.

Demographic

The demographic risks are as follows:-

- Future changes in life expectancy (longevity) that cannot be predicted with any certainty
- Potential strains from ill health retirements, over and above what is allowed for in the valuation assumptions for employers
- Deteriorating pattern of early retirements (including those granted on the grounds of ill health)
- Unanticipated acceleration of the maturing of the Fund resulting in materially negative cashflows and shortening of liability durations

Increasing longevity is something which government policies, both national and local, are designed to promote. It does, however, result in a greater liability for pension funds.

Ill health retirements can be costly for employers, particularly small employers where one or two costly ill health retirements can take them well above the "average" implied by the valuation assumptions. Increasingly we are seeing employers mitigate the number of ill health retirements by employing HR / occupational health preventative measures. These in conjunction with ensuring the regulatory procedures in place to ensure that ill-health retirements are properly controlled, can help control exposure to this demographic risk.

Apart from the regulatory procedures in place to ensure that ill-health retirements are properly controlled, **employing bodies should be doing everything in their power to minimise the number of ill-health retirements**.

Early retirements for reasons of redundancy and efficiency do not affect the solvency of the Fund because they are the subject of a direct charge.

With regards to increasing maturity (e.g. due to further cuts in workforce and/or restrictions on new employees accessing the Fund), the Administering Authority regularly monitors the position in terms of cashflow requirements and considers the impact on the investment strategy.

Insurance of certain benefits

The contributions for any employer may be varied as agreed by the Actuary and Administering Authority to reflect any changes in contribution requirements as a result of any benefit costs being insured with a third party or internally within the Fund.

Regulatory

The key regulatory risks are as follows:-

- Changes to Regulations, e.g. changes to the benefits package, retirement age, potential new entrants to Fund,
- Changes to national pension requirements and/or HMRC Rules

Membership of the LGPS is open to all local government staff and should be encouraged as a valuable part of the contract of employment. However, increasing membership does result in higher employer monetary costs.

Governance

The Fund has done as much as it believes it reasonably can to enable employing bodies and Fund members to make their views known to the Fund and to participate in the decision-making process. The first draft of this FSS was consulted on during Q4 2020. The revisions to the FSS have been incorporated into this draft and the updated draft was finalised following the Committee meeting on 26 March 2021.

Governance risks are as follows:-

- The quality of membership data deteriorates materially due to breakdown in processes for updating the information resulting in liabilities being under or overstated
- Administering Authority unaware of structural changes in employer's membership (e.g. large fall in employee numbers, large number of retirements) with the result that contribution rates are set at too low a level
- Administering Authority not advised of an employer closing to new entrants, something which would normally require an increase in contribution rates
- An employer ceasing to exist with insufficient funding or adequacy of a bond. Where there is a guarantor body in place, any outstanding funding deficit that is not recovered from the outgoing employer / bond will need to be paid by the guarantor (or the assets and liabilities for the outgoing employer will need to be subsumed by the guarantor). For cases where there is no guarantor or bond in place, any outstanding funding deficit that is not recovered from the outgoing employer will need to be subsumed by the Fund as a whole and spread across all employers.
- An employer ceasing to exist without prior notification, resulting in a large exit credit requirement from the Fund impacting on cashflow requirements.
- Changes in the Committee membership.

For these risks to be minimised much depends on information being supplied to the Administering Authority by the employing bodies. Arrangements are strictly controlled and monitored, but in most cases the employer, rather than the Fund as a whole, bears the risk. Nevertheless, where an employer defaults on its liabilities the risk in some cases may be borne by the whole Fund, so to that extent all Fund employers have joint and several liabilities to the Fund.

8

Monitoring and Review

The Administering Authority has taken advice from the actuary in preparing this Statement, and has consulted with the employers participating in the Fund.

A full review of this Statement will occur no less frequently than every three years, to coincide with completion of a full actuarial valuation. Any review will take account of the current economic conditions and will also reflect any legislative changes.

The Administering Authority will monitor the progress of the funding strategy between full actuarial valuations. If considered appropriate, the funding strategy will be reviewed (other than as part of the triennial valuation process), for example, if there:

- has been a significant change in market conditions, and/or deviation in the progress of the funding strategy
- have been significant changes to the Fund membership, or LGPS benefits
- have been changes to the circumstances of any of the employing authorities to such an extent that they impact on or warrant a change in the funding strategy
- have been any significant special contributions paid into the Fund.
- there has been a change in Regulations or Guidance which materially impacts on the policies within the funding strategy.

When monitoring the funding strategy, if the Administering Authority considers that any action is required, the relevant employing authorities will be contacted. In the case of admitted bodies, there is statutory provision for rates to be amended between valuations and this will be considered in conjunction with the employer affected and any associated guarantor of the employer's liabilities (if relevant).

Cost Management Process

The cost management process was set up by HMT, with an additional strand set up by the Local Government Pension Scheme (Scotland) Advisory Board (for the Scottish LGPS). The aim of this was to control costs for employers and taxpayers via adjustments to benefits and/or employee contributions.

As part of this, it was agreed that employers should bear the costs/risks of external factors such as the discount rate, investment returns and inflation changes, whereas employees should bear the costs/risks of other factors such as wage growth, life expectancy changes, ill health retirement experience and commutation of pension.

The outcome of the initial cost management valuation was expected to be implemented by now, based on data from the 2017 valuations for the Scottish LGPS. This had been put on hold due to age discrimination cases (the McCloud judgment) brought in respect of the firefighters and judges schemes, relating to protections provided when the public sector schemes were changed (which was on 1 April 2015 for the Scottish LGPS). The cost cap has now been un-paused and we expect more detail to emerge in due course over 2021. Consideration of the outcome of this process would be expected to be taken in to account at the next valuation (in 2023) unless the outcome requires this to be done prior to then.

The McCloud judgment

The government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. A consultation was issued in July 2020, which confirms that the remedy will have the effect of removing the current age criteria applied to the underpin implemented in 2015 for the LGPS, which would then apply to all members who were active as at 1 April 2012. The relevant estimated costs of the remedy have been quantified and notified to employers on this basis. The final funding position and certified contributions for each employer include the estimated costs of the McCloud remedy.

As a consequence of McCloud, cost management had been paused until recently (HMT and GAD are now considering the LGPS specific impact before commenting on the outcomes). No allowance for cost management has been made in this valuation. This will be reconsidered once the final outcomes are known.

Appendix A – Actuarial Method and Assumptions

Method

The actuarial method to be used in the calculation of the solvency funding target is the Projected Unit method, under which the salary increases assumed for each member are projected until that member is assumed to leave active service by death, retirement or withdrawal from service. This method implicitly allows for new entrants to the Fund on the basis that the overall age profile of the active membership will remain stable. As a result, for those employers which are closed to new entrants, an alternative method is adopted, which makes advance allowance for the anticipated future ageing and decline of the current closed membership group potentially over the period of the rates and adjustments certificate.

Financial assumptions – solvency Funding target

Investment return (discount rate)

The discount rate has been derived based on the expected return on the Fund assets based on the long term strategy set out in the Statement of Investment Principles (SIP). It includes appropriate margins for prudence. When assessing the appropriate discount rate consideration has been given to the returns in excess of CPI inflation (as derived below). The discount rate at the valuation date has been derived based on an assumed return of 1.25% per annum above CPI inflation i.e. a real return of 1.25% per annum equating to a total discount rate of 3.35% per annum. This real return will be reviewed from time to time based on the investment strategy, market outlook and the Fund's overall risk metrics. The discount rate will be reviewed as a matter of course at the time of a formal valuation or a formal employer rate review.

Where warranted by an employer's circumstances, the Administering Authority retains the discretion to apply a discount rate based on a lower risk investment strategy for that employer to protect the Fund as a whole.

Inflation (Consumer Prices Index)

The inflation assumption will be taken to be the investment market's expectation for RPI inflation as indicated by the difference between yields derived from market instruments, principally conventional and index-linked UK Government gilts as at the valuation date (reflecting the profile and duration of the Fund’s accrued liabilities) but subject to an adjustment due to retirement pensions being increased annually by the change in the Consumer Price Index rather than the Retail Price Index.

The overall average reduction to the assumption to long term RPI inflation to arrive at the CPI inflation assumption at the valuation date is 0.6% per annum. The CPI inflation assumption at the valuation date is 2.1% per annum. This adjustment to the RPI inflation assumption will be reviewed from time to time to take into account any changes in market expectations caused by the reform of the RPI index. Any change will then be implemented for all relevant policies in this Funding Strategy Statement.

Salary increases

In relation to benefits earned prior to 1 April 2015, the assumption for real salary increases (salary increases in excess of price inflation) will be determined by an allowance of 1.5% p.a. over the inflation assumption as described above. This includes allowance for promotional increases. In addition to the long term salary increase assumption allowance has been made for expected short term pay restraint for some employers as budgeted in their financial plan. Depending on the circumstances of the employer, the variants on short term pay that have been applied are either no allowance or allowances based on evidence from the employer of 1% or 2% per annum, or alternatively assuming the increase will be in line with the CPI assumption set out above, for each year from the valuation date up to 31 March 2023. The allowance made has been notified to each employer separately on their individual results schedule.

Application of bespoke salary increase assumptions as put forward by individual employers will be at the ultimate discretion of the Administering Authority but as a minimum must be reasonable and practical. To the extent that experience differs to the assumption adopted, the effects will emerge at the next actuarial valuation.

Pension increases/Indexation of CARE benefits

Increases to pensions are assumed to be in line with the inflation (CPI) assumption described above. This is modified appropriately to reflect any benefits which are not fully indexed in line with the CPI (e.g. Guaranteed Minimum Pensions where the LGPS is not required to provide full indexation). The exception to this is for members who will reach state pension age after 5 April 2021. In line with expected future changes to the regulations, we have allowed for increases on Guaranteed Minimum Pensions to increase in line with the inflation (CPI) assumption described above.

For members in pensionable employment, their CARE benefits are also indexed by CPI although this can be less than zero, i.e. a reduction in benefits, whereas for pension increases this cannot be negative, as pensions cannot be reduced.

Demographic assumptions

Mortality/Life Expectancy

The mortality in retirement assumptions will be based on the most up-to-date information in relation to self-administered pension schemes published by the Continuous Mortality Investigation (CMI), making allowance for future improvements in longevity and the experience of the Fund. The mortality base tables used are set out below, with a loading reflecting Fund specific experience. The derivation of the mortality assumption is set out in a separate paper as supplied by the Actuary.

A specific mortality assumption has also been adopted for current members who retire on the grounds of ill health. For all members, it is assumed that the trend in longevity seen over recent time periods (as evidenced in the 2019 CMI analysis) will continue in the longer term and as such, the assumptions build in a level of longevity 'improvement' year on year in the future in line with the CMI 2019 projections and a long term improvement trend of 1.75% per annum.

As an indication of impact, we have set out the life expectancies at age 65 based on the 2020 assumptions:

	Male Life Expectancy at 65		Female Life Expectancy at 65	
	2017	2020	2017	2020
Pensioners	22.6	21.4	24.6	24.1
Actives aged 45 now	25.5	23.0	27.8	26.2
Deferreds aged 45 now	23.4	21.7	26.6	25.2

For example, a male pensioner, currently aged 65, would be expected to live to age 86.4. Whereas a male active member aged 45 would be expected to live until age 88.0. This is a reflection of the expected improvement in life expectancy over the next 20 years in the assumptions above.

The mortality before retirement has also been adjusted based on LGPS wide experience.

Commutation

It has been assumed that, on average, 50% of retiring members will take the maximum tax-free cash available at retirement and 50% will take the standard 3/80ths cash sum. The option which members have to commute part of their pension at retirement in return for a lump sum is a rate of £12 cash for each £1 p.a. of pension given up.

Other Demographics

Following an analysis of Fund experience carried out by the Actuary, the incidence of ill health retirements, withdrawal rates and the proportions married/civil partnership assumption remain in line with the assumptions adopted for the last valuation. In addition, no allowance will be made for the future take-up of the 50:50 option (this is the same assumption as at the last valuation). Where any member has actually opted for the 50:50 scheme, this will be allowed for in the assessment of the rate for the next 3 years. Other assumptions are as per the last valuation.

Expenses

Expenses are met out the Fund, in accordance with the Regulations. This is allowed for by adding 0.4% of pensionable pay to the contributions as required from participating employers. This addition is reassessed at each valuation. Investment expenses have been allowed for implicitly in determining the discount rates.

Discretionary Benefits

The costs of any discretion exercised by an employer in order to enhance benefits for a member through the Fund will be subject to additional contributions from the employer as required by the Regulations as and when the event occurs. As a result, no allowance for such discretionary benefits has been made in the valuation

Method and assumptions used in calculating the cost of future accrual (or primary rate)

The future service liabilities are calculated using the same assumptions as the funding target except that a different financial assumption for the discount rate is used. A critical aspect here is that the Regulations state the desirability of keeping the “Primary rate” (which is the future service rate) as stable as possible so this needs to be taken into account when setting the assumptions.

As future service contributions are paid in respect of benefits built up in the future, the Primary rate should take account of the market conditions applying at future dates, not just the date of the valuation, thus it is justifiable to use a slightly higher expected return from the investment strategy. In addition, the future liabilities for which these contributions will be paid have a longer average duration than the past service liabilities as they relate to active members only.

The financial assumptions in relation to future service (i.e. the Primary rate) are based on an overall assumed real discount rate of 1.50% per annum above the long term average assumption for consumer price inflation of 2.10% per annum. This leads to a discount rate of 3.60% per annum.

Employer Asset Shares

The Fund is a multi-employer pension scheme that is not formally unitised and so individual employer asset shares are calculated at each actuarial valuation. This means it is necessary to make some approximations in the timing of cashflows and allocation of investment returns when deriving the employer asset share.

In attributing the overall investment performance obtained on the assets of the Fund to each employer a pro-rata principle is adopted. This approach is effectively one of applying a notional individual employer investment strategy identical to that adopted for the Fund as a whole unless agreed otherwise between the employer and the Fund at the sole discretion of the Administering Authority.

At each review, cashflows into and out of the Fund relating to each employer, any movement of members between employers within the Fund, along with investment return earned on the asset share, are allowed for when calculating asset shares at each valuation.

Other adjustments are also made on account of the funding positions of orphan bodies which fall to be met by all other active employers in the Fund.

Summary of key whole Fund assumptions used for calculating funding target and cost of future accrual (the "primary rate") for the 2020 actuarial valuation

Long-term yields		
	Market implied RPI inflation	2.70% p.a.
Solvency Funding Target financial assumptions		
	Investment return/Discount Rate	3.35% p.a.
	CPI price inflation	2.10% p.a.
	Short Term Salary Increases	Varies by employer - 3 year period to 31 March 2023 as noted above
	Long Term Salary increases	3.60% p.a.
	Pension increases/indexation of CARE benefits	2.10% p.a.
Future service accrual financial assumptions		
	Investment return/Discount Rate	3.60% p.a.
	CPI price inflation	2.10% p.a.
	Short Term Salary Increases	Varies by employer - 3 year period to 31 March 2023 as noted above
	Long Term Salary increases	3.60% p.a.
	Pension increases/indexation of CARE benefits	2.10% p.a.

Life expectancy assumptions

The post retirement mortality tables adopted for this valuation are set out below:

Current Status	Retirement Type	Mortality Table (M/F)
Annuitant	Normal Health	114% S3PMA_CMI_2019 [1.75%] 101% S3PFA_M_CMI_2019 [1.75%]
	Dependant	150% S3PMA_CMI_2019 [1.75%] 104% S3DFA_CMI_2019 [1.75%]
	Ill Health	136% S3IMA_CMI_2019 [1.75%] 144% S3IFA_CMI_2019 [1.75%]
	Future Dependant	146% S3PMA_CMI_2019 [1.75%] 121% S3DFA_CMI_2019 [1.75%]

Active	Normal Health	121% S3PMA_CMI_2019 [1.75%] 101% S3PFA_M_CMI_2019 [1.75%]
	Ill Health	134% S3IMA_CMI_2019 [1.75%] 151% S3IFA_CMI_2019 [1.75%]
Deferred	All	144% S3PMA_CMI_2019 [1.75%] 116% S3PFA_M_CMI_2019 [1.75%]
Future Dependant	Dependant	153% S3PMA_CMI_2019 [1.75%] 128% S3DFA_CMI_2019 [1.75%]

All life expectancies are normal health "cohort" expectancies from age 65 in 2020 and non-pensioners' current age assumed to be 45.

Other demographic assumptions are set out in the Actuary's formal report.

Appendix B – Admission and Termination Policy

Introduction

This document details the North East Scotland Pension Fund's (NESPF) policy on the methodology for assessment of ongoing contribution requirements and termination payments in the event of the cessation of an employer's participation in the Fund. This document also covers NESPF's policy on admissions into the Fund and sets out the considerations for current and former admission bodies. It supplements the general policy of the Fund as set out in the Funding Strategy Statement (FSS).

- Admission bodies are required to have an "admission agreement" with the Fund. In conjunction with the Regulations, the admission agreement sets out the conditions of participation of the admission body including which employees (or categories of employees) are eligible to be members of the Fund.

- Scheme Employers have a statutory right to participate in the LGPS and their staff therefore can become members of the LGPS at any time, although some organisations (Part 2 Scheme Employers) do need to designate eligibility for its staff.

A list of all current employing bodies participating in the NESPF is kept as a live document and will be updated by the Administering Authority as bodies are admitted to, or leave the NESPF.

Please see the glossary for an explanation of the terms used throughout this Appendix.

Entry to the Fund

Prior to admission to the Fund, an Admitted Body is required to carry out an assessment of the level of risk on premature termination of the contract to the satisfaction of the Administering Authority. If the risk assessment and/or bond amount is not to the satisfaction of the Administering Authority (as required under the LGPS (Scotland) Regulations) it will consider and determine whether the admission body must pre-fund for termination with contribution requirements assessed using the minimum risk methodology and assumptions.

Some aspects that the Administering Authority may consider when deciding whether to apply a minimum risk methodology are:

- Uncertainty over the security of the organisation's funding sources e.g. the body relies on voluntary or charitable sources of income or has no external funding guarantee/reserves;
- If the admitted body has an expected limited lifespan of participation in the Fund;
- The average age of employees to be admitted and whether the admission is closed to new joiners.

In order to protect other Fund employers, where it has been considered undesirable to provide a bond, a guarantee must be sought in line with the Regulations.

Admitted bodies providing a service

Generally Admitted Bodies providing a service will have a guarantor within the Fund that will stand behind the liabilities on default. Accordingly, in general, the minimum risk approach to funding and termination will not apply for these bodies.

As above, the Admitted Body is required to carry out an assessment of the level of risk on premature termination of the contract to the satisfaction of the Administering Authority. This assessment would normally be based on advice in the form of a "risk assessment report" provided by the actuary to the NESPF. As the Scheme Employer is effectively the ultimate guarantor for these admissions to the NESPF it must also be satisfied (along with the Administering Authority) over the level (if any) of any bond requirement. Where bond agreements are to the satisfaction of the Administering Authority, the level of the bond amount will be subject to review on a regular basis.

In the absence of any other specific agreement between the parties, deficit recovery periods for Admitted Bodies will be set in line with the Fund's general policy as set out in the FSS.

Any risk sharing arrangements agreed between the Scheme Employer and the Admitted Body will be documented in the commercial agreement between the two parties and not the admission agreement.

An exception to the above policy applies if the guarantor is not a participating employer within the NESPF, including if the guarantor is a participating employer within another LGPS Fund. In order to protect other employers within the NESPF the Administering Authority may in this case treat the admission body as pre-funding for termination, with contribution requirements assessed using the minimum risk methodology and assumptions.

Pre-Funding for Termination

An employing body may choose to pre-fund for termination i.e. to amend their funding approach to a minimum risk methodology and assumptions. This will substantially reduce the risk of an uncertain and potentially large debt being due to the Fund at termination. However, it is also likely to give rise to a substantial increase in contribution requirements, when assessed on the minimum risk basis.

For any employing bodies funding on such a minimum risk strategy a notional investment strategy will be assumed as a match to the liabilities if agreed by the Administering Authority based on the advice of the Actuary. In particular the employing body's notional asset share of the Fund will be credited with an investment return in line with the minimum risk funding assumptions adopted rather than the actual investment return generated by the actual asset portfolio of the entire Fund. The Fund reserves the right to modify this approach in any case where it might materially affect the finances of the Scheme, or depending on any case specific circumstances.

Exiting the Fund

Termination of an employer's participation

When an employing body terminates for any reason, employees may transfer to another employer, either within the Fund or elsewhere. If this is not the case the employees will retain pension rights within the Fund i.e. either deferred benefits or immediate retirement benefits.

In addition to any liabilities for current employees the Fund will also retain liability for payment of benefits to former employees, i.e. to existing deferred and pensioner members except where there is a complete transfer of responsibility to another Fund with a different Administering Authority.

In the event that unfunded liabilities arise that cannot be recovered from the employing body, these will normally fall to be met by the Fund as a whole (i.e. all employers) unless there is a guarantor or successor body within the Fund.

The NESPF's general policy is that a termination assessment will be made based on a minimum risk funding basis, unless the employing body has a guarantor within the Fund or a successor body exists to take over the employing body's liabilities (including those for former employees). This is to protect the other employers in the Fund as, at termination, the employing body's liabilities will become orphan liabilities within the Fund, and there will be no recourse to it if a shortfall emerges in the future (after participation has terminated).

In addition, in certain circumstances the Fund may agree to issue a "suspension notice" to an employer to suspend that employer's liability to pay an exit payment starting from the date when that employer would otherwise become an exiting employer. Should this occur, the employer must continue to make such contributions towards the liabilities of the fund in respect of benefits for the employer's current and former employees until a new and satisfactory valuation is carried out and the suspension notice is withdrawn. The Fund reserves the right to require a side legal agreement alongside any suspension notices detailing the terms of the arrangement including for example the length of such a notice, and the conditions for cessation of the agreement/notice.

Employers with a Guarantor

If the employing body has a guarantor within the Fund or a successor body exists to take over the employing body's liabilities, the NESPF's policy is that the valuation funding basis will be used for the termination assessment unless the guarantor informs the NESPF otherwise.

The residual assets and liabilities and hence any surplus or deficit will normally transfer back to the guarantor. (For Admission bodies, this process is sometimes known as the "novation" of the admission agreement where a successor body exists to take over the employing body's liabilities; this may (if agreed by the successor body) constitute a complete amalgamation of the assets and liabilities).

In circumstances where an exiting employer is expected to still be responsible for the termination position, an exit payment/exit credit may be payable from/to the exiting employer. This is subject to agreement from all interested parties who will need to consider any separate contractual agreements that have been put in place between the exiting employer and the guarantor. If all parties do not agree, then the surplus will be paid directly to the exiting employer (despite any other agreements that may be in place).

In some instances, the outgoing employer may only be responsible for part of the residual deficit or surplus as per a separate risk sharing agreement. The default is that any surplus would be retained by the Fund in favour of the outsourcing employer/guarantor unless agreed otherwise by all parties. For the avoidance of doubt, where the outgoing employer is not responsible for any costs under a risk sharing agreement then no exit credit will be paid.

Employers without a Guarantor

A termination assessment will be made based on a minimum risk funding basis. This is to protect the other employers in the Fund as, at termination, the employing body's liabilities will become orphan liabilities within the Fund, and there will be no recourse to it if a shortfall emerges in the future (after participation has terminated).

- In the case of a surplus, the Fund pays the exit credit to the exiting employer following completion of the termination process.
- In the case of a deficit, the Fund would require the exiting employer to pay the termination deficit to the Fund as a lump sum cash payment (unless agreed otherwise by the Administering Authority at their sole discretion) following completion of the termination process.

The Administering Authority can vary the treatment on a case by case basis of its sole discretion if circumstances warrant it based on the advice of the Actuary and, for example, may adjust any exit payment or exit credit to take into account any risk sharing arrangements which exist between the exiting employer and other Fund employers.

Furthermore, if appropriate, a reasonable allowance for expenses will also be made in relation administration and other expenses. This will be allowed for in the final termination assessment.

It is possible under certain circumstances that an employer can apply to transfer all assets and current and former members' benefits to another LGPS Fund in Scotland. In these cases no termination assessment is required as there will no longer be any orphan liabilities in the NESPF. Therefore, a separate assessment of the assets to be transferred will be required.

Allowing for the McCloud Judgement in Termination Valuations

The government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. A consultation was issued in July 2020, which confirms that the remedy will have the effect of removing the current age criteria applied to the underpin implemented in 2015 for the Scottish LGPS, which would then apply to all members who were active as at 1 April 2012.

As part of any termination assessment, a reasonable estimate for the potential cost of McCloud will be included. However, where a surplus or deficit is being subsumed, no allowance will be made for McCloud within the calculations and the impact will be considered at the next contribution rate review.

Where a surplus or deficit isn't being subsumed, McCloud will be allowed for as a matter of policy.

The allowance will be calculated in line with the treatment set out in this Funding Strategy Statement for all members of the outgoing employer using the termination assessment assumptions. For the avoidance of doubt, there will be no recourse for an employer with regard to McCloud, once the final termination has been settled and payments have been made. Once the remedy is known, any calculations will be performed in line with the prevailing regulations and guidance in force at the time.

The Administering Authority can vary the treatment on a case-by-case basis at its sole discretion if circumstances warrant it based on the advice of the.

Future Terminations

In many cases, termination of an employer's participation is an event that can be foreseen, for example, because the organisation's operations may be planned to be discontinued and/or the admission agreement is due to cease. Under the Regulations, in the event of the Administering Authority becoming aware of such circumstances, it can amend an employer's minimum contributions such that the value of the assets of the employing body is neither materially more nor materially less than its anticipated liabilities at the date it appears to the Administering Authority that it will cease to be a participating employer. In this case, employing bodies are encouraged to open a dialogue with the Fund to commence planning for the termination as early as possible. Where termination is disclosed in advance the Fund will operate procedures to reduce the sizeable volatility risks to the debt amount in the run up to actual termination of participation. The Fund will modify the employing body's approach in any case, where it might materially affect the finances of the Scheme, or depending on any case specific circumstances.

The Fund's standard policy is to recover termination deficits (including interest and expenses) as a one off payment. However, at the discretion of the Administering Authority, the deficit can be recovered over an agreed period as certified by the Actuary. This period will depend on the Administering Authority's view on the covenant of the outgoing employer.

Minimum Risk Termination basis

The minimum risk financial assumptions that applied at the actuarial valuation date (31 March 2020) are set out below in relation to any liability remaining in the Fund. These will be updated on a case-by-case basis, with reference to prevailing market conditions at the relevant employing body's cessation date.

Least risk assumptions	**31 March 2020**
Discount Rate	0.70% p.a.
CPI price inflation	2.10% p.a.
Pension increases/indexation of CARE benefits	2.10% p.a.

The financial assumptions above are as at 31 March 2020. These assumptions will be reviewed on an ongoing basis to allow for changes in market conditions along with any other structural or legislative changes.

In particular, since the valuation date it has been announced that RPI inflation will be reformed with effect from 2030 to align the index with the CPIH inflation measure. This therefore needs to be reflected when deriving an updated market estimate of CPI inflation.

For example, when assessing a termination position (at March 2020) we will adjust the market RPI inflation to arrive at the CPI inflation assumption by deducting 0.6% per annum when assessing an employer's termination position. This adjustment will be kept under review over time.

All demographic assumptions will be the same as those adopted for the 2020 actuarial valuation, except in relation to the life expectancy assumption. Given the minimum risk financial assumptions do not protect against future adverse demographic experience a higher level of prudence will be adopted in the life expectancy assumption.

The termination basis for an outgoing employer will include an adjustment to the assumption for longevity improvements over time by increasing the rate of improvement in mortality rates to 2.25% p.a. from 1.75% used in the 2020 valuation for ongoing funding and contribution purposes.

Appendix C – Covenant Assessment and Monitoring Policy

Introduction

This document sets out the Fund's approach to Employer risk management and in particular in respect of those bodies in the Fund defined as 'admission bodies'. This document supports the Fund's Employer Engagement Strategy

1.1 ADMISSION BODIES

Under the Local Government Pension Scheme (LGPS) (Scotland) Regulations, certain employers are allowed to participate in the North East Scotland Pension Fund (the Fund) if they satisfy the relevant criteria. These are known as admission bodies. An admission body is required to have an 'admission agreement' with the Fund. In conjunction with the regulations, the admission agreement sets out the conditions of participation of the admission body including which employees (or categories of employees) are eligible to be members of the Fund.

In line with Schedule 2 of the Regulations, all new admission bodies are required to carry out, to the satisfaction of the administering authority, an assessment, taking account of actuarial advice, of the level of risk arising on premature termination of the provision of service or assets by reason of insolvency, winding up or liquidation of the admission body.

The admission body is required to enter into a bond to cover this risk but, where it is not possible for the admission body to enter into a bond then a guarantee can be obtained from another entity provided certain conditions are met.

It is acceptable for the original transferring employer to instruct in writing to the Administering Authority that they should waive the requirement for a bond/indemnity and/or other guarantee on the basis of the guarantee provided by the original scheme employer under the Regulations. The Administering Authority will consider if this is acceptable depending on the covenant of the original scheme employer.

1.2 EMPLOYER COVENANT

An employer's covenant underpins its legal obligation and ability to fund the Scheme now and in the future. The strength of covenant depends upon the robustness of the legal agreements in place and the likelihood that the employer can meet them. The covenant effectively underwrites the risks to which the Scheme is exposed, including underfunding, longevity, investment and market forces.

An Assessment of employer covenant focuses on determining the following:

- Type of body and its origins.
- Nature and enforceability of legal agreements.
- Whether there is a bond in place and the level of the bond.
- Whether a more accelerated recovery plan should be enforced.
- Whether there is an option to call in contingent assets.
- Is there a need for monitoring of ongoing and termination funding ahead of the next actuarial valuation?

The strength of employer covenant can be subject to substantial variation over relatively short periods of time and, as such, regular monitoring and assessment is vital.

2 RISK

2.1 DEFINITION OF RISK

Risk can be defined as the combination of the probability of an event and its consequences. In this instance, the probability centres around participation in the Fund coming to an end or being prematurely terminated and if employees are not transferred to another employer, pension rights will be retained within the Fund in respect of the outgoing employer. These pension rights, deferred benefits, immediate retirement benefits or existing pensions in payment form the employer's liabilities. In the event that liabilities arise that cannot be recovered from the admission body, these will normally fall to be met by the original Scheme employer where they are acting as a guarantor, or the Fund as a whole where there is no guarantor in the Fund. Therefore, the consequence is that the Fund is exposed to risk where employers are unable to meet their liabilities and there is no cover provided by a guarantor.

Risk management includes identifying and assessing risks (the 'inherent risks') and responding to them.

Response to risk, which is initiated within the organisation, is through management of risk and may involve one or more of the following:

- Tolerating risk.
- Treating risk in an appropriate way to constrain the risk to an acceptable level.
- Transferring the risk.
- Terminating the activity giving rise to the risk.

The level of risk remaining after a review is that which has been accepted (the ‘residual risk”) and is the exposure in respect of that risk, and should be acceptable and justifiable.

2.2 IDENTIFYING RISK

The North East Scotland Pension Fund (the Fund) is exposed to a number of risks associated with admission bodies and other employers. In order to mitigate these risks, it is necessary to identify them and prescribe them certain levels so as to ascertain which are deemed tolerable and those that need to be addressed.

Broadly speaking the key risks specific to the Fund are as follows:

Financial - Market fluctuations, investment returns and pay/price inflation.

Demographic - Increased longevity and the cost of early retirements/death-in-service.

Regulatory - Changes to regulations and changes to national pension requirements and/or HMRC rules.

Governance - Administering authority unaware of structural changes in employer’s membership, administering authority not advised of an employer closing to new entrants, and an employer ceasing to exist with insufficient funding or adequacy of a bond. In addition lack of quality data from the employer can impact of the risk profile.

Employers - Sustainability of an employer or their ability to meet their liabilities within the agreed funding strategy.

Clearly some of the risks identified are beyond the control of the Fund and, therefore, it is important to target those where it does have influence when mitigating risk. With this in mind, the focus of this document will be in the areas of governance and employers’ activities or actions, but consideration should also be given to the cost of early retirements (including in ill health) and death in service and the potential for the transfer of such risk through appropriate insurance whether externally or internally within the Fund.

2.3 LEVELS OF RISK

The levels of risk facing the Fund can be generally classified as lower, medium and higher risk as illustrated below:

Participating Employers

Lower Risk	Medium Risk	Higher Risk
Local Authorities	Bodies which are part of a group or pooled bodies which share unfunded costs on default	Admission bodies with no guarantors and a significant deficit
Bodies with local authority guarantor	Admission bodies with small deficit or surplus of assets over liabilities	Bodies with potentially limited life span and in deficit
Bodies with long-term funding from local or central government		No active members or is closed with a significant deficit
		Relies on voluntary or charitable source of income with significant deficit

A key aspect of the risk categorisation will be the level of deficit in the Fund. This will be monitored as noted below.

The Fund will consider whether further banding of risk is required for employers and in certain cases it may be full assessment of potential risk is needed on a bespoke basis.

In addition in the context of those employers providing a guarantee to the Fund for certain employer liabilities (typically Local Authorities) the risk would be re-categorised ignoring the guarantee. This will be to show the guarantors the level of exposure in terms of their existing guarantees.

2.4 NATURE OF RISK

The principal risk facing the North East Scotland Pension Fund is the inability of an employer to be able to meet its regular pension contributions and/or its liabilities upon termination. A deficit upon termination of an admission agreement might arise in the following scenarios:

a) Non-payment of contributions to the Fund by an employer prior to closure

b) Premature termination of a contract where market values are depressed relative to the liabilities in respect of an admission body, assessed on consistent assumptions to those adopted in the previous actuarial valuation.

c) The reality is less favourable than the assumptions used in setting contribution rates for that employer – for instance, lower than expected investment returns, higher than expected rates of early retirement or excessive pay increases.

d) Additional liabilities created as a result of the body closing, in particular the possible payment of immediate retirement benefits to all those eligible at that time.

e) A pre-existing deficit in the Fund (past service liability).

f) A change from open to closed status.

3 ASSESSMENT OF RISK

3.1 RISK CRITERIA

The Pensions Regulator has set out prescribed guidelines detailing the assessment criteria upon which an employer should be reviewed:

- Nature and prospects of the employer's industry.
- Employer's competitive position and relative size.
- Management ability and track record.
- Financial policy of the employer.
- Profitability, capital structure, cashflow and financial flexibility.
- Employer's credit rating.
- Position of the economy as a whole.

CIPFA also include information on how covenant and risk should be considered in their guidance Preparing and Maintaining a Funding Strategy Statement in the Local Government Pension Scheme.

Not all of the above would be applicable to assessing employer risk within the North East Scotland Pension Fund rather a balanced approach to consideration of the above criteria would be made, with further consideration given to the following:

- The scale of obligations to the pension scheme relative to the size of the employer's operating cashflow.
- The relative priority placed on the pension scheme compared to corporate finances.
- An estimate of the amount which might be available to the scheme on insolvency of the employer as well as the likelihood of that eventuality.

3.2 RISK PARAMETERS

For the North East Scotland Pension Fund, the risk a particular employer represents will be quantified using a five pronged approach, governed by the assessment criteria or triggers outlined below. Where one or more of these triggers is engaged, such employers will be subject to a more detailed review by the Fund. These criteria, when analysed in conjunction with the strength of the employer covenant (Section 5), will provide the basis for the framework upon which risk will be continually assessed and employer stability monitored.

1. Employer with less than five active members
2. Employer where significant member movements are imminent
3. Employer with a known participation length of 18 months or less
4. Employer with a known deficit of a significant level, relative to size of its financial metrics
5. Employer with a funding level identified at the last review of less than 80% or a deficit greater than £0.5m

4 MONITORING/SCREENING OF THE EMPLOYER COVENANT

4.1 ASSESSING THE EMPLOYER COVENANT

The employer covenant should be assessed objectively and the ability of employers or guarantors to meet their obligations should be viewed in the context of the Fund's exposure to risk and volatility, while preserving the interests of other employers within the Fund. The monitoring of covenant strength by itself does not strengthen the Fund's security; however, it does enable the Fund to anticipate and pre-empt employer funding issues and thus adopt a proactive approach with a view to reminding employers of their obligations and managing their expectations. In order to objectively monitor the strength of an employer's covenant, adjacent to the risk posed to the Fund, the proposal is for a number of fundamental financial metrics to be appraised to develop an overview of the employer's stability. These financial metrics centre around the following:

- Does the employer have a guarantor within the Fund or employer structure?
- The employer's funding source and length (if known).
- The employer's cashflow forecast, ideally over the next three to five years.
- If the employer has any contingent assets which can be used by the Fund to provide security.

In order to accurately monitor employer covenant, it will be necessary for research to be carried out into employers' backgrounds and, in addition, for those employers to be contacted sensitively to gather as much information as possible. Focus will be placed on the continual monitoring of employers with a proactive rather than reactive view to mitigating risk.

An overview of the framework upon which an employer's covenant will be monitored is detailed in the diagram overleaf (4.4). It is considered that this will provide the basis for actions to be taken and ultimately the management of risk, covered in the next section.

4.2 FREQUENCY OF MONITORING

The funding position and contribution rate for each employer participating in the Fund will be reviewed as a matter of course with each triennial actuarial valuation. However, it is important that the relative financial strength of employers is reviewed regularly to allow for a thorough assessment of the financial metrics. There will be instances where known 'events' or individual employer circumstances are to be taken into consideration, and they will be incorporated into the monitoring framework.

Employers subject to a more detailed review, where a risk criterion is triggered, will be reviewed at least every six months, but more realistically with a quarterly focus. In such cases a more in depth analysis will be carried out taking into consideration all of the financial metrics and extenuating circumstances.

Separately the funding position will be monitored in conjunction with the Actuary to consider the potential exposure of the Fund in light of the covenant strength.

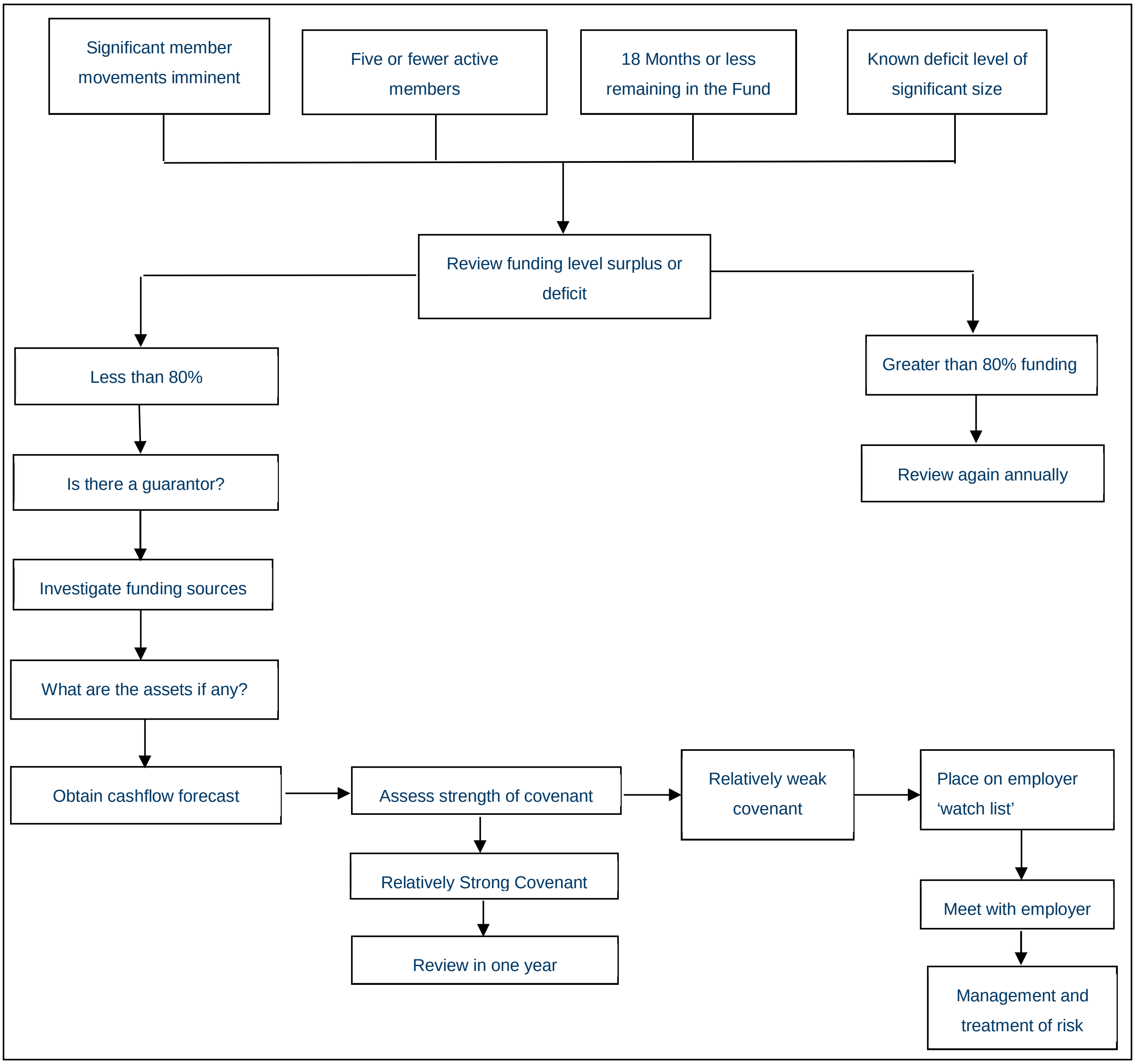
4.3 EMPLOYER MEETINGS

As a basis for the monitoring of employers within the Fund, meetings are to be scheduled with those organisations where there is a particular concern over strength of their covenant, accrual of liabilities and future funding levels. Priority will be given to those employers requiring a more detailed review and the aim would be for meetings to be scheduled every six months for such organisations. In addition, it will also be necessary to arrange meetings with employers where there is a need to gain an understanding of their financial position with a view to assisting the monitoring process.

It is recognised that meetings will be tailored to each employer's needs, in conjunction with the Fund's assessment of that organisation; however, it is anticipated that the payment of pension liabilities on termination will feature heavily in these discussions.

There may also be a requirement for such organisations to draft a payment proposal for the Fund's consideration, along with a projection of future cash flows and income/expenditure.

4.4 GUIDE TOWARDS MONITORING OF THE EMPLOYER COVENANT



5 MANAGEMENT OF RISK
5.1 OVERVIEW

The focus of the Fund's risk management is the identification and treatment of the risks. It will be a continuous and evolving process which runs throughout the Fund's strategy. This management of risk is not a linear process; rather it is the balancing of a number of interwoven elements which interact with each other and which have to be in balance with each other if the management is to be effective.

5.2 INITIAL STEPS

For new bodies seeking admission to the Fund, the Pension Fund will conduct an audit to review the financial strength of the organisation, based on their accounts and other key criteria (scored out of 100).

- Regulation requires that relevant admission agreements must contain a provision requiring all bodies to undertake an assessment of the level of risk posed to the Fund in the event that the service contract terminates prematurely as a result of the organisation's insolvency, winding up or liquidation. Such assessments must take into account actuarial advice and must be carried out to the satisfaction of the relevant administering authority.
- In respect of outsourcing bodies, the North East Scotland Pension Fund (the Fund) will send out a risk assessment form to be completed by the outsourcing body at their expense. In order for a risk assessment to be conducted by the Fund actuary, the Scheme employer will need to provide a standard data file of the transferring staff to include names, national insurance numbers and details of current salary.
- For admission bodies, upon receipt of the results of the risk assessment, which will include a calculation of the employer contribution rate, details of the contracted arrangement between the Scheme employer and organisation will be clarified. The Scheme employer will be required to confirm the responsibility for pension costs and any other contractual arrangements which may affect the participation and also whether a bond or separate guarantee is required. If there is a limit on the amount that should be reclaimed directly from the outgoing employer due to contractual arrangements then the Scheme employer must notify the Fund in writing that this needs to be taken into account. Any residual deficit (or surplus) will revert to the Scheme employer.
- On termination of the admission agreement, any contributions due will first be reclaimed from the organisation. If the organisation defaults on any payments then the bond (if a bond is in place) would be called on. Any outstanding monies or residual surplus would then be dealt with as per Appendix B.

The Fund will require confirmation of a suitable guarantor or indemnity for any admission body applications (see comments in 5.3 below).

5.3 BOND/GUARANTEE

In the event that an organisation becomes insolvent, it is unlikely to be able to meet its funding obligations to the Fund. Allowing organisations to become an admission body, therefore, creates an element of risk for the Fund, for other employers participating in the Fund and, in particular, for any outsourcing employing body.

If a risk assessment identifies a material level of risk, for an admission body, the administering authority will require the organisation to provide an indemnity or bond to protect against the identified risk or alternatively a separate guarantee.

Outsourcing employing bodies should regularly review the level of risk relating to an admission agreement, and require the admission body to put in place a revised bond or indemnity as appropriate.

The bond is the third party legal instrument required in respect of an organisation's admission to the LGPS (together with the service contract and the admission agreement). Organisations should consider employer rate and/or cost of bonds when making tender. Therefore, it is ideal these increased costs are considered early in contract/tender discussions.

Where a bond has been requested by the parent body or administering authority there will be a defined amount and timescale set. It is, therefore, important for the Fund to document the expiry date of such bonds and to monitor these closely. Bond information will be reviewed annually or when an expiry date is approaching. The aim would be to inform parent bodies where an expiry date is imminent to allow them to consider whether a revised bond is required. In cases where a revised bond is not required or cannot be obtained, it will be emphasised to the parent body that the potential for liability exists as ultimate guarantor.

As an alternative to a bond, the Fund will allow the organisation in question to set up an alternative guarantee or contingent assets e.g. an escrow account to which the Fund has direct claim upon in the event of insolvency or default, for the equivalent of the bond amount calculated by the Fund actuary. The Fund will require satisfactory evidence of such an alternative particularly on the understanding that it can only be closed or terminated via mutual consent. More detail is set out in 5.5 below.

5.4 SHORTENED RECOVERY PERIOD

The Fund actuary, in line with the Fund's Funding Strategy Statement (FSS), assumes a deficit recovery period based on the specifics of each employer group or individual employer. The Fund reserves the right to adjust this recovery period, where appropriate, dependent on the strength of an individual employer's covenant, its financial stability and future prospects.

In doing so, the Fund makes provision for any potential liability to be recouped over a shorter timescale, particularly where there is a risk the body in question may cease to exist. The shortening of the recovery period will of course increase the rates at which the employer must contribute and this needs to be weighed up in terms of its reasonable affordability vs impact on longer term covenant.

This involves a fine balancing act as it is not in the Fund's or guarantor's interest to impose an employer rate which is unaffordable and ultimately results in the premature cessation of that employer.

5.5 CONTINGENT ASSETS

Contingent assets are assets which exist upon the occurrence of one or more specified future events, at the behest of the Fund – for instance, the failure to achieve a specified funding level. They are not typically included as Scheme assets, for the purpose of assessing whether a scheme meets its funding objective, until they are transferred to the scheme. Examples of contingent assets include:

- a known guarantor, which agrees to cover all liabilities/, a proportion of those liabilities (or equally receive all surplus or proportion of surplus), arising upon termination (the contingent event). This can take place through the absorption of the assets and liabilities by the guarantor to form part of its own position or through the payment of a specified amount.
- security over other assets – for instance, property or securities, such that the asset is transferred to the Fund if the contingent event occurs.
- a letter of credit or a bond (see 5.3).
- sterling cash put aside in a bank account whereby some or all of the cash would be released to the Fund on the occurrence of the contingent event – for example, an escrow account.

The above list is not exhaustive and the Fund will consider alternatives as appropriate to each individual circumstance.

5.6 PHASED IMPLEMENTATION OF EMPLOYER CONTRIBUTION RATE

For certain bodies, the decision may be taken for the Fund's actuary to certify an employer rate lower than the target rate calculated for that particular body. This will usually involve the certified rate being set at the same level as that from the previous actuarial valuation and is with a view to providing that employer with a period of stability to alleviate short term cash funding issues. In such cases, the Fund will look for employers to increase their contributions on a phased basis, culminating in their reaching the Fund actuary's target rate at the end of an agreed period - typically a 3 year implementation period. The underpayment would be expected to be paid as soon as practical.

In order to calculate the annual increments applicable, the methodology will be based on the Fund actuary's target contributions, over the current contributions payable by the employer.

It will be stressed to employers that such rates still remain subject to change at the next triennial actuarial valuation and the approach will be taken on a case by case basis, including the treatment of the underpayment.

5.7 INFLATED EMPLOYER CONTRIBUTION RATE (RISK PREMIUM)

Consistent with the Funding Strategy Statement (FSS), the funding objective for triennial actuarial valuations is to achieve and then maintain assets equal to the funding target. The funding target is the present value of 100% of projected accrued liabilities, including allowance for projected final pay, on the appropriate assumptions applicable to that employer.

In practice, each new employer's position is assessed separately and their individual rates take into account the differing circumstances of each employer and the funding plan covered in the FSS.

It is an avenue open to the Fund that contributions for an admitted body, where there is a weak employer covenant and an associated concern, could be set relative to the funding target in excess of 100% of the liabilities. This higher target represents a "risk premium" against potential additional liabilities on failure of that admitted body. For example, the employer contributions could be based upon a funding target of 110% of projected accrued liabilities or set dependent upon the Fund's view towards each employer's risk.

6. TRANSFER OF RISK FOR OUTSOURCED BODIES

6.1 TRANSFER OF RISK

In order to preclude cross subsidy within the Fund between certain admitted bodies and other employers, the costs and financial effects of employers' participation in the Fund are separately identified ('separation basis'). One result of this approach is that the risks associated with a defined-benefit scheme promise in respect of the transferring staff, are transferred to the new employer. The costs relating to salary increases and early retirements also become the responsibility of the new employer. This allocation of risk to the new employer is very important to protect the position of other employers in the Fund, particularly the letting authority. There are ways in which risks can be shared with the original employer and new employer such as via the separate contractual arrangement. This can include fixing or limiting the contribution requirements on an ongoing or termination basis within certain parameters. Whilst not a direct party in these arrangements the Administering Authority would need to be notified of any such arrangements if these are to be taken into account at the termination of participation.

7. TREATMENT OF MATERIALISED RISK

7.1 OVERVIEW

The Fund recognises that there will be instances where, despite the monitoring of employer covenant and steps taken to both manage and transfer risk (where practical), this risk will nevertheless materialise. As identified previously, the principal risk facing the North East Scotland Pension Fund is the inability of an employer to be able to meet its liabilities upon termination or otherwise. Therefore, a prescribed set of measures need to be agreed to respond to this eventuality, in order to minimise the impact on the Fund.

7.2 TERMINATION OF AN ADMISSION AGREEMENT

In the event of termination of an admission agreement, for any one of the reasons covered in section 2.4, it will be necessary for the Fund actuary to calculate the associated deficit on a least-risk or gilts basis (unless the liabilities are to be transferred to another employer in the Fund e.g. where another body is acting as a guarantor in which case typically the assumptions would be on an ongoing actuarial valuation basis). The organisation in question will be responsible for paying the actuary's fee for this work, and the Administering Authority reserves the right to include it in the termination assessment and final contribution due from the employer or recharge it directly from the employer.

The Fund will emphasise to employers their responsibility for the position upon termination; however, in certain circumstances where an exit payment is required, it may not be possible for an organisation to pay the total termination deficit in one lump-sum. In this scenario, the Fund would request the organisation provides a payment plan for review and, if this is not satisfactory, consideration will be given to an independent financial and governance review (see 7.6). In addition, in certain circumstances the Fund may agree to issue a “suspension notice” to an employer to suspend that employer’s liability to pay an exit payment starting from the date when that employer would otherwise become an exiting employer. Should this occur, the employer must continue to make such contributions towards the liabilities of the fund in respect of benefits for the employer’s current and former employees until a new and satisfactory valuation is carried out and the suspension notice is withdrawn. The Fund reserves the right to require a side legal agreement alongside any suspension notices detailing the terms of the arrangement including for example the length of such a notice, and the conditions for cessation of the agreement/notice.

Under the Regulations effective 1 April 2015 employers will automatically be deemed to terminate participation when the last active member leaves service.

7.3 CLOSED ADMISSION AGREEMENT WHERE NO ACTIVE MEMBERS REMAIN IN THE FUND

A closed admission agreement relates only to a fixed population of employees. In the case of an admission body, only those employees who transferred to the organisation from the outsourcing employing body can remain members of the LGPS through the admission agreement. Therefore, upon cessation of the last active member of a closed agreement, no further active members can be admitted and the approach for such cases would be the same as with ‘Termination of an admission agreement’ detailed in section 7.2.

7.4 OPEN ADMISSION AGREEMENT WHERE NO ACTIVE MEMBERS REMAIN IN THE FUND

An open admission agreement for an admission body potentially allows further employees of the organisation to become a member of the LGPS. In some cases however the employer may not propose employees do join.

Under the Regulations effective 1 April 2015 employers would automatically be deemed to terminate participation when the last active member leaves service. Such cases would be dealt with as per section 7.2.

All cases will be considered on their own merits and the Fund reserves the right to request full payment of the deficit assessed by the Fund Actuary. Set out below is a rule of thumb guide to the parameters that would be considered for a covenant based recovery period for an employer in deficit, where compliant with the parameters set out in the Funding Strategy Statement (FSS):

Weak employer covenant	A short recovery period (one or two valuation cycles i.e. 3-6 years) is preferable subject to contributions being reasonably affordable to the extent they do not impair the covenant.
Moderate employer covenant	As above but with perhaps 6-9 years being acceptable.
Strong employer covenant	As above but with perhaps 9-13 years being acceptable.

The covenant of the employer will be monitored on an ongoing basis as per section 4 above.

As with termination of an admission agreement, the costs of the Fund actuary's calculations will be the responsibility of the body in question. Agreement to the annual lump-sum payments will be required from the admitted body, in the same way that it would be sought in relation to ongoing employer rate contributions, calculated as part of the triennial actuarial valuation.

7.5 WINDING-UP, INSOLVENCY, OR CESSATION OF AN EMPLOYER

In the event an employer ceases to exist, the Fund would act as a creditor engaging with the administrator to recovery monies.

As part of the covenant assessment the Fund will consider the legal responsibility the employer has on termination in light of other legislation and priority order of other creditors.

7.6 INDEPENDENT FINANCIAL AND GOVERNANCE STANDING REVIEW BY THIRD PARTY AUDITOR

In addition to the Fund taking preventative steps towards risk and responding in the appropriate fashion to address materialising risk, it may be necessary for the Fund to appoint a third party agent to conduct an independent review.

This review would be centred upon the financial measures and wider robustness of the governance of the organisation, particularly with a view to instances of substandard management or negligent practice. The appraisal also provides the Fund with an external audit of the monitoring and risk aversion process employed, which is aimed at preserving the interests of all other participating employers and/or guarantor. The key objectives of this review will be to evaluate the financial standing and underlying governance arrangements, specifically:

- an assessment of the strength of the balance sheet and, based on this, drawing conclusions on the affordability of proposed termination payments. This element of the review will include, for example, structure/liquidity ratios; and
- a high-level evaluation of the body's overall governance structures and the adequacy of management's medium-term planning arrangements in addressing weaknesses and risks; and
- to develop an assessment methodology that can be applied to bodies in assessing their capability and capacity to manage and meet pension liabilities.

The above is not an exhaustive list of criteria that will be applied and each case will be considered on its own merits by the third party agent.

Appendix D – Glossary

Actuarial Valuation: an investigation by an actuary into the ability of the Fund to meet its liabilities. For the LGPS the Fund Actuary will assess the funding level of each participating employer and agree contribution rates with the administering authority to fund the cost of new benefits and make good any existing deficits as set out in the separate Funding Strategy Statement. The asset value is based on market values at the valuation date.

Administering Authority: the council with a statutory responsibility for running the Fund and that is responsible for all aspects of its management and operation.

Admission bodies: A specific type of employer under the Local Government Pension Scheme (the “LGPS”) who do not automatically qualify for participation in the Fund but are allowed to join if they satisfy the relevant criteria set out in the Regulations.

Benchmark: a measure against which fund performance is to be judged.

Best Estimate Assumption: an assumption where the outcome has a 50/50 chance of being achieved.

Bonds: loans made to an issuer (often a government or a company) which undertakes to repay the loan at an agreed later date. The term refers generically to corporate bonds or government bonds (gilts).

Career Average Revalued Earnings Scheme (CARE): with effect from 1 April 2015, benefits accrued by members in the LGPS take the form of CARE benefits. Every year members will accrue a pension benefit equivalent to 1/49th of their pensionable pay in that year. Each annual pension accrued receives inflationary increases (in line with the annual change in the Consumer Prices Index) over the period to retirement.

Contingent Assets: assets held by employers in the Fund that can be called upon by the Fund in the event of the employer not being able to cover the debt due upon termination. The terms will be set out in a separate agreement between the Fund and employer.

Covenant: the assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term or affordability constraints in the short term.

CPI: acronym standing for "Consumer Prices Index". CPI is a measure of inflation with a basket of goods that is assessed on an annual basis. The reference goods and services differ from those of RPI. These goods are expected to provide lower, less volatile inflation increases. Pension increases in the LGPS are linked to the annual change in CPI.

CPIH: An alternative measure of CPI which includes owner occupiers' housing costs and Council Tax (which are excluded from CPI).

Deficit: the extent to which the value of the Fund's past service liabilities exceeds the value of the Fund's assets. This relates to assets and liabilities built up to date, and ignores the future build-up of pension (which in effect is assumed to be met by future contributions).

Discount Rate: the rate of interest used to convert a cash amount e.g. future benefit payments occurring in the future to a present value.

Employing bodies: any organisation that participates in the LGPS, including admission bodies and Fund employers.

Employer's Future Service Contribution Rate (Primary Rate): the contribution rate payable by an employer, expressed as a % of pensionable pay, as being sufficient to meet the cost of new benefits being accrued by active members in the future. The cost will be net of employee contributions and will include an allowance for the expected level of administrative expenses.

Equities: shares in a company which are bought and sold on a stock exchange.

Exit Credit: the amount payable from the Fund to an exiting employer in the case where the exiting employer is determined to be in surplus at the point of cessation based on a termination assessment by the Fund Actuary.

Funding or solvency Level: the ratio of the value of the Fund's assets and the value of the Fund's liabilities expressed as a percentage.

Funding Strategy Statement: this is a key governance document that outlines how the administering authority will manage employer's contributions and risks to the Fund.

Government Actuary's Department (GAD): the GAD is responsible for providing actuarial advice to public sector clients. GAD is a non-ministerial department of HM Treasury.

Guarantee / guarantor: a formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's covenant to be as strong as its guarantor's.

Investment Strategy: the long-term distribution of assets among various asset classes that takes into account the Fund's objectives and attitude to risk.

Letting employer: an employer that outsources part of its services/workforce to another employer, usually a contractor. The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer.

LGPS: the Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility, members' contribution rates, benefit calculations and certain governance requirements.

Liabilities: the actuarially calculated present value of all benefit entitlements i.e. Fund cashflows of all members of the Fund, built up to date or in the future. The liabilities in relation to the benefit entitlements earned up to the valuation date are compared with the present market value of Fund assets to derive the deficit and funding/solvency level. Liabilities can be assessed on different set of actuarial assumptions depending on the purpose of the valuation.

Maturity: a general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.

McCloud Judgment: This refers to the linked legal cases of Sargeant and McCloud, and which found that the transitional protections (which were afforded to older members when the public service pension schemes were reformed in 2014/15) constituted unlawful age discrimination.

Members: the individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).

Minimum risk Basis: an approach where the discount rate used to assess the liabilities is determined based on the market yields of Government bond investments based on the appropriate duration of the liabilities being assessed. This is usually adopted when an employer is exiting the Fund. At the valuation date this was equivalent to a discount rate of CPI less 1.4% p.a.

Orphan liabilities: liabilities in the Fund for which there is no sponsoring employer within the Fund. Ultimately orphan liabilities must be underwritten by all other employers in the Fund.

Percentiles: relative ranking (in hundredths) of a particular range. For example, in terms of expected returns a percentile ranking of 75 indicates that in 25% of cases, the return achieved would be greater than the figure, and in 75% cases the return would be lower.

Phasing/stepping of contributions: when there is an increase/decrease in an employer's long term contribution requirements, the increase in contributions can be gradually stepped or phased in over an agreed period. The phasing/stepping can be in equal steps or on a bespoke basis for each employer.

Pooling: employers may be grouped together for the purpose of calculating contribution rates, (i.e. a single contribution rate applicable to all employers in the pool). A pool may still require each individual employer to ultimately pay for its own share of deficit, or (if formally agreed) it may allow deficits to be passed from one employer to another.

Prepayment: the payment by employers of contributions to the Fund earlier than that certified by the Actuary. The amount paid will be reduced in monetary terms compared to the certified amount to reflect the early payment.

Present Value: the value of projected benefit payments, discounted back to the valuation date.

Primary rate: the contribution rate required to meet the cost of future accrual of benefits, ignoring any past service surplus or deficit but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer's covenant.

Profile: the profile of an employer's membership or liability reflects various measurements of that employer's members, i.e. current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc.

Prudent Assumption: an assumption where the outcome has a greater than 50/50 chance of being achieved i.e. the outcome is more likely to be overstated than understated. Legislation and Guidance requires the assumptions adopted for an actuarial valuation to be prudent.

Rates and Adjustments Certificate: a formal document required by the LGPS (Scotland) Regulations, which must be updated at least every three years at the conclusion of the formal valuation. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three year period until the next valuation is completed.

Real Return or Real Discount Rate: a rate of return or discount rate net of (CPI) inflation.

Recovery period: the target length of time over which the current deficit is intended to be paid off or the current surplus is intended to be refunded.

Recovery Plan: a strategy by which an employer will make up a funding deficit or run off surplus over a specified period of time ("the recovery period"), as set out in the Funding Strategy Statement.

Secondary rate: the adjustment to the Primary rate to arrive at the total contribution each employer is required to pay. It is essentially the additional contribution (or reduction in contributions) resulting from any deficit (or surplus) attributable to the employer within the Fund.

Section 13 Valuation: in accordance with Section 13 of the Public Service Pensions Act 2014, the Government Actuary's Department (GAD) have been commissioned to advise the Scottish Public Pensions Agency (SPPA) in connection with reviewing the 2020 LGPS actuarial valuations. All LGPS Funds therefore will be assessed on a standardised set of assumptions as part of this process.

Solvency Funding Target: an assessment of the present value of benefits to be paid in the future. The desired funding target is to achieve a solvency level of a 100% i.e. assets equal to the accrued liabilities at the valuation date assessed on the ongoing concern basis.

Suspension Notice: A notice that may be issued to an employer to suspend that employer's liability to pay an exit payment in circumstances where the employer would otherwise exit. Should a notice be made, the employer must continue to make such contributions towards the liabilities of the fund in respect of benefits for the employer's current and former employees until a new and satisfactory valuation is carried out and the suspension notice is withdrawn. A side legal agreement may be required alongside such notices.

SWAPS: a generic term for contracts put in place with financial institutions such as banks to limit the Fund's investment and other financial risks.

Valuation funding basis: the financial and demographic assumptions used to determine the employer's contribution requirements. The relevant discount rate used for valuing the present value of liabilities is consistent with an expected rate of return of the Fund's investments. This includes an expected out-performance over gilts in the long-term from other asset classes, held by the Fund.

50/50 Scheme: in the LGPS, active members are given the option of accruing a lower personal benefit in the 50/50 Scheme, in return for paying a lower level of contribution.

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Report on the Actuarial Valuation as at 31 March 2020

North East Scotland Pension Fund

March 2021

welcome to brighter

Contents

Appendices

Introduction

This report is addressed to the Administering Authority of the North East Scotland Pension Fund ("the Administering Authority") and is provided to meet the requirements of Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended) ("the Regulations"). It describes the factors considered by the Administering Authority when carrying out the actuarial valuation as at 31 March 2020 and the decisions reached as a result.

The purpose of the actuarial valuation is for the Administering Authority to determine:

1. The expected cost of providing the benefits built up by members at the valuation date (the 'liabilities'), and compare this against the funds held by the Fund (the 'assets').

2. The contributions needed to cover the cost of the benefits that active members will build up in the future and other costs incurred in running the Fund (the 'Primary Contribution Rate').

3. An appropriate plan for making up the shortfall if the Fund has less assets than liabilities or refunding the surplus if the Fund has more assets than liabilities. This plan will cover the amounts which will need to be paid (the 'Secondary Contribution Rate') and the timeframe over which they will be paid ('the Spread Period').

Signature		
Name	Paul Middleman	Laura Evans
Qualification	Fellow of the Institute and Faculty of Actuaries	Fellow of the Institute and Faculty of Actuaries
Date	31 March 2021	

This report uses various technical terms. These are explained in more detail in the explanatory boxes which appear throughout this report, and in the Glossary at Appendix H.

This report has been prepared in accordance with Technical Actuarial Standards TAS 100: Principles for Technical Actuarial Work and TAS 300: Pensions which are issued by the Financial Reporting Council. The calculations referred to in the report use methods and assumptions appropriate for reviewing the financial position of the Fund and determining a contribution rate for the future. Mercer does not accept liability to any third party in respect of this report; nor do we accept liability to the Administering Authority if the information provided in this report is used for any purpose other than that stated. The report may be disclosed to members and others who have a statutory right to see it. It may also be disclosed to any participating employer and, if the Administering Authority and Mercer consent, it may be disclosed to other third parties.

1 Funding Strategy – Key Elements

Fundamental to the valuation results is the funding strategy adopted by the Fund. This funding strategy is set out in a specific document (the Funding Strategy Statement or FSS for short) which is one of the Administering Authority's key governance documents for the Fund. In essence, the FSS sets out an overview of the approach to be used for the actuarial valuation. Amongst other things it outlines the assumptions, both economic and demographic, to be used in calculating the value of the liabilities built up, the contributions required to correct any funding shortfall or surplus, and the contribution rate required to fund the benefits for future service. It also sets out the strategy for making good any funding shortfall, in particular how any shortfall is expected to be financed in terms of the balance between future contributions and future investment returns, and the period over which any surplus or shortfall is expected to be recovered.

> The FSS is the Administering Authority's key governance document in relation to the actuarial valuation. It sets out the funding policies adopted, the actuarial assumptions used, and the timescales over which deficits will be paid off. Employers are consulted about the FSS as part of the actuarial valuation process.

The principal elements of the funding strategy adopted for this actuarial valuation are as follows:

- The McCloud judgment (see Appendix D for details) – the valuation results as set out in Section 2 of this report include an allowance in relation to the potential cost of the McCloud judgment. An estimate of the effect of the judgment, based on the proposed remedy in the consultation launched in July 2020 for the Whole Fund is shown at the end of that section. Each employer has been notified of the estimate of the potential cost of the proposed remedy which has been included in their liabilities and the additional contributions over 2021/24 in respect of this. For simplicity, although the proposed remedy would lead to the underpin no longer applying to accrual post 31 March 2022, the estimated cost of future accrual up to that point has been spread over the three years of the certification period i.e. 1 April 2021 – 31 March 2024.

> The "McCloud judgment" refers to the legal decisions in the Sargeant/McCloud cases for the Fire and Judiciary pension arrangements. The courts ruled that the transitional protections afforded to older members when these schemes were amended constituted unlawful age discrimination. Remedial action, in the form of benefit changes for these schemes, will therefore be required. Although the above cases did not relate directly to the LGPS, the UK Government has accepted that remedies will need to apply to all the public service pension schemes, including the LGPS. For the LGPS the transitions protections took the form of an underpin, where older members got the better of the benefits payable under the new and old schemes. At this stage it seems likely that the remedy will be to extend this underpin to younger members (see Appendix D for more details), and we have allowed for this in our calculations.

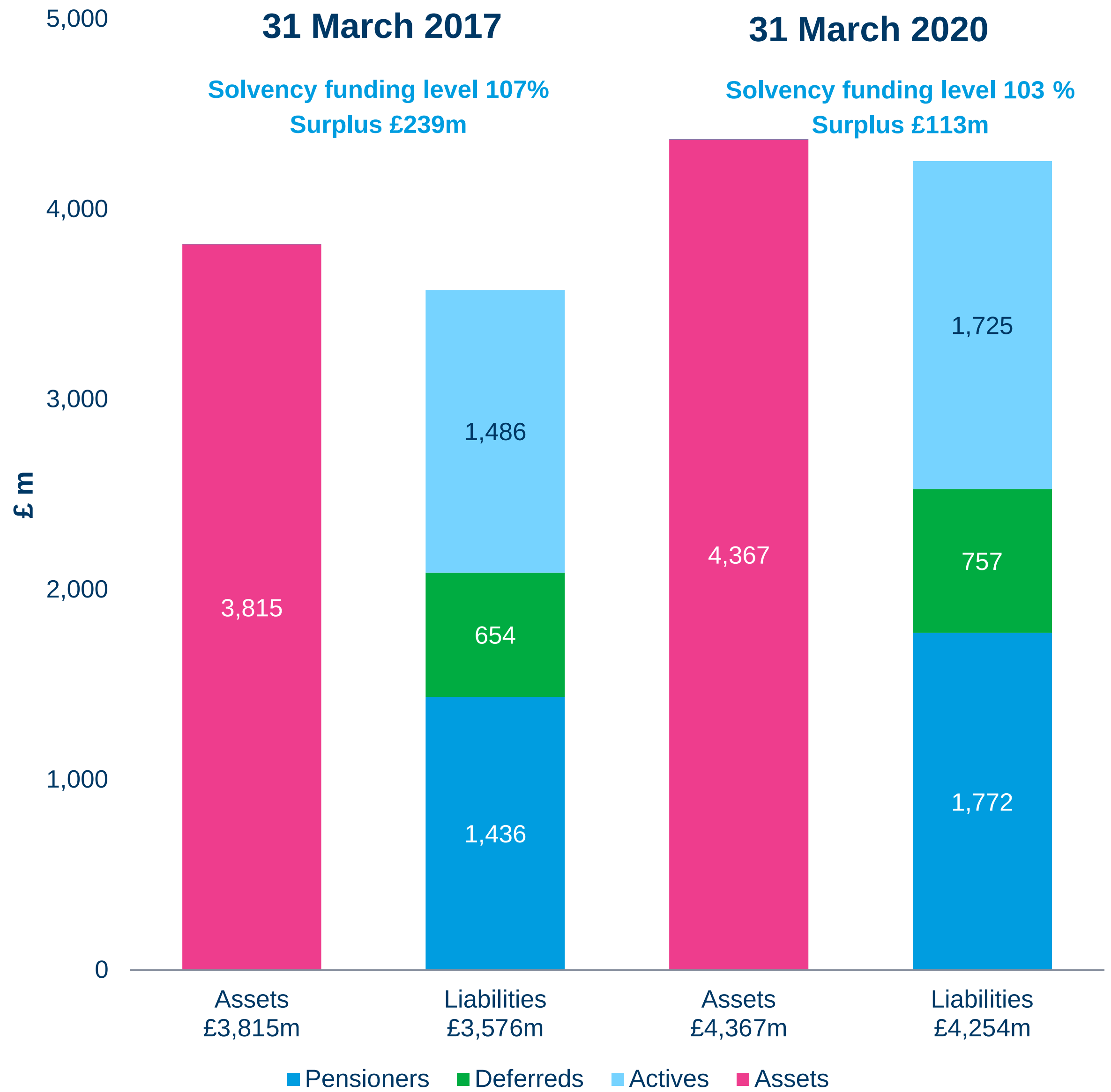
- Following the Government's recent consultation, the liabilities also allow for the "Interim solution" for GMP to be extended in order to provide full CPI indexation on GMP benefits in payment for all members with a state pension age after 5 April 2016. The cost of this (combined with the cost of the McCloud judgment) is set out in Section 2.
- We have made allowance for the Fund's pre 86 pension increase recharge arrangement with the Aberdeen City Council Transport Fund.
- Assumed rate of future long term average CPI inflation – 2.1% p.a., based on the yields available on gilts and index-linked gilts of appropriate duration less an adjustment of 0.6% p.a. to allow for the difference between market-implied future RPI and estimated future CPI inflation.
- Since the valuation date, it has been announced that RPI inflation will be reformed with effect from 2030 to align the index with the CPIH inflation measure. At the valuation, CPI inflation was assumed to be 0.6% p.a. lower than RPI inflation. This adjustment will be kept under review over time.
- Real investment returns over and above CPI for past service – 1.25% p.a., based on the anticipated real returns achievable on the Fund's expected long-term investment strategy with a suitable margin for prudence.
- Real investment returns over and above CPI for future service – 1.50% p.a., based on the anticipated real returns achievable on future invested contributions.
- Future pay growth – Depending on individual circumstances, some employers have made allowance for either 1% p.a. or 2% p.a. over the three years to 31 March 2023, and then 1.5% p.a. over and above CPI in the longer term.
- Baseline life expectancy based on a scheme-specific mortality study.
- Future mortality improvements based on the CMI 2019 model with a long-term improvement trend of 1.75% p.a.
- An average spread period of 12 years for correcting any imbalance between the existing assets and past service liabilities. The FSS sets out the circumstances in which this might vary from one employer to another.

2

Key results of the funding assessment

Solvency funding position

The table below compares the assets and liabilities of the Fund at 31 March 2020. Figures are also shown for the last valuation as at 31 March 2017 for comparison.



The liability value at 31 March 2020 shown in the chart above is known as the Fund's "solvency funding target". The solvency funding target is calculated using assumptions that the Administering Authority has determined are appropriate having consulted with the actuary, and are also set out in the FSS.

The chart shows that **at 31 March 2020 there was a surplus of £113m** against the Fund's solvency funding target. An alternative way of expressing the position is that **the Fund's assets were sufficient to cover 103% of its liabilities** – this percentage is known as the solvency funding level of the Fund.

At the previous valuation at 31 March 2017 the surplus was £239m, equivalent to a solvency funding level of 107%. The key reasons for the changes between the two valuations are considered in Section 3.

Further details of the way in which the solvency funding target has been calculated are set out in Appendix A.

The LGPS Regulations require the contributions to be set so as to secure the Fund's solvency and long-term cost efficiency. In this context solvency means being able to meet the liabilities as and when they arise, with long-term cost efficiency meaning that contribution levels should not be set so as to give rise to additional costs at a later date. In practice, contribution levels have been set so as to target a solvency funding level of 100%, based on the funding parameters outlined in Section 1 above.

Primary Contribution Rate

The valuation looks at the normal employer contribution rate required to cover the cost of the benefits (including death benefits and expenses) that will be built up over the year after the valuation date (the "Primary Contribution Rate"). A summary of the assumptions used is provided in Appendix A.

The table below gives a breakdown of the Primary Contribution Rate at 31 March 2020 and also shows the corresponding rate at 31 March 2017 for comparison. In calculating the average Primary Contribution Rate we have not made any allowance for future members to opt for the 50:50 scheme.

The "Primary rate" of the employers' contribution is the contribution rate required to meet the cost of the future accrual of benefits including ancillary, death in service and ill health benefits together with administration costs.

Active members pay contributions to the Fund as a condition of membership in line with the rates required under the governing Regulations (see Appendix D).

	% of Pensionable Pay	
PRIMARY CONTRIBUTION RATE	**31 March 2020**	**31 March 2017**
Normal Contribution rate for retirement and death benefits	27.4	27.7
Allowance for administrative expenses	0.4	0.4
Total normal contribution rate	27.8	28.1
Average member contribution rate	6.1	6.1
Primary contribution rate*	21.7	22.0

** In line with updated CIPFA guidance, the 2020 Primary Contribution Rate is the weighted average of the individual employer Primary Contribution Rates as derived based on their individual circumstances (e.g. whether or not they are closed to new entrants).*

Correcting the imbalance – Secondary Contribution Rate

The funding objective as set out in the FSS is to achieve and maintain a solvency funding level of 100% of liabilities (the solvency funding target). In line with the FSS, where a shortfall exists at the effective date of the valuation a recovery plan will be put in place which requires additional contributions to correct the shortfall. Equally, where there is a surplus it is usually appropriate to offset this against contributions for future service, in which case contribution reductions will be put in place to allow for this.

The FSS sets out the process for determining the recovery plan in respect of each employer. At this actuarial valuation the average weighted spread period adopted is 12 years and the total initial surplus offset (the "Secondary rate" for 2021/22) is an offset of approximately 2.5% of pay per annum (which allows for the contribution plans which have been set for individual employers under the provisions of the FSS), including the estimated costs in relation to the McCloud judgment.

The "Secondary rate" of an individual employers' contribution is an adjustment to the Primary Contribution Rate to reflect any past service deficit or surplus, to arrive at the rate the employers are required to pay.

The McCloud Judgment and GMP indexation

> The "McCloud judgment" refers to a legal challenge in relation to historic benefit changes for all public sector schemes being age discriminatory. The Government announced in 2019 that this needs to be remedied for all schemes including the LGPS. This is likely to result in increased costs for some employers. This remedy is not yet agreed but the consultation in 2020 set out the Government's intended approach to address the implications.

As described in Section 1 of this report, the above figures include an allowance for the estimated cost of the McCloud judgment. Additionally, they also assume that full CPI indexation of GMP benefits in payment will be extended to cover all members with a state pension age after 5 April 2016. At the overall Fund level we estimate that the cost of both these factors could be an increase in past service liabilities of broadly £45 million and an increase in the Primary Contribution rate in respect of the McCloud Judgment of 0.8% of Pensionable Pay per annum from 2020 until 2022. For the purpose of contribution setting, we have spread this over the three years in the certification period resulting in a cost of c0.5% of Pensionable pay per annum from 1 April 2021 – 31 March 2024.

3

Experience since last valuation

Summary of key inter-valuation experience

The outcomes from the valuation are determined both by the assumptions adopted for the future, and the Fund's historic experience relative to assumptions made in the past. In this section we consider the effect of the Fund's experience over the last three years.

The last actuarial valuation was carried out with an effective date of 31 March 2017. With effect from 1 April 2015 the scheme's benefit structure changed from a Final Salary Scheme to a Career Average Revalued Earnings (CARE) Scheme, and the 2017 actuarial valuation took these changes into account.

The average Pensionable Salary increase for the Fund members who were in service for the whole of the inter-valuation period was c4% per annum.

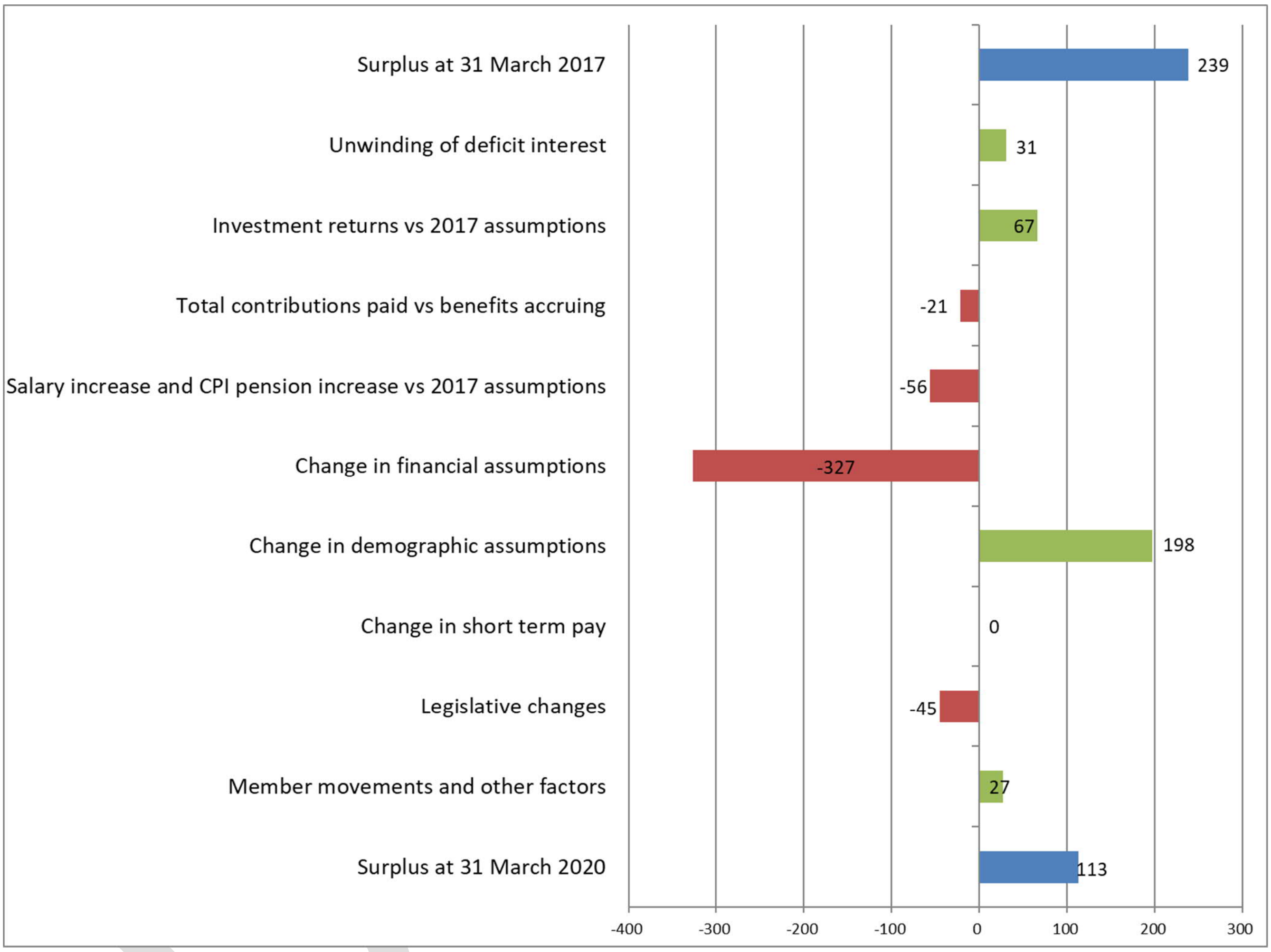
Pensions in payment (in excess of Guaranteed Minimum Pensions (GMPs) were increased as guaranteed under the Fund as follows:

- April 2018 3.0%
- April 2019 2.4%
- April 2020 1.7%

Over the inter-valuation period, benefit inflation has averaged 2.4% p.a. Over the three years to 31 March 2020 the gross investment return on the Fund's assets has averaged 5.8% per annum, meaning that the average real return over CPI inflation has been about 3.4% p.a.

Reasons for the change in funding position since the last actuarial valuation

The surplus at the last valuation date was £239m. The chart below sets out the main reasons for the change in the shortfall between 31 March 2017 and 31 March 2020 (figures shown in £m).



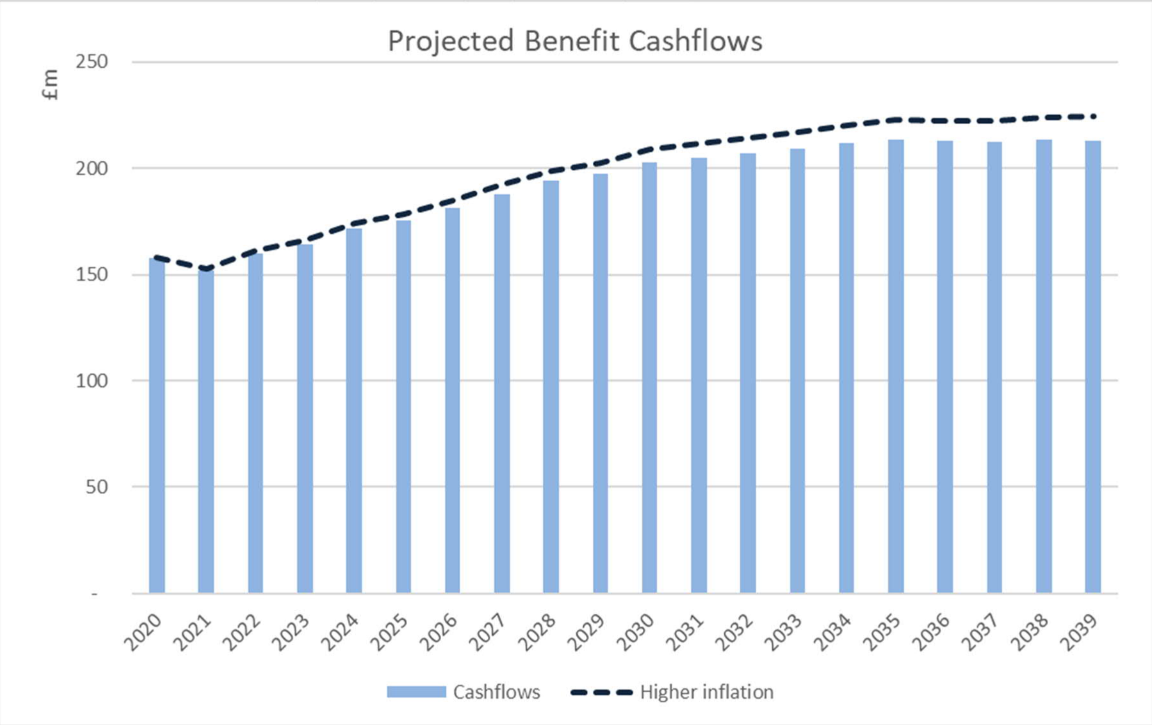
4

Cash flows, risks and alternative funding positions

Benefit cash flows

The projected benefit cash flows which result from applying the assumptions as set out in Appendix A are shown in the chart below. The additional trendline sets out how those total projected benefit cash flows would change if we were to assume inflation of 0.25% p.a. higher than the assumption of 2.1% p.a. used for the actuarial valuation. Over the 20 years following the valuation date, the extra benefit payments which would result from the extra 0.25% p.a. inflation assumption are projected to be £113m.

The actuarial valuation process is principally concerned with projecting all the expected benefit cash flows into the future, and then converting them into present day values by discounting them to allow for assumed future investment returns. The chart shows those projected cash flows, and also illustrates how sensitive they are to the future inflation assumption.



Projected funding position at next actuarial valuation

As part of this valuation, the Administering Authority has set an average spread period of approximately 12 years. The next actuarial valuation will take place with an effective date of 31 March 2023. If experience up to that date were to be in line with the assumptions made for this current actuarial valuation and contributions are paid at the agreed rates or amounts, there would be a surplus at 31 March 2023 of £56m, equivalent to a funding level of 101%.

Material risks faced by the Fund

The Fund is subject to some potentially material risks that are, to an extent, outside the Administering Authority's control, but could affect the funding level and ultimately the employer contribution requirements. Any material worsening of the funding level will mean more contributions are needed (either at an increased rate or at the same rate over a longer period) to be able to provide the benefits built up in the Fund – unless experience acts in other ways to improve the funding level. Examples of such risks, and how the Administering Authority manages them, are:

> Funding a defined benefit pension scheme such as the LGPS which is open to new members is by its nature uncertain, and involves some level of risk. The principal funding risks are investment (e.g. whether the Fund earns the desired level of long-term real returns) and demographic (e.g. whether longevity of members is longer or shorter than anticipated). In practice, the key is whether such risks can be managed and mitigated.

- If an Employer becomes unable to pay contributions or to make good deficits in the future, the Fund's assets will be lower than expected and the funding level will be worse than expected. The Administering Authority regularly monitors the financial strength of the Employers so that actions can be taken to mitigate (but not fully remove) the risk.
- If future investment returns on assets are lower than assumed in the valuation, the Fund's assets will be lower, and the funding level worse, than expected. The Administering Authority has a process in place to monitor investment performance quarterly, and it reviews the Fund's investment strategy alongside each actuarial valuation.
- If improvements in life expectancy are greater than assumed, the cost of benefits will increase because members are living longer than expected. This will mean the funding level will be worse than expected. The Administering Authority regularly reviews the Fund's experience and ensures that the assumptions it makes about members' life expectancy take the most recent information available into account.
- If members make decisions about their options which increase the Fund's liabilities, the funding level will be worse than expected. An example would be if members commute less pension for cash, than is being assumed. The Administering Authority reviews the Fund's experience at each valuation to ensure that their treatment of member options remains appropriate.

Impact of COVID-19

The valuation results and employer contributions shown in this report are assessed as at 31 March 2020. In March 2020 we saw significant falls in equity markets around the world in relation to the COVID-19 pandemic, though markets subsequently rebounded strongly over the year. This potentially has far-reaching consequences in terms of funding and risk which have been considered when discussing contribution requirements with employers. As the position continues to evolve, this will be kept under review by the Administering Authority, who will monitor the development of the situation and keep all stakeholders informed of any potential implications so that the outcome can be managed effectively.

Sensitivity of funding position to changes in key assumptions

The value placed on the Fund's liabilities is critically dependent on the assumptions used to carry out the calculations. If future experience differs from the assumptions the Administering Authority has used after consulting with the Employers, then the projected future funding level will be different from the level described above.

To illustrate how sensitive the funding level is to experience being different from assumed, the table below shows how the valuation results at 31 March 2020 would have differed given small changes in the key assumptions.

Assumption change	Increase/(Reduction) in surplus at 31 March 2020 (£m)	Resultant surplus (deficit) at 31 March 2020 (£m)
Original solvency funding position	-	113
Real investment return 0.25% lower than assumed	-172	(59)
Pensionable Salary growth 0.25% higher than assumed	-18	95
Long term improvement rate in life expectancy increased by 0.25% per annum	-31	82
Assets fall by 25%	-1,092	(979)

Minimum risk funding position

In assessing the value of the Fund's liabilities (the solvency funding target), allowance has been made for investment returns as described in Appendix A, taking into account the investment strategy adopted by the Fund, as set out in the Fund's Statement of Investment Principles (SIP).

It is not possible to construct a portfolio of investments which produces a stream of income exactly matching the expected liability outgo. However, it is possible to construct a portfolio which attempts closely to match the liabilities and provide a high level of certainty in future investment returns above CPI inflation. This represents a "minimum risk" investment position. Such a portfolio would consist mainly of a mixture of long-term index-linked and fixed interest gilts. Investment of the Fund's assets in line with the minimum risk portfolio would minimise fluctuations in the Fund's minimum risk funding level between successive actuarial valuations but would result in much higher employer contributions (all other things being equal).

If, at the valuation date, the Fund had been invested in this portfolio, then in carrying out the valuation it would not be appropriate to make any allowance for out-performance of the Fund investments. In this event the value of the Fund liabilities would have increased substantially, to £7,074m, and the funding level would have reduced correspondingly to 62%. If the actuarial assumptions are borne out in practice and contributions are paid in line with the Rates and Adjustment Certificate for all employers, the projected funding level on this basis at the next actuarial valuation would be slightly higher at 63%.

The value of the liabilities on the ongoing solvency funding target assumptions was £4,254m, which is £2,820m less than the value on the minimum risk basis. The funding plan is therefore making a prudent allowance for future investment returns of £2,820m over and above those available from the notional minimum risk investment portfolio to support the funding of member benefits along with contributions payable. This is an indication of the expected return built into the funding strategy for the Fund as a whole

.

Appendices

Appendix A
Assumptions

How the benefits are valued

In order to calculate the liabilities, there is a need to make assumptions about various factors that affect the cost of the benefits provided by the Fund – for example, how long members will live, or the future level of inflation. The table below explains the key assumptions being made in the valuation.

Assumption	Why it is important and how it impacts on the liabilities
Discount rate	The majority of benefits in a pension fund are paid many years in the future. In the period before the benefits are paid, the Administering Authority invests the funds held by the Fund with the aim of achieving a return on those funds. When calculating how much money is needed now to make these benefit payments, it is appropriate to make allowance for the investment return that is expected to be earned on these funds. This is known as "discounting". The higher the investment return achieved, the less money needs to be set aside now to pay benefits. The calculation reflects this by placing a lower value on the liabilities if the "discount rate" is higher.
Inflation	Pensions in payment increase in line with Consumer Price Inflation (CPI). Salary growth is also normally linked to price inflation in the long term. A higher inflation assumption will, all other things being equal, lead to a higher value being placed on the liabilities.
Pensionable Salary growth	Benefits earned prior to 1 April 2015 for active members are based on their salaries immediately before retirement, so it is necessary to make an assumption about future Pensionable Salary growth. The higher this assumption, the higher the value placed on the liabilities for active members.
Life expectancy	Pensions are paid while the member (and potentially their spouse or partner) is alive. The longer people live, the greater is the cost of providing a pension. Allowing for longer life expectancy therefore increases the liabilities.

The liabilities of the Fund are calculated by projecting forward all of the future benefit cash flows and discounting them back to the effective date of the valuation, using these assumptions. For example, the liability for a single pensioner is calculated by estimating the amount of each pension payment they will receive in the future, multiplying by the probability that the member will still be alive by the date of each payment, and then discounting each payment back to the effective date of the valuation using the appropriate discount rate, and then summing up all of these discounted amounts. The liabilities for the whole Fund are calculated by summing the liabilities for each of the individual members.

Financial assumptions used to calculate the solvency funding target

The table below summarises the key financial assumptions used in the calculation of the solvency funding target at whole Fund level and those used for the 31 March 2017 actuarial valuation. Section 1 of this report sets out how these assumptions might vary from one employer to another.

Financial assumptions	31 March 2020	31 March 2017
Discount rate	3.35 % p.a.	4.15% p.a.
Price inflation (CPI)	2.1% p.a.	2.4% p.a.
Salary increases (short term)	Varies by employer*	Varies by employer**
Salary increases (long term)	3.60% p.a.	3.90% p.a.
Pension increases in payment:	2.1% p.a.	2.4% p.a.

** Employers selected one of the following; no short term pay allowance, 1% p.a. or 2% p.a. for the three year period to 31 March 2023.*

*** Employers selected one of the following; no short term pay allowance, 1% p.a. or 2.4% p.a. (i.e CPI) for the three year period to 31 March 2020.*

Our analysis of expected future real investment returns uses a Monte Carlo simulation (stochastic) model, based on 4,000 simulations. Within the overall analysis we specify and calibrate a range of economic and asset class models. Our analysis uses an asset correlation matrix to help generate each stochastic simulation. The model includes estimates for long-term expected returns and inflation along with volatilities each asset class and inflation.

The key financial assumption is the expected long term investment return above CPI inflation as this is usually the principal factor which determines the long term cost to employers via their contributions. In determining this we consider first the long term real returns (i.e. returns above CPI) which the Fund's investment strategy can be expected to deliver based on market outlook at the valuation date taking into account the projected cashflow position of the Fund. This analysis then helps us recommend and agree with the Administering Authority on a suitably prudent assumption for the valuation discount rate based on the investment strategy, any risk management framework in place, and reasonably allowing for the likely changes in investment strategy as the Fund matures. In order to consider the level of prudence we look at the likelihood of the expected real return from the Fund's assets exceeding the assumption made. We measure this by considering the percentile expected return from the analysis. A return assumption higher than the 50th percentile return from the analysis can be deemed to be prudent and retain margins to provide some protection against increases in contributions at future valuations.

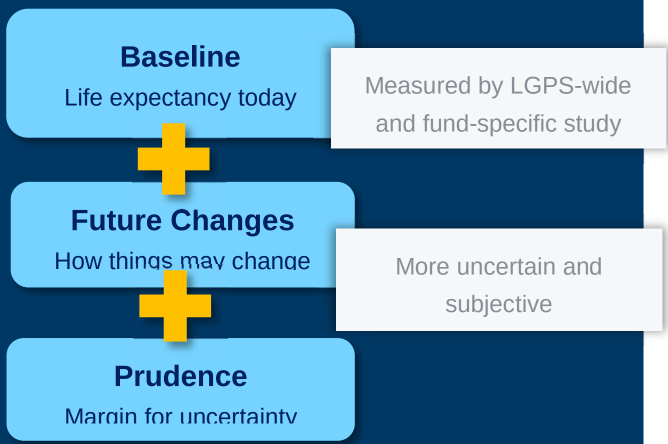
At this actuarial valuation the real discount rate which we have used is 1.25 % p.a., which is broadly the 58th percentile return from our analysis. At the previous valuation the real discount rate used was 1.75% p.a., which at the time was the 70th percentile return from similar analysis at the time.

Demographic assumptions used

Post-retirement Mortality

There are two separate decisions on mortality assumptions:

- The baseline table for the current rates of mortality; and
- The allowance for future improvements.



Mortality (or life expectancy) tables are typically made up of three elements: a baseline table (equivalent to the expected current mortality), an allowance for future improvements, and a margin for prudence. Very few pension funds are large enough for them to be able to determine a bespoke set of baseline assumptions based purely on the fund's own membership experience. Typically, the life expectancy assumptions are set by benchmarking a fund's membership profile and mortality experience against larger external datasets. For this actuarial valuation, we have benchmarked the Fund's membership profile and experience against the "S tables" published by the CMI. We have applied weightings as appropriate to adjust the standard tables so as to arrive at assumptions which are appropriate for the Fund. We have generally used the S3PA tables ("middle" tables for females), other than for female dependants where the S3DA tables have been used and for members retiring in ill health where the S3IA tables have been used. At the 2017 actuarial valuation the S2PA tables were used (S2DA tables for female dependants).

The weightings and age ratings applied to the above are set out in the table below.

Current Status	Retirement Type	2020 weighting/age rating	2017 weighting/age rating
Annuitant	Normal Health	114% males, 101% females	103% males, 98% females
	Dependant	150% males, 104% females	129% males, 113% females
	Ill Health	136% males, 144% females	103% males, 98% females with an age rating of +3 years in each case
	Future Dependant	146% males, 121% females	125% males, 114% females
Active	Normal Health	121% males, 101% females	100% males, 90% females
	Ill Health	134% males, 151% females	100% males, 90% females with an age rating of +4 years in each case
Deferred	All	144% males, 116% females	128% males, 104% females
Active/ deferred	Future Dependant	153% males, 128% females	107% males, 104% females

A weighting applied to an actuarial table has the effect of increasing or reducing the chance of survival at each age, which increases or reduces the corresponding life expectancy. Similarly, an age rating applied to an actuarial table has the effect of assuming that beneficiaries have a life expectancy equal to those older (or younger) than their actual age.

Future improvements are assumed to follow the CMI 2019 model with a 1.75% p.a. long-term improvements trend. At the 2017 actuarial valuation the CMI 2015 model with 1.75% p.a. long-term trend for males and 1.5% for females was used.

The mortality assumptions used for the 31 March 2020 valuation result in the following life expectancies:

	Years
Life expectancy for a male aged 65 now	21.4
Life expectancy at 65 for a male aged 45 now	23.0
Life expectancy for a female aged 65 now	24.1
Life expectancy at 65 for a female aged 45 now	26.2

Pre-retirement Mortality

The following mortality tables (together with any appropriate weightings) have been adopted for mortality rates in the period up to retirement.

	31 March 2020	31 March 2017
Base Table	DxL08 tables with adjustments of 80% (male) 50% (female) to reflect the Fund's membership profile	DxL08 tables with adjustments of 80% (male) 50% (female) to reflect the Fund's membership profile
Allowance for Future Improvements	CMI_2015 [1.5%]	CMI_2015 [1.5%]

Commutation

It has been assumed that, on average, 50% of retiring members will take the maximum tax-free cash available at retirement and 50% will take a 3/80ths cash sum (the standard for pre April 2008 service). Members have the option to commute part of their pension at retirement in return for a lump sum at a rate of £12 cash for each £1 per annum of pension given up.

Retirement lump sums are less costly for the Fund to provide than the alternative pension, as members receive only £12 of each £1 p.a. of pension given up. If members take the cash sum option at a higher rate than has been assumed then this will normally lead to an improvement in the funding level.

Early retirement

Some members are entitled to receive their benefits (or part of their benefits) unreduced from an age prior to the Fund's normal pension age under the "Rule of 85" provisions of the Regulations. This age will be at some point between ages 60 and 65, depending on the length of a member's pensionable service.

If members take early retirement to a greater extent than has been assumed then this will typically lead to a worsening of the funding level. This is because many members are able to take substantial parts of their benefits from age 60 without them being reduced for early payment.

The calculations in respect of the relevant service to which these terms apply (basically pre April 2008 service but with transitional protections for certain members) allow for members to retire at this age.

For post April 2008 service (other than protected service) the situation is different since the "Rule of 85" has been removed (and for post December 2006 service for new entrants to the Scheme from that date). For this service we have assumed the earliest age at which unreduced benefits become an entitlement is 65, except for those members who have protected status under the transitional provisions.

For post April 2015 service, early retirement factors are applied where the retirement age described above is below the member's eligible retirement age for unreduced benefits for post April 2015 service. Factors are in line with the standard scheme factors produced by the Government Actuary's Department.
No allowance has been made for non-ill health early retirements prior to the ages specified above. Additional capital contributions will be paid by employers in respect of the cost of these retirements.

However, for those members who are entitled to receive their accrued benefits (or part of those benefits) prior to the retirement age described above and who are over this age but under 65, a proportion of the active membership is assumed to retire in normal health prior to age 65, as set out below:

	% retiring per annum	**% retiring per annum**
Age	Males	Females
60	10	20
61	8	15
62	8	15
63	8	15
64	8	15
65	100	100

The appropriate early retirement factors applied to the relevant tranche of benefits are in line with the Government Actuary's Department (GAD) guidance.

Ill health retirement

A small proportion of the active membership has been assumed to retire owing to ill health. As an example of the rates assumed, the following is an extract from the decrement table used:

The level of ill-health retirement benefit provided for a member falls into one of two "tiers", depending on whether and when the member might be expected to resume gainful employment. Tier 1, for example, is on the basis that the member is unlikely to be able to do so before Normal Pension Age. Full details are set out in the LGPS (Scotland) Regulations and associated guidance.

	% retiring per annum	% retiring per annum
Age	Males	Females
35	0.03	0.03
45	0.09	0.09
55	0.41	0.36

The proportion of ill health early retirements falling into each tier category, split by males and females, has been assumed to be as set out below:

Tier 1	Tier 2
86%	14%

Withdrawal

This assumption relates to those members who leave the scheme with an entitlement to a deferred pension or transfer value. It has been assumed that active members will leave the Scheme at the following sample rates:

	% leaving per annum	% leaving per annum
Age	Males	Females
25	20.25	22.38
35	5.09	6.27
45	2.54	3.89

In relation to pre 2015 benefits, deferred benefits tend to be less costly for the Fund to provide than if the member had remained in the Fund until retirement. If the number of members leaving the Fund is greater than expected then this will typically lead to a slight improvement in the funding level.

Partners' and Dependants' Proportions

It has been assumed that the proportions of members below will
on death give rise to a dependant's pension (spouse's and partner's), and that spouses/partners of female (male) members are three years older (younger), on average than the member.

	% spouse/partner	% spouse/partner
Age	Males	Females
25	43	46
35	69	60
45	72	60
55	74	60
65	76	55

If more members than assumed have partners then this will lead to an increase in the number of dependants pensions coming into payment over and above that expected. This would lead to a worsening of the funding level.

Assumptions used to calculate the Primary Contribution Rate

The cost of future accrual (the Primary Contribution Rate) has been calculated using the same actuarial assumptions as used to calculate the solvency funding target and recovery plan as set out above except that the financial assumptions adopted are as described below.

The financial assumptions for assessing the future service contribution rate should take account of the fact that contributions will be invested in market conditions applying at future dates, which are unknown at the effective date of the valuation, and which are not directly linked to market conditions at the valuation date.

The financial assumptions in relation to future service (i.e. the Primary Contribution Rate) are not specifically linked to investment conditions as at the valuation date itself, and are based on an overall assumed real return (i.e. return in excess of price inflation) of 1.50% per annum. This represents a reduction of 0.25% per annum compared to the 2017 valuation, which increases the estimated cost of providing LGPS benefits. With a long term average assumption for price inflation of 2.1% per annum, this gives rise to an overall discount rate of 3.60% p.a. (the corresponding discount rate at the 2017 actuarial valuation was 4.15% p.a.).

Nevertheless, it is instructive to consider the assumption against the long term real returns (i.e. returns above CPI) which the Fund's investment strategy can be expected to deliver based on the current market outlook. At this actuarial valuation the real discount rate used was 1.50% p.a., which is broadly the 55th percentile return from our analysis. At the previous valuation the real discount rate used was 1.75% p.a., which at the time was the 70th percentile return from similar analysis at the time.

Appendix B

Summary membership data

The membership data is summarised in the table, with figures at the previous valuation shown for comparison.

Data in relation to members of the Fund were supplied by the Fund's administrator on behalf of the Administering Authority. The accuracy of the data provided has been relied on. While reasonableness checks on the data have been carried out, they do not guarantee the completeness or the accuracy of the data. Consequently, Mercer does not accept any liability in respect of its advice where it has relied on data that is incomplete or inaccurate.

	31 March 2020	31 March 2017
Active members		
Number	25,960	25,260
Total Pensionable Salaries (£000s p.a.)	504,847	471,747
Average Pensionable Salary (£ p.a.)	19,447	18,676
Average age (pension weighted)	51.2	51.1
Deferred pensioners		
Number	22,159	20,433
Total deferred pensions revalued to valuation date (£000s p.a.)	38,358	33,652
Average deferred pension (£ p.a.)	1,731	1,647
Average age (pension weighted)	49.8	49.2
Pensioners (including dependants)		
Number	22,092	19,159
Total pensions payable (£000s p.a.) Gross of pre 1986 recharges	110,413	89,185
Average pension (£ p.a.)	4,998	4,655
Average age (pension weighted)	70.7	70.4

Appendix C

Assets

The market value of the Fund's assets was £4,367,000,000 on the valuation date.

The Administering Authority's investment strategy is to proportion the Fund's assets by asset class as shown in the table below. The actual distribution of assets will vary over time due to changes in financial markets. The table also shows the distribution of assets at the valuation date.

	Investment strategy	Actual market value of assets at 31 March 2020	
	%	£000s	%
UK equities	45.0%	982,472	22.5%
Overseas equities		1,218,265	27.9%
Private equity	5.0%	266,359	6.1%
Diversified Growth	7.5%	310,024	7.1%
Infrastructure	10.0%	183,395	4.2%
Property	10.0%	406,088	9.3%
Fixed interest gilts	0.0%	113,530	2.6%
Index-linked gilts	5.0%	205,227	4.7%
Corporate bonds	15.0%	554,551	12.7%
Cash	2.5%	126,631	2.9%
Total	100%	4,366,542	100%

The Administering Authority also holds additional voluntary contributions (AVCs) which are separately invested. These assets have been excluded from the market value shown as they exactly match the value of the benefits they cover.

The details of the assets at the valuation date and the financial transactions during the inter-valuation period have been obtained from the audited accounts for the Fund.

Appendix D
Scheme Benefits

The benefits valued within our calculations are those in force at the effective date of the valuation. Full details of these can be found in the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended). The principal details are as follows:

The Local Government Pension Scheme (Scotland) Regulations 2018 (https://www.legislation.gov.uk/ssi/2018/141/contents)

The Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014 (https://www.legislation.gov.uk/ssi/2014/233/contents/made)

Directions made by the Treasury under Section 59A of the Social Security Pensions Act 1975 (https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/761639/Treasury_Direction_under_section_59A_Social_Security_Pensions_Act_1975.pdf) and recent consultation on future treatment (https://www.gov.uk/government/consultations/public-service-pensions-guaranteed-minimum-pension-indexation-consultation). We have also assumed that that the directions will ultimately be extended to require the LGPS to become responsible for increases to GMPs for **all** members reaching State Pension Age after 5 April 2016.

The Fund is also responsible for paying and, where appropriate, recharging to employers the benefits arising from the award of compensatory added years (CAY) of service on premature retirement. Unless these CAY benefits have been converted into "funded" benefits, they are normally recharged to the relevant employer (together with associated pension increases), and so are excluded from the valuation.

The benefits that will emerge from money purchase AVCs paid by members, and SCAVCs paid by employers, and the corresponding invested assets in respect of these AVCs and SCAVCs, have been excluded from the valuation.

UK and European law requires pension schemes to provide equal benefits to men and women in respect of service after 17 May 1990 (the date of the "Barber" judgment) and this includes providing equal benefits accrued from that date to reflect the differences in GMPs. Following the Lloyds Bank case in 2018, HM Treasury has issued a consultation on equalising and indexation of GMPs in all the public service pension schemes, including the LGPS, and discussions are ongoing about the extent of any inequalities and how these might be addressed.

The valuation makes no allowance for removal of these inequalities. It is consequently possible that additional funding will be required for equalisation once the law has been clarified. It is recommended that the Administering Authority seek further legal advice if it is concerned about this issue.

The McCloud Judgment

The McCloud judgment in the LGPS refers to the legal decisions (initially by the Employment Appeal Tribunal and then ratified by the Court of Appeal) in the Sargeant/McCloud cases for the Fire and Judiciary pension arrangements. The Court ruled that transitional protections afforded to older members when these schemes were amended constituted unlawful age discrimination. Remedial action, in the form of benefit changes for these schemes, will therefore be required.

Although the above cases did not relate directly to the LGPS, the LGPS also put in place protections for older members as part of the reforms which came into effect from 2015. For the LGPS these took the form of an underpin, where older members would get the better of the benefits payable under the new and old schemes. The UK Government set out a proposed remedy in a consultation in July 2020, which broadly would ensure that all members who were in the LGPS before 31 March 2012 would be granted the statutory underpin protection for all service up to 31 March 2022.

As advised by the SPPA and following discussions with the Administering Authority, in order to consider a reasonable provision for the potential costs in employer contributions we have valued the cost of McCloud to be the estimated cost of providing the underpin set out above to all members. More specifically we have agreed with the Administering Authority to:

- Estimate the underpin benefits for members for service after 31 March 2015 (when the new scheme took effect) who joined the Fund before 2012.
- Compare this to the actual post 31 March 2015 benefits.
- Calculate the cost for each member as the value of the underpin benefits less the value of the actual benefits (ignoring members where the value of the actual benefits is higher).
- Sum these costs across all members to give the impact of the underpin for each employer.

We have calculated this cost across all benefits (including deferred benefits for active members who are assumed to leave the scheme before retirement in the future).

Further detail on the proposed remedy can be found in the below consultation document:

https://www.lgpslibrary.org/assets/cons/lgpsscot/20200731CD.pdf

Appendix E

Analysis of Membership Experience

The analysis below compares the actual experience over the 3 year period with the assumptions used for the 2020 valuation.

	Actual	Expected	%
Ill Health Retirements	218	234	93
Withdrawals	6,090	3,731	163
Pensioner Deaths (lives)	1,790	1,398	128
Pensioner Deaths (£000 p.a. of pension)	6,213	5,666	110

Note that actual withdrawals can include members moving to another LGPS Fund, bulk transfers and also transfers under the special transfer club terms.

Appendix F

Rates and Adjustments Certificate issued in accordance with Regulation 60

Name of fund	North East Scotland Pension Fund

Primary Contribution Rate

I hereby certify that, in my opinion, the primary rate of the employers' contribution for the whole Fund for each of the three years beginning 1 April 2021 is 21.7% of pensionable pay.

The primary rate of contribution for each employer for the three year period beginning 1 April 2021 is set out in the attached schedule.

Secondary Contribution Rate

I hereby certify that, in my opinion, the secondary rate of the employer's contribution for the whole Fund for each of the three years beginning 1 April 2021 is as follows:

2021/22 -2.5% of pensionable pay

2022/23 -2.5% of pensionable pay

2023/24 -2.5% of pensionable pay

The secondary rate of contribution for each employer for each of the three years beginning 1 April 2021 is set out in the attached schedule. The above secondary rates, and the secondary rates for each employer, include a provision for the costs of the McCloud judgment as set out in the notes to Appendix G.

Contribution amounts payable

The total contribution payable for each employer is the total of the primary and secondary rates as detailed in the attached schedule. Contributions will be paid monthly in arrears with each payment normally being due by the 19th of the following month (or the 22nd if paid electronically) or at intervals agreed with the Administering Authority unless otherwise noted in the schedule.

Further adjustments

A further individual adjustment shall be applied in respect of each non-ill health early retirement occurring in the period of three years covered by this certificate. This further individual adjustment will be calculated in accordance with methods agreed from time to time between the Fund's Actuary and the Administering Authority.

The contributions set out in the attached schedule represent the minimum contribution which may be paid by each employer in total over the 3 years covered by the certificate. Additional contributions or a different pattern of contributions may be paid if requested by the employer concerned at the sole discretion of the Administering Authority as agreed with the Actuary. The total contributions payable by each employer will be subject to a minimum of nil%.

The individual employer contributions may be varied as agreed by the Actuary and Administering Authority to reflect any changes in contribution requirements as a result of the McCloud judgment remedy as set out in this report and/or any benefit costs being insured with a third party or parties including where the third party or parties participate in the Fund.

In cases where an element of an existing Scheme employer's surplus or deficit is transferred to a new employer on its inception, the Scheme employer's secondary contributions, as shown on the schedule to this Certificate in Appendix G, may be reallocated between the Scheme employer and the new employer to reflect this, on the advice of the Actuary and as agreed with the Administering Authority so that the total payments remain the same overall.

The Administering Authority and employer with advice from the Fund's Actuary can agree that contributions payable under this certificate can be sourced under an alternative financing arrangement which provides the Fund with equivalent cash contributions.

Regulation 60(8)

No allowance for non-ill health early retirements has been made in determining the results of the valuation, on the basis that the costs arising will be met by additional contributions. Allowance for ill health retirements has been included in each employer's contribution rate, on the basis of the method and assumptions set out in the report.

Signature:		
Name:	Paul Middleman	Laura Evans
Qualification:	Fellow of the Institute and Faculty of Actuaries	Fellow of the Institute and Faculty of Actuaries
Date of signing:	31 March 2021	

Appendix G

Schedule to the Rates and Adjustments Certificate dated 31 March 2021

Employer	Notes	Primary rate 2021/22 to 2023/24	Secondary rates			Total Contribution rates		
			2021/22	2022/23	2023/24	2021/22	2022/23	2023/24
Scheme Employers								
Aberdeen City Council	6	21.0%	-3.1%	-3.1%	-3.1%	17.9%	17.9%	17.9%
Aberdeenshire Council	6	22.0%	-2.7%	-2.7%	-2.7%	19.3%	19.3%	19.3%
The Moray Council	6	22.3%	-3.0%	-3.0%	-3.0%	19.3%	19.3%	19.3%
Grampian Valuation Joint Board		21.9%	-2.6%	-2.6%	-2.6%	19.3%	19.3%	19.3%
Moray College		21.9%	0.8%	1.3%	1.5%	22.7%	23.2%	23.4%
NESTRANS		18.5%	6.4%	6.4%	6.4%	24.9%	24.9%	24.9%

Employer	Notes	Primary rate 2021/22 to 2023/24	Secondary rates			Total Contribution rates		
			2021/22	2022/23	2023/24	2021/22	2022/23	2023/24
North East Scotland College		21.8%	1.6%	3.0%	3.0%	23.4%	24.8%	24.8%
Scottish Fire and Rescue Service		21.3%	0.1%	0.1%	0.1%	21.4%	21.4%	21.4%
Scottish Police Authority (combined)		21.5%	0.8%	0.8%	0.8%	22.3%	22.3%	22.3%
Scottish Water		21.6%	-3.4%	-3.4%	-3.4%	18.2%	18.2%	18.2%
Community Admission Bodies								
Aberdeen Cyrenians		21.7%	-1.3%	-1.3%	-1.3%	20.4%	20.4%	20.4%
Aberdeen Endowments Trust		23.2%	2.2%	2.2%	2.2%	25.4%	25.4%	25.4%
Aberdeen Foyer		24.3%	-4.3%	-4.3%	-4.3%	20.0%	20.0%	20.0%
Aberdeen Heat and Power		23.1%	0.2%	0.2%	0.2%	23.3%	23.3%	23.3%
Aberdeen Performing Arts		22.3%	-2.8%	-2.8%	-2.8%	19.5%	19.5%	19.5%
Aberdeen Sports Village		23.8%	1.8%	1.8%	1.8%	25.6%	25.6%	25.6%

Employer	Notes	Primary rate 2021/22 to 2023/24	Secondary rates			Total Contribution rates		
			2021/22	2022/23	2023/24	2021/22	2022/23	2023/24
Aberlour Child Care Trust		22.5%	-1.0%	-1.0%	-1.0%	21.5%	21.5%	21.5%
Archway		26.1%	0.0%	0.0%	0.0%	26.1%	26.1%	26.1%
Fersands and Fountain		23.4%	1.7%	1.7%	1.7%	25.1%	25.1%	25.1%
Fraserburgh Harbour		21.9%	-1.1%	-1.1%	-1.1%	20.8%	20.8%	20.8%
Home Start Aberdeen		29.3%	36.5%	36.5%	36.5%	65.8%	65.8%	65.8%
Homestart NEA		26.2%	0.0%	0.0%	0.0%	26.2%	26.2%	26.2%
Inspire		23.2%	-1.3%	-1.3%	-1.3%	21.9%	21.9%	21.9%
Mental Health Aberdeen		25.9%	-2.4%	-2.4%	-2.4%	23.5%	23.5%	23.5%
North East Sensory Services		24.2%	£30,000	£31,080	£32,200	24.2% plus £30,000	24.2% plus £31,080	24.2% plus £32,200
Osprey Housing		23.2%	-0.6%	-0.6%	-0.6%	22.6%	22.6%	22.6%
Outdoor Access Trust Scotland		22.7%	-0.7%	-0.7%	-0.7%	22.0%	22.0%	22.0%

Employer	Notes	Primary rate 2021/22 to 2023/24	Secondary rates			Total Contribution rates		
			2021/22	2022/23	2023/24	2021/22	2022/23	2023/24
Pathways		20.8%	0.4%	0.4%	0.4%	21.2%	21.2%	21.2%
Peterhead Port Authority		22.0%	1.6%	1.6%	1.6%	23.6%	23.6%	23.6%
Printfield Community Project		26.0%	-0.2%	-0.2%	-0.2%	25.8%	25.8%	25.8%
Robert Gordon's College		24.1%	1.2%	2.7%	4.3%	25.3%	26.8%	28.4%
Sanctuary Scotland		23.7%	0.0%	0.0%	0.0%	23.7%	23.7%	23.7%
Save Cash and Reduce Fuel		23.6%	-3.5%	-3.5%	-3.5%	20.1%	20.1%	20.1%
Scotland's Lighthouse Museum		21.4%	-1.2%	-1.2%	-1.2%	20.2%	20.2%	20.2%
Sport Aberdeen		22.4%	-7.2%	-7.2%	-7.2%	15.2%	15.2%	15.2%
St Machar Parent Support Project		25.0%	-0.3%	1.0%	2.1%	24.7%	26.0%	27.1%
Station House Media Unit		21.0%	-9.1%	-9.1%	-9.1%	11.9%	11.9%	11.9%
The Robert Gordon University		20.0%	0.3%	0.3%	0.3%	20.3%	20.3%	20.3%

Employer	Notes	Primary rate 2021/22 to 2023/24	Secondary rates			Total Contribution rates		
			2021/22	2022/23	2023/24	2021/22	2022/23	2023/24
Transferee Admission Bodies								
Alcohol and Drugs Action		24.2%	-4.6%	-4.6%	-4.6%	19.6%	19.6%	19.6%
Bon Accord Care and Bon Accord Support (combined)		21.8%	-2.5%	-2.5%	-2.5%	19.3%	19.3%	19.3%
Citymoves Dance Agency		26.0%	1.4%	1.4%	1.4%	27.4%	27.4%	27.4%
Forth and Oban		27.0%	-2.0%	-2.0%	-2.0%	25.0%	25.0%	25.0%
Forth And Oban (Shire)		26.0%	-6.9%	-6.9%	-6.9%	19.1%	19.1%	19.1%
idVerde		23.5%	-6.7%	-6.7%	-6.7%	16.8%	16.8%	16.8%
Robertsons City		26.4%	-3.9%	-3.9%	-3.9%	22.5%	22.5%	22.5%
Robertsons Shire		23.9%	-0.3%	-0.3%	-0.3%	23.6%	23.6%	23.6%
Xerox UK Ltd		23.8%	-8.5%	-8.5%	-8.5%	15.3%	15.3%	15.3%

The following employers exited the Fund during 2020/21. Termination assessments will be required and any additional contributions required will be notified separately:

Employer
Inspire Catering

Important notes to the Certificate:

1. The percentages shown are percentages of pensionable pay and apply to all members, including those who are members under the 50:50 option under the LGPS.

2. With the agreement of the Administering Authority employers may also opt to pay any other element of their employer contributions in advance instead of monthly amounts, with either all three years being paid in April 2021 or payment being made in the April of the year in question. The projected cash amounts payable will be reduced in return for this early payment as follows:

   - Payments made in the April of the certified year will be reduced by 1.63% (i.e. the above amounts will be multiplied by 0.9837)
   - 2022/23 payments made in April 2021 will be reduced by 4.82% (i.e. the above amounts will be multiplied by 0.9518)
   - 2023/24 payments made in April 2021 will be reduced by 7.90% (i.e. the above amounts will be multiplied by 0.9210)

3. Where % contributions are being paid in advance, for these cases the employer will need to estimate in advance the pensionable pay for the entire period (subject to an agreed adjustment with the Administering Authority) and a balancing adjustment to reflect the actual pensionable pay over the period would be made at the end of the period (no later than 30th April as appropriate following the year-end). Consideration will be required for employers in surplus as at 31 March 2020, where any surplus offset would be made up front before any reduction for early payment is applied. Further information on the policy for prepayments can be provided by the Fund upon request.

4. Where the secondary rate is a deduction to the primary rate due to an employer being in surplus, the total annual contributions payable by each employer will be subject to a minimum of nil % i.e. no monies can be refunded to an employer whilst they participate in the Fund.

5. The above primary and secondary contributions include provision for the estimated effect of the McCloud judgment based on the proposed remedy set out in the 2020 Government consultation. Once the final remedy for McCloud is known, the position will be reviewed.

6. Separate payments will be made from the North East Scotland Pension Fund to the Aberdeen City Council Transport Fund in relation to pension increases payable to retired members relating to benefits accrued prior to 26 October 1986, unless capitalised via a one off payment as agreed with the Administering Authority of both Funds and First Aberdeen Limited which results in the ceasing of the arrangement. Any required recharge amounts will be calculated by the Fund separately where appropriate.

Appendix H
Glossary

Actuarial Valuation: an investigation by an actuary into the ability of the Fund to meet its liabilities. For the LGPS the Fund Actuary will assess the funding level of each participating employer and agree contribution rates with the administering authority to fund the cost of new benefits and make good any existing deficits as set out in the separate Funding Strategy Statement.

Administering Authority: the council with a statutory responsibility for running the Fund and that is responsible for all aspects of its management and operation.

Best Estimate Assumption: an assumption where the outcome has a 50/50 chance of being achieved.

Bonds: loans made to an issuer (often a government or a company) which undertakes to repay the loan at an agreed later date. The term refers generically to corporate bonds or government bonds (gilts).

Career Average Revalued Earnings Scheme (CARE): with effect from 1 April 2015, benefits accrued by members in the LGPS take the form of CARE benefits. Every year members will accrue a pension benefit equivalent to 1/49th of their pensionable pay in that year. Each annual pension accrued receives inflationary increases (in line with the annual change in the Consumer Prices Index) over the period to retirement.

CPI: acronym standing for "Consumer Prices Index". CPI is a measure of inflation with a basket of goods that is assessed on an annual basis. The reference goods and services currently differs from those of RPI. These goods are expected to provide lower, less volatile inflation increases. Pension increases in the LGPS are linked to the annual change in CPI.

CPIH: An alternative measure of CPI which includes owner occupiers' housing costs and Council Tax (which are excluded from CPI).

Deficit: the extent to which the value of the Fund's past service liabilities exceeds the value of the Fund's assets.

Discount Rate: the rate of interest used to convert a cash amount e.g. future benefit payments occurring in the future to a present value.

Employer Covenant: the degree to which an employer participating in an occupational pension scheme is willing and able to meet the funding requirements of the scheme.

Employer's Future Service Contribution Rate: the contribution rate payable by an employer, expressed as a % of pensionable pay, as being sufficient to meet the cost of new benefits being accrued by active members in the future. The cost will be net of employee contributions and will include an allowance for the expected level of administrative expenses. It is normally the same as an employer's Primary Contribution Rate under the Regulations.

Employer's Primary Contribution Rate: the contribution rate required to meet the cost of the future accrual of benefits including ancillary, death in service and ill health benefits together with administration costs. It is expressed as a percentage of pensionable pay, ignoring any past service surplus or deficit, but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer's covenant. The Primary Contribution Rate for the whole Fund is the weighted average (by payroll) of the individual employers' Primary Contribution Rates.

Employer's Secondary Contribution Rate: an adjustment to the Primary Rate to reflect any past service deficit or surplus, to arrive at the rate each employer is required to pay. The Secondary Rate may be expressed as a percentage adjustment to the Primary Rate, and/or a cash adjustment in each of the three years beginning 1 April in the year following that in which the valuation date falls. The Secondary Rate is specified in the Rates and Adjustments Certificate. For any employer, the rate they are actually required to pay is the sum of the Primary and Secondary Rates. Secondary Rates for the whole fund in each of the three years shall also be disclosed. These will be calculated as the weighted average based on the whole fund payroll in respect of percentage rates and as a total amount in respect of cash adjustments.

Equities: shares in a company which are bought and sold on a stock exchange.

Funding or solvency Level: the ratio of the value of the Fund's assets and the value of the Fund's liabilities expressed as a percentage.

Funding Strategy Statement (FSS): This is a key governance document that outlines how the Administering Authority will manage employer's contributions to the Fund.

Guaranteed Minimum Pension (GMP): This part of a member's pension which was earned between 6 April 1978 and 5 April 1997 and which replaces part of that member's State Scheme benefits in respect of that period.

Investment Strategy: the long-term distribution of assets among various asset classes that takes into account the Funds objectives and attitude to risk.

Liabilities: the actuarially calculated present value of all benefit entitlements i.e. Fund cashflows of all members of the Fund, built up to date or in the future. The liabilities in relation to the benefit entitlements earned up to the valuation date are compared with the present market value of Fund assets to derive the deficit and funding/solvency level. Liabilities can be assessed on different set of actuarial assumptions depending on the purpose of the valuation.

McCloud Judgment: This refers to the linked legal cases of Sargeant and McCloud, and which found that the transitional protections (which were afforded to older members when the public service pension schemes were reformed in 2014/15) constituted unlawful age discrimination.

Past Service Liabilities: this is the present value of the benefits accrued by members up to the valuation date. It is assessed based on a set of assumptions agreed between the Administering Authority and the Actuary.

Percentile: A method of ranking a series of outcomes. For example, a 10th percentile outcome means that only 10% of results would be expected to be as good as or better than the 10th percentile and 90% of results would be expected to be worse.

Prepayment: the payment by employers of contributions to the Fund earlier than that certified by the Actuary. The amount paid will be reduced compared to the certified amount to reflect the early payment.

Present Value: the value of projected benefit payments, discounted back to the valuation date.

Prudent Assumption: an assumption where the outcome has a greater than 50/50 chance of being achieved i.e. the outcome is more likely to be overstated than understated. Legislation and guidance requires the assumptions adopted for an actuarial valuation overall to be prudent.

Real Return or Real Discount Rate: a rate of return or discount rate net of CPI inflation.

Recovery Plan: a strategy by which an employer will make up a funding surplus/deficit over a specified period of time ("the spread period"), as set out in the Funding Strategy Statement.

SAB Funding Basis or SAB Basis: a set of actuarial assumptions determined by the LGPS Scheme Advisory Board (SAB). Its purposes are to set out the funding position on a standardised approach so that comparisons can be made with other LGPS Funds, and to assist with the "Section 13 review" as carried out by the Government Actuary's Department. As an example, the real discount rate over and above CPI used in the SAB Basis as at 31 March 2020 was 2.4% p.a., so it can be substantially different from the actuarial assumptions used to calculated the Fund's solvency funding position and contribution outcomes for employers.

Solvency/Funding Level: the ratio of the value of the Fund's assets and the value of the Fund's liabilities expressed as a percentage.

Solvency Funding Target: an assessment of the present value of benefits to be paid in the future. The desired funding target is to achieve a solvency level of a 100% i.e. assets equal to the past service liabilities assessed on the ongoing concern basis.

Spread Period: a strategy by which the Fund will remove a funding surplus via contribution adjustments over a specified period of time ("the spread period"), as set out in the Funding Strategy Statement.

50/50 Scheme: in the LGPS, active members are given the option of accruing a lower benefit in the 50/50 Scheme, in return for paying a lower level of contribution.

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Aberdeen City Council Transport Fund

Funding Strategy Statement

March 2021

Aberdeen City Council

This Funding Strategy Statement has been prepared by Aberdeen City Council (the Administering Authority) to set out the funding strategy for the North East Scotland Pension Fund (the “Fund”), in accordance with Regulation 56 of the Local Government Pension Scheme (Scotland) Regulations 2014 (as amended) and guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA)

welcome to brighter

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Appendices

Executive Summary

Ensuring that the Aberdeen City Council Transport Fund (the "Fund") has sufficient assets to meet its pension liabilities in the long term is the fiduciary responsibility of the Administering Authority (Aberdeen City Council). The Funding Strategy adopted by the Aberdeen City Council Transport Fund will therefore be critical in achieving this.

The purpose of this Funding Strategy Statement ("FSS") is to set out a clear and transparent funding strategy that will identify how each Fund employer's pension liabilities are to be met going forward.

The details contained in this Funding Strategy Statement will have a financial and operational impact on all participating employers in the Aberdeen City Council Transport Fund (i.e. First Aberdeen Limited and First Glasgow Limited).

It is imperative therefore that the employers are aware of the details contained in this statement.

Given this, and in accordance with governing legislation, all interested parties connected with the Aberdeen City Council Transport Fund have been consulted and given opportunity to comment prior to this Funding Strategy Statement being finalised and adopted. This statement takes into consideration all comments and feedback received.

THE FUND'S OBJECTIVE

The Administering Authority's long term objective is for the Fund to achieve and maintain a 100% solvency level over a reasonable time period and then maintain sufficient assets in order for it to pay all benefits arising as they fall due.

The general principle adopted by the Fund is that the assumptions used, taken as a whole, will be chosen sufficiently prudently for pensions already in payment to continue to be paid, and to reflect the commitments that will arise from members' accrued pension rights.

The funding strategy set out in this document has been developed alongside the Fund's investment strategy on an integrated basis taking into account the overall financial and demographic risks inherent in the Fund.

The funding strategy includes appropriate margins to allow for the possibility of adverse events (e.g. material reduction in investment returns, economic downturn and higher inflation outlook) leading to a worsening of the funding position which could lead to volatility of contribution rates at future valuations if these margins were not included. This prudence is required by the Regulations and guidance issued by professional bodies and Government agencies to assist the Fund in meeting its primary solvency objective. Individual employer results will also have regard to their covenant strength.

LONG TERM COST EFFICIENCY

Each employers' contributions are set at such a level to achieve full solvency in a reasonable timeframe. Solvency is defined as a level where the Fund's liabilities i.e. benefit payments can be reasonably met as they arise.

Employer contributions are also set in order to achieve long term cost efficiency. Long term cost-efficiency implies that contributions must not be set at a level that is likely to give rise to additional costs in the future. The funding parameters and assumptions must have regard to this requirement which means a level of prudence is needed. Furthermore, the FSS must have regard to the desirability of maintaining as nearly constant a primary rate of contribution as possible.

When formulating the funding strategy, the Administering Authority has taken into account these key objectives and also considered the implications of the requirements under Section 13(4)(c) of the Public Service Pensions Act 2013. As part of these requirements the Government Actuary's Department (GAD) must, following an actuarial valuation, report on whether the rate of employer contributions to the Fund is set at an appropriate level to ensure its "solvency" and "long term cost efficiency" of the Local Government Pension Scheme (Scotland) (the "LGPS") so far as relating to the Fund.

MERGER AND PENSIONER BUY-IN

The sole employer previously in the Strathclyde Pension Fund - No3. Fund, First Glasgow Limited, was transferred to the Aberdeen City Council Transport Fund and became an employer within the Fund in 2019.

The Fund subsequently completed a c£230m pensioner buy-in transaction with Rothesay Life in November 2020. This transaction insures the pension payments of 1,371 pensioners across both employers through a pensioner-only buy-in.

This was a significant de-risking step for Fund and its employers by:

- hedging longevity risk
- closely matching cashflows for pensioners' liabilities
- reducing credit risk
- reducing reliance on the sponsors

Overall the transaction places the Fund and the tax-payer in a strong position for the future.

SURPLUS SPREAD PERIOD AND CONTRIBUTIONS

As the solvency level of the Fund is above 100% at the valuation date i.e. the assets of the Fund are greater than the liabilities, the surplus can be used to reduce ongoing contribution requirements. This surplus will be removed at a rate which depends on the circumstances of each employer. This will depend on the financial covenant and if the employer may potentially exit the Fund in the near future. Any contributions are subject to a minimum of zero.

Having regard to the overall risk profile of the residual Fund following the buy-in with Rothesay Life, the employers' covenant and the investment strategy, the Administering Authority have agreed that the surplus can be used to offset the primary contribution requirements such that the employer contributions will be nil for the period 1 April 2021 – 31 March 2024.

It is the Fund's objective that any future funding deficits that may arise are eliminated as quickly as the participating employers can reasonably afford given other competing cost pressures and based on the Administering Authority's view of the employers' covenant and risk to the Fund.

The objective is to maintain at least 100% solvency, and this will be periodically reviewed. Full details are set out in this FSS.

The government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. A consultation was issued in July 2020, which confirms that the remedy will have the effect of removing the current age criteria applied to the underpin implemented in 2015 for the LGPS, which would then apply to all members who were active as at 1 April 2012. The relevant estimated costs of the remedy have been quantified and notified to the employers on this basis. The final funding position and certified contributions for each employer include the estimated costs of the McCloud remedy.

ACTUARIAL ASSUMPTIONS

The actuarial assumptions used for assessing the funding position of the Fund and the employer, the “Primary” contribution rate, and any contribution variations due to underlying surpluses or deficits (i.e. the “Secondary” rate) are set out in an Appendix to this FSS.

The discount rate has been derived based on the current objectives of the Administering Authority based on the long term strategy set out in its Statement of Investment Principles (SIP). When assessing the appropriate prudent discount rate, consideration has been given to the level of expected asset returns based on the assets held but ultimately it has been set in relation to the long term “self-sufficiency” target based on a low risk portfolio of assets. It is proposed at this valuation discount rate for determining the past service liabilities and future service (“Primary”) contribution rates is set equal to the return on a gilt yield appropriate for the profile and duration of the Scheme’s accrued liabilities.

The inflation assumption will be taken to be the investment market’s expectation for RPI inflation as indicated by the difference between yields derived from market instruments, principally conventional and index-linked UK Government gilts as at the valuation date, reflecting the profile and duration of the Fund’s accrued liabilities.

For the purposes of the valuation, we have assumed that the RPI/CPI wedge will be 1% p.a. until 2030 and then 0% p.a. after 2030 to reflect the announcement that the RPI index will be aligned with the CPIH inflation measure from 2030.

Where warranted by an employer’s circumstances, the Administering Authority retains the discretion to apply an adjusted discount rate to reflect the termination assumptions for an employer if it were to exit the Fund to protect the Fund as a whole. Such cases will be determined by the Section 95 Officer and reported to the Committee.

The demographic assumptions are based on the Fund Actuary’s bespoke analysis for both employers in the Fund, also taking into account the experience of the wider LGPS where relevant.

EMPLOYER ASSET SHARES

The Fund is a multi-employer pension scheme that is not formally unitised and so individual employer asset shares are calculated at each actuarial valuation. This means it is necessary to make some approximations in the timing of cashflows and allocation of investment returns when deriving each employer's asset share.

At each review, cashflows into and out of the Fund relating to each employer, any movement of members between employers within the Fund, along with investment return earned on the asset share, are allowed for when calculating asset shares at each valuation. In addition, the asset shares may be restated for changes in data or other policies.

FUND POLICIES

In addition to the information/approaches required by overarching guidance and Regulation, this statement also summarises the Fund's practice and policies in a number of key areas:

1. Covenant assessment and monitoring

An employer's financial covenant underpins its legal obligation and crucially the ability to meet its financial responsibilities to the Fund now and in the future. The strength of covenant to the Fund effectively underwrites the risks to which the Fund is exposed. These risks include underfunding, longevity, investment and market forces.

The strength of employer covenant can be subject to substantial variation over relatively short periods of time and, as such, regular monitoring and assessment is vital to the overall risk management and governance of the Fund. The employers' covenants will be assessed and monitored objectively in a proportionate manner, and an employer's ability to meet its obligations in the short and long term will be considered when determining its funding strategy.

After the valuation, the Fund will continue to monitor the employer covenants in conjunction with the funding position over the inter-valuation period and the employers have agreed to provide periodic information to support that. This will enable the Fund to anticipate and pre-empt any material issues arising and thus adopt a proactive approach in partnership with the employer.

2. Termination policy for employers exiting the Fund

When an employer ceases to participate within the Fund, it becomes an exiting employer under the Regulations. The Fund is then required to obtain an actuarial valuation of that employer's liabilities in respect of the benefits of the exiting employer's current and former employees, along with a termination contribution certificate.

Please see Appendix C for the full policy.

1 Introduction

The Local Government Pension Scheme (Scotland) Regulations 2018 (as amended) (“the 2018 Regulations”) and the Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014 (“the 2014 Transitional Regulations”) (collectively; “the Regulations”) provide the statutory framework from which the Administering Authority is required to prepare a Funding Strategy Statement (FSS). The key requirements for preparing the FSS can be summarised as follows:

- After consultation with all relevant interested parties involved with the Aberdeen City Council Transport Fund (the “Fund”), the Administering Authority will prepare and publish their funding strategy;
- In preparing the FSS, the Administering Authority must have regard to:
  - the guidance issued by CIPFA for this purpose; and
  - the Statement of Investment Principles (SIP) for the Fund published under Regulation 12 of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 (as amended);
- The FSS must be revised and published whenever there is a material change in either the policy set out in the FSS or the SIP.

Benefits

The benefits provided by the Fund are specified in the governing legislation contained in the Regulations referred to above. Benefits payable under the Fund are guaranteed by statute and thereby the pensions promise is secure for members. The FSS addresses the issue of managing the need to fund those benefits over the long term, whilst at the same time facilitating scrutiny and accountability through improved transparency and disclosure.

The Fund is a defined benefit arrangement with principally final salary related benefits earned by contributing members up to 1 April 2015 and Career Averaged Revalued Earnings (“CARE”) benefits earned thereafter. There is also a “50:50 Scheme Option”, where members can elect to accrue 50% of the full scheme benefits in relation to the member only and pay 50% of the normal member contribution.

Employer Contributions

The required levels of employee contributions are specified in the Regulations. Employer contributions are determined in accordance with the Regulations (which require that an actuarial valuation is completed every three years by the actuary, including a rates and adjustments certificate specifying the “primary” and “secondary” rate of the employer’s contribution).

Primary rate

The “Primary rate” for an employer is the contribution rate required to meet the cost of the future accrual of benefits, including ancillary death in service and ill health benefits together with administration costs. It is expressed as a percentage of pensionable pay, plus a £ amount in respect of expected administration expenses, ignoring any past service surplus or deficit, but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer’s covenant.

The Primary rate for the whole Fund is the weighted average (by payroll) of the individual employers’ Primary rates.

Secondary rate

The “Secondary rate” is an adjustment to the Primary rate to arrive at the total rate of contribution the employer is required to pay. The Secondary rate may be expressed as a percentage adjustment to the Primary rate and a cash adjustment in each of the three years beginning 1 April in the year following the actuarial valuation. The Secondary rate is specified in the rates and adjustments certificate.

For any employer, the rate they are actually required to pay is the sum of the Primary and Secondary rates, subject to a minimum of nil.

Secondary rates for the whole Fund in each of the three years shall also be disclosed. These will be the calculated weighted average based on the whole Fund payroll in respect of percentage rates and the total amount in respect of cash adjustments.

2 Purpose of FSS in Policy Terms

Funding is the making of advance provision to meet the cost of accruing benefit promises. Decisions taken regarding the approach to funding will therefore determine the rate or pace at which this advance provision is made. Although the Regulations specify the fundamental principles on which funding contributions should be assessed, implementation of the funding strategy is the responsibility of the Administering Authority, acting on the professional advice provided by the actuary.

The Administering Authority's long term objective is for the Fund to achieve a 100% solvency level over a reasonable time period and then maintain sufficient assets in order for it to pay all benefits arising as they fall due.

The purpose of this Funding Strategy Statement is therefore:

- to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward by taking a prudent longer-term view of funding those liabilities with a view to moving to a self-sufficient position which relies less on the employer covenants
- to establish contributions at a level to "secure the solvency" of the pension fund and the "long term cost efficiency",
- to have regard to the desirability of maintaining as nearly constant a primary rate of contribution as possible.

The intention is for this strategy to be both cohesive and comprehensive for the Fund as a whole, recognising that there will be conflicting objectives which need to be balanced and reconciled.

3

Aims and Purpose of the Fund

The aims of the Fund are to:

- manage employers' liabilities effectively and ensure that sufficient resources are available to meet all liabilities as they fall due
- enable employer contribution rates to be kept at a reasonable and affordable cost to the employer, while achieving and maintaining Fund solvency and long term cost efficiency, which should be assessed in light of the profile of the Fund now and in the future.
- maximise the returns from investments within reasonable risk parameters taking into account the above aims.

The purpose of the Fund is to:

- receive monies in respect of contributions, transfer values and investment income (including income from Rothesay Life in respect of the insured pensioners), and
- pay out monies in respect of Fund benefits, transfer values, exit credits, costs, charges and expenses as defined in the Regulations

4

Responsibilities of the Key Parties

The efficient and effective management of the Fund can only be achieved if all parties exercise their statutory duties and responsibilities conscientiously and diligently. The key parties for the purposes of the FSS are the Administering Authority (and, in particular the Pensions Committee), the employers and the Fund Actuary and details of their roles are set out below. Other parties required to play their part in the fund management process are bankers, custodians, investment managers, auditors and legal, investment and governance advisors, along with the Local Pensions Board created under the Public Service Pensions Act 2013.

Key parties to the FSS

The **Administering Authority** should:

- operate the pension fund
- collect employer and employee contributions, investment income and other amounts due to the pension scheme as stipulated in the Regulations (including payments from Rothesay Life in respect of the buy-in)
- pay from the pension fund the relevant entitlements as stipulated in the Regulations
- invest surplus monies in accordance the Regulations
- ensure that cash is available to meet liabilities as and when they fall due
- take measures as set out in the Regulations to safeguard the fund against the consequences of employer default
- manage the valuation process in consultation with the Fund's actuary
- prepare and maintain an FSS and a SIP, both after proper consultation with interested parties
- monitor all aspects of the Fund's performance and funding, amending the FSS/SIP as necessary, and
- establish, support and monitor a Local Pension Board (LPB) as required by the Public Service Pensions Act 2013, the Regulations and the Pensions Regulator's relevant Code of Practice.

The **Individual Employer** should:

- deduct contributions from employees' pay correctly after determining the appropriate employee contribution rate (in accordance with the Regulations)
- pay all contributions, including their own as determined by the actuary, promptly by the due date

- develop a policy on certain discretions and exercise those discretions as permitted within the regulatory framework
- make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of Fund benefits, early retirement strain
- have regard to the Pensions Regulator's focus on data quality and comply with any requirement set by the Administering Authority in this context
- notify the Administering Authority promptly of any changes to membership which may affect future funding, and
- understand that the quality of the data provided to the Fund will directly impact on the assessment of the liabilities and contributions. In particular, any deficiencies in the data would normally result in the employer paying higher contributions than otherwise would be the case if the data was of high quality.

The **Fund Actuary** should:

- prepare valuations including the setting of employer contribution rates at a level to ensure fund solvency after agreeing assumptions with the Administering Authority and having regard to their FSS and the Regulations
- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters such as pension strain costs, ill health retirement costs etc.
- provide advice and valuations on the termination of admission agreements including in relation to exit credit payments
- provide advice to the Administering Authority on bonds and other forms of security against the financial effect on the Fund of employer default
- assist the Administering Authority in assessing whether employer contributions need to be revised between valuations as required by the Regulations
- advise on funding strategy, the preparation of the FSS and the inter-relationship between the FSS and the SIP, and
- ensure the Administering Authority is aware of any professional guidance or other professional requirements which may be of relevance to the Fund Actuary's role in advising the Fund.

5

Solvency Funding Target

Securing the "solvency" and "long term cost efficiency" is a regulatory requirement. To meet these requirements the Administering Authority's long term funding objective is for the Fund to achieve and then maintain sufficient assets to cover 100% of projected accrued liabilities (the "funding target") assessed on an ongoing past service basis including allowance for projected final pay where appropriate. In the long term, the employer's total contribution rate would ultimately revert to its Primary rate of contribution.

Solvency and Long Term Efficiency

Each employer's contributions are set at such a level to achieve full solvency in a reasonable timeframe. Solvency is defined as a level where the Fund's liabilities i.e. benefit payments can be reasonably met as they arise.

Employer contributions are also set in order to achieve long term cost efficiency. Long term cost-efficiency implies that contributions must not be set at a level that is likely to give rise to additional costs in the future. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the appropriate time.

When formulating the funding strategy the Administering Authority has taken into account these key objectives and also considered the implications of the requirements under Section 13(4)(c) of the Public Service Pensions Act 2013. As part of these requirements the Government Actuary's Department (GAD) must, following an actuarial valuation, report on whether the rate of employer contributions to the Fund is set at an appropriate level to ensure the "solvency" of the pension fund and "long term cost efficiency" of the LGPS so far as relating to the Fund.

Determination of the solvency Funding Target and Recovery Plan

The principal method and assumptions to be used in the calculation of the funding target are set out in **Appendix A.**   The principles underlying the Employer contribution Plans are set out below. This covers the run off of any surplus assets over liabilities where applicable.

Underlying these assumptions are the following two tenets:

- that the Fund is expected to continue for the foreseeable future; and

- favourable investment performance can play a valuable role in achieving adequate funding over the longer term.

This allows the Fund to take a longer term view when assessing the contribution requirements for certain employers.

In considering this the Administering Authority, based on the advice of the Fund Actuary, will consider if this results in a reasonable likelihood that the funding plan will be successful taking into account any changes in funding after the valuation date (including the buy-in secured in November 2020) up to the finalisation of the valuation by 31 March 2021 at the latest.

Employer contributions will be expressed and certified as two separate elements:

  - the **Primary rate**: a percentage of pensionable payroll in respect of the cost of the future accrual of benefits, plus a £ amount in respect of expected administration expenses
  - the **Secondary rate**: a fixed % of pay and/or £ amounts adjusted as appropriate to arrive at the required overall contributions over 2021/24

The total contributions the employer is actually required to pay in any one year is the sum of the Primary and Secondary rates (subject to an overall minimum of zero). Both elements are subject to further review from April 2024 based on the results of the 2023 actuarial valuation.

Spreading of Surplus / recovery of Deficit contributions

It is the Fund's objective that, where a deficit exists, it is eliminated as quickly as the participating employers can reasonably afford based on the Administering Authority's view of the employer's covenant and risk to the Fund.

In the case of a deficit, recovery periods will be set by the Fund on a consistent basis across employers where possible and communicated as part of the discussions with employers. This will determine the minimum contribution requirement and employers will be free to select any shorter deficit recovery period and higher contributions if they wish, including the option of prepaying the deficit contributions in one lump sum either on an annual basis or a one-off payment. This will be reflected in the monetary amount requested via a reduction in overall deficit contributions payable. The Administering Authority does retain ultimate discretion in applying these principles for individual employers on grounds of affordability and covenant strength.

The key principles when considering surplus/deficit spreading are as follows:

- The Fund does not believe it appropriate for contribution reductions to apply compared to the existing funding plan where deficits remain unless there is compelling reason to do so.

- Employers will have the freedom to pay above the minimum contributions if they so wish. Subject to affordability considerations and other factors, a bespoke period may be applied in respect of particular employers where the Administering Authority considers this to be warranted. The average recovery period adopted by all employers will be set out within the Actuary's report. Employers will be notified of their individual deficit recovery period as part of the provision of their individual valuation results.

- Where an employer is in surplus this will be run off over a period determined by the Administering Authority on the advice of the Actuary. This will depend on the nature of employer, allowing for the financial covenant strength and reasonable affordability of contributions. The objective is to maintain stability of total contributions at this and future valuations. Where an employer is expected to exit the Fund then in normal circumstances, the surplus would be spread over the remaining period to exit.

- In determining the actual recovery period to apply for any particular employer, the Administering Authority may take into account some or all of the following factors:
    - The size of the funding shortfall / surplus;
    - The business plans of the employer;
    - The assessment of the financial covenant of the employer, and security of future income streams;
    - Any contingent security available to the Fund or offered by the employer such as guarantor or bond arrangements, charge over assets, etc.

  The objective is to recover any deficit or remove any surplus over a reasonable timeframe, and this will be periodically reviewed.

- As part of the process of agreeing funding plans with individual employers, the Administering Authority will consider the use of contingent assets and other tools such as bonds or guarantees that could assist employing bodies in managing the cost of their liabilities or could provide the Fund with greater security against outstanding liabilities.

- For those bodies identified as having a weaker covenant, the Administering Authority will need to balance the level of risk plus the solvency requirements of the Fund with the sustainability of the organisation when agreeing funding plans.

- Notwithstanding the above principles, the Administering Authority, in consultation with the actuary, has also had to consider whether any exceptional arrangements should apply in particular cases.

Termination Approach

When an employer ceases to participate within the Fund, it becomes an exiting employer under the Regulations. The Fund is then required to obtain an actuarial valuation of that employer's liabilities in respect of the benefits of the exiting employer's current and former employees, along with a termination contribution certificate.

The full termination policy is set out in Appendix C.

Funding for Non-Ill Health Early Retirement Costs

Employers are required to meet all costs of early retirement strain by capital payments into the Fund as determined on the advice of the Actuary.

6

Link to Investment Policy and the Statement of Investment Principles (SIP)

The results of the 2020 valuation show the liabilities to be 114% covered by the current assets as at the valuation date with a surplus of c£37m. During the valuation process, the Fund, employers and its advisors agreed to secure a buy-in policy in respect of the pensioner population of both employers. This buy-in was completed on 19 November 2020 with Rothesay Life. To bring you more up to date, the approximate funding position at 30 November 2020 (i.e. after the buy-in) was a funding level of c111% and a surplus of c£32m.

Other than by purchasing insurance with a bulk annuity provider (as the Fund has done in respect of its pensioner population), it is not possible to construct a portfolio of investments which produces a stream of income exactly matching the expected liability outgo. However, it is possible to construct a portfolio which represents the “minimum risk” investment position which would deliver a very high certainty of returns at or above the return on a gilt yield appropriate for the profile and duration of the Scheme’s accrued liabilities. Such a portfolio would consist of UK Government gilt stocks and other instruments of varying durations. Investment of the Fund’s assets in line with this portfolio would minimise fluctuations in the Fund’s funding position between successive actuarial valuations. It has been agreed at this valuation to set the funding target to be based on such a portfolio of assets i.e. using a discount rate based on the gilt curve over the duration of the liability cashflows.

The post buy-in investment holdings (at February 2021) are:

	INVESTMENT STRATEGY (%)
Index Linked Gilts	70
Cash & Matching Assets	30
Total	**100**

The post buy-in strategy is still being reviewed by the Fund and its advisors and will be discussed with the employers as appropriate. The expected return is covered in the SIP. For the purposes of setting funding strategy however, the Administering Authority believes that it is appropriate to recognise a low risk asset portfolio return only (based on Government bond yields) and let any positive experience emerge.

7 Identification of Risks and Counter-Measures

The funding of defined benefits is by its nature uncertain. Funding of the Fund is based on both financial and demographic assumptions. These assumptions are specified in the actuarial valuation report.

The buy-in policy materially reduces the demographic and financial risks to the Fund and the employers in respect of the insured members.

For the non-insured members, when actual experience is not in line with the assumptions adopted a, surplus or shortfall will emerge at the next actuarial assessment and will require a subsequent contribution adjustment to bring the funding back into line with the target.

The Actuary's formal report includes quantification of the key risks to the funding position allowing for the risk mitigation provided by holding the buy-in policy. Examples of the risks the Fund is expose to are as follows:

Financial

The key financial risks are as follows:-

- Investment markets fail to perform in line with expectations
- Any risk management policies fail to perform in line with expectations
- Market outlook moves at variance with assumptions
- Investment Fund Managers fail to achieve performance targets over the longer term
- Asset re-allocations in volatile markets may lock in past losses
- Pay and price inflation significantly more or less than anticipated
- An employer ceasing to exist without prior notification, resulting in a large exit credit requirement from the Fund impacting on cashflow requirements.
- Default of Insurer (this is heavily mitigated by solvency requirements)

Any increase in employer contribution rates (as a result of these risks) may in turn impact on the service delivery of that employer and their financial position.

In practice, the low risk investment strategy and the prudent discount rate has predominantly mitigated the residual investment risk for the Fund in respect of the non-insured members. The Fund's asset allocation is kept under constant review and the performance of the investment managers is regularly monitored.

Demographic

The key demographic risks are as follows for non-insured benefits:-

- Future changes in life expectancy (longevity) that cannot be predicted with any certainty
- Potential strains from ill health retirements, over and above what is allowed for in the valuation assumptions for employers
- Deteriorating pattern of early retirements (including those granted on the grounds of ill health)
- Unanticipated acceleration of the maturing of the Fund resulting in materially negative cashflows and shortening of liability durations

The buy-in policy is expected to provide protection against demographic risk in respect of the insured benefits for pensioners, although residual risk remains to the extent there is any benefit mismatch between Fund benefits paid out and the insurance policy (for example in the event of retrospective regulatory changes in the future).

Increasing longevity is something which government policies, both national and local, are designed to promote. It does, however, result in a greater liability for pension funds.

Ill health retirements can be costly for employers. Increasingly we are seeing employers mitigate the number of ill health retirements by employing HR / occupational health preventative measures. These measures, in conjunction with ensuring the regulatory procedures in place to ensure that ill-health retirements are properly controlled, can help control exposure to this demographic risk.

Apart from the regulatory procedures in place to ensure that ill-health retirements are properly controlled, **employing bodies should be doing everything in their power to minimise the number of ill-health retirements**.

Early retirements for reasons of redundancy and efficiency do not affect the solvency of the Fund because they are the subject of a direct charge.

With regards to increasing maturity, the Administering Authority regularly monitors the position in terms of cashflow requirements and considers the impact on the investment strategy and liquidity requirements.

Insurance of certain benefits

The contributions for any employer may be varied as agreed by the Actuary and Administering Authority to reflect any changes in contribution requirements as a result of any benefit costs being insured with a third party.

Regulatory

The key regulatory risks are as follows (these apply equally to the insured and non-insured benefits):-

- Changes to Regulations, e.g. changes to the benefits package, retirement age
- Changes to national pension requirements and/or HMRC Rules

Governance

The Fund has done as much as it believes it reasonably can to enable employing bodies and Fund members to make their views known to the Fund and to participate in the decision-making process. This FSS was consulted on during 2020. The document was finalised following the Committee meeting on 26 March 2021.

The key governance risks are as follows:-

- The quality of membership data deteriorates materially due to breakdown in processes for updating the information resulting in liabilities being under or overstated
- Administering Authority is unaware of structural changes in the employer's membership (e.g. unexpected fall in employee numbers, large number of retirements or redundancy exercises for older members) with the result that contribution rates are set at too low a level
- An employer ceasing to exist without prior notification, resulting in a large exit credit requirement from the Fund impacting on cashflow requirements.
- Changes in the Committee membership.

For these risks to be minimised much depends on information being supplied to the Administering Authority by the employing bodies. Arrangements are strictly controlled and monitored, but in most cases the employer, rather than the Fund as a whole, bears the risk.

8

Monitoring and Review

The Administering Authority has taken advice from the actuary in preparing this Statement, and has consulted with the employers participating in the Fund.

A full review of this Statement will occur no less frequently than every three years, to coincide with completion of a full actuarial valuation. Any review will take account of the current economic conditions and will also reflect any legislative changes.

The Administering Authority will monitor the progress of the funding strategy between full actuarial valuations. If considered appropriate, the funding strategy will be reviewed (other than as part of the triennial valuation process), for example, if there:

- has been a change in investment strategy
- has been a significant change in market conditions, and/or deviation in the progress of the funding strategy
- have been significant changes to the Fund membership, or LGPS benefits
- have been changes to the circumstances of the employer to such an extent that they impact on or warrant a change in the funding strategy
- have been any significant special contributions paid into the Fund.
- there has been a change in Regulations or Guidance which materially impacts on the policies within the funding strategy.

When monitoring the funding strategy, if the Administering Authority considers that any action is required, the employers will be contacted.

Cost Management Process

The cost management process was set up by HMT, with an additional strand set up by the Local Government Pension Scheme (Scotland) Advisory Board (for the Scottish LGPS). The aim of this was to control costs for employers and taxpayers via adjustments to benefits and/or employee contributions.

As part of this, it was agreed that employers should bear the costs/risks of external factors such as the discount rate, investment returns and inflation changes, whereas employees should bear the costs/risks of other factors such as wage growth, life expectancy changes, ill health retirement experience and commutation of pension.

The outcome of the initial cost management valuation was expected to be implemented by now, based on data from the 2017 valuations for the Scottish LGPS. This had been put on hold due to age discrimination cases (the McCloud judgment) brought in respect of the firefighters and judges schemes, relating to protections provided when the public sector schemes were changed (which was on 1 April 2015 for the Scottish LGPS). The cost cap has now been un-paused and we expect more detail to emerge in due course over 2021. Consideration of the outcome of this process would be expected to be taken in to account at the next valuation (in 2023) unless the outcome requires this to be done prior to then.

The McCloud judgment

The government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. A consultation was issued in July 2020, which confirms that the remedy will have the effect of removing the current age criteria applied to the underpin implemented in 2015 for the LGPS, which would then apply to all members who were active as at 1 April 2012. The relevant estimated costs of the remedy have been quantified and notified to employers on this basis. The final funding position and certified contributions for each employer include the estimated costs of the McCloud remedy.

As a consequence of McCloud, cost management had been paused until recently (HMT and GAD are now considering the LGPS specific impact before commenting on the outcomes). No allowance for cost management has been made in this valuation. This will be reconsidered once the final outcomes are known.

Appendix A – Actuarial Method and Assumptions

Method

The actuarial method to be used in the calculation of the solvency funding target is the Projected Unit method, under which the salary increases assumed for each member are projected until that member is assumed to leave active service by death, retirement or withdrawal from service. This method makes advance allowance for the anticipated future ageing and decline of the current closed membership group potentially over the period of the rates and adjustments certificate.

Financial assumptions – solvency Funding target and the cost of future accrual (or Primary Rate)

Investment return (discount rate)

The discount rate at the valuation has been derived based on an assumed return equal to the gilt yield derived from market instruments, principally conventional and index-linked UK Government gilts as at the valuation date, reflecting the profile and duration of the Scheme's accrued liabilities. This return will be reviewed from time to time based on the investment strategy, market outlook and the Fund's overall risk metrics.

Inflation (Consumer Prices Index)

The inflation assumption will be taken to be the investment market's expectation for RPI inflation as indicated by the difference between yields derived from market instruments, principally conventional and index-linked UK Government gilts as at the valuation date, reflecting the profile and duration of the Fund's accrued liabilities.

For the purposes of the valuation, we have assumed that the RPI/CPI wedge will be 1% p.a. until 2030 and then 0% p.a. after 2030. The overall average reduction to the assumption to long term RPI inflation to arrive at the CPI inflation assumption at the valuation date is therefore broadly 0.55% per annum.

This adjustment to the RPI inflation assumption will be reviewed from time to time to take into account any changes in market expectations caused by the reform of the RPI index. Any change will then be implemented for all relevant policies in this Funding Strategy Statement.

Salary increases

In relation to benefits earned prior to 1 April 2015, the assumption for real salary increases (salary increases in excess of price inflation) will be determined by an allowance of 0.5% p.a. over the inflation

(CPI) assumption as described above in respect of First Aberdeen employees and an allowance of 1.375% p.a. over the CPI assumption in respect of First Glasgow employees. This includes allowance for promotional increases.

Pension increases/Indexation of CARE benefits

Increases to pensions are assumed to be in line with the inflation (CPI) assumption described above. This is modified appropriately to reflect any benefits which are not fully indexed in line with the CPI e.g. Guaranteed Minimum Pensions where the LGPS is not required to provide full indexation. The exception to this is for members who will reach state pension age after 5 April 2021. In line with expected future changes to the regulations, we have allowed for increases on Guaranteed Minimum Pensions to increase in line with the inflation (CPI) assumption described above.

For members in pensionable employment, their CARE benefits are also indexed by CPI although this can be less than zero, i.e. a reduction in benefits, whereas for pension increases this cannot be negative, as pensions cannot be reduced.

Demographic assumptions

Mortality/Life Expectancy

The mortality in retirement assumptions will be based on the most up-to-date information in relation to self-administered pension schemes published by the Continuous Mortality Investigation (CMI), making allowance for future improvements in longevity and the experience of the Fund. The mortality base tables used are set out below, with a loading reflecting Fund specific experience. The derivation of the mortality assumption is set out in a separate paper as supplied by the Actuary.

A specific mortality assumption has also been adopted for current members who retire on the grounds of ill health. For all members, it is assumed that the trend in longevity seen over recent time periods up to the valuation date (as evidenced in the 2019 CMI analysis) will continue in the longer term and as such, the assumptions build in a level of longevity 'improvement' year on year in the future in line with the CMI 2019 projections and a long term improvement trend of 1.75% per annum.

As an indication of impact, we have set out the life expectancies at age 65 based on the 2020 assumptions:

	Male Life Expectancy at 65		Female Life Expectancy at 65	
	First Aberdeen	First Glasgow	First Aberdeen	First Glasgow
Pensioners	21.9	21.3	25.2	24.7
Actives aged 45 now	23.6	23.6	25.3	27.4
Deferreds aged 45 now	21.7	22.1	26.2	25.6

For example, a First Aberdeen male pensioner, currently aged 65, would be expected to live to age 86.9. Whereas a First Aberdeen male active member aged 45 would be expected to live until age 88.6. This is a reflection of the expected improvement in life expectancy over the next 20 years in the assumptions above.

The mortality before retirement has also been adjusted based on LGPS wide experience.

Commutation

It has been assumed that, on average, 50% of retiring members will take the maximum tax-free cash available at retirement and 50% will take the standard 3/80ths cash sum. The option which members have to commute part of their pension at retirement in return for a lump sum is a rate of £12 cash for each £1 p.a. of pension given up.

Other Demographics

Following an analysis of Fund experience carried out by the Actuary, withdrawal rates, the proportions married/civil partnership assumption and incidence of ill health retirements used for the Whole Fund were unchanged from the last ACCTF valuation. The assumption for the retirement age of non-pensioners was slightly adjusted since the previous valuation in order to allow for members who are over their critical retirement age, but under 65, to retire in line with decrements, as set out in the valuation report. In addition, no allowance will be made for the future take-up of the 50:50 option (this is the same assumption as at the last valuation). Where any member has actually opted for the 50:50 scheme, this will be allowed for in the assessment of the rate for the next 3 years.

Expenses

Expenses are met out the Fund, in accordance with the Regulations. This is allowed for by including an agreed amount in the assessed contributions required from the employer. This addition is reassessed at each valuation. Investment expenses have been allowed for implicitly in determining the discount rates.

Discretionary Benefits

The costs of any discretion exercised by the employer in order to enhance benefits for a member through the Fund will be subject to additional contributions from the employer as required by the Regulations as and when the event occurs. As a result, no allowance for such discretionary benefits has been made in the valuation.

Employer Asset Shares

The Fund is a multi-employer pension scheme that is not formally unitised and so individual employer asset shares are calculated at each actuarial valuation. This means it is necessary to make some approximations in the timing of cashflows and allocation of investment returns when deriving the employer asset share.

In attributing the overall investment performance obtained on the assets of the Fund to each employer a pro-rata principle is adopted. This approach is effectively one of applying a notional individual employer investment strategy identical to that adopted for the Fund as a whole unless agreed otherwise between the employer and the Fund at the sole discretion of the Administering Authority.

At each review, cashflows into and out of the Fund relating to each employer, any movement of members between employers within the Fund, along with investment return earned on the asset share, are allowed for when calculating asset shares at each valuation.

Summary of key whole Fund assumptions used for calculating funding target and cost of future accrual (the "primary rate") for the 2020 actuarial valuation

Long-term yields		
	Market implied RPI inflation	2.8% p.a.
Solvency Funding Target financial assumptions		
	Investment return/Discount Rate	0.7% p.a.
	CPI price inflation	RPI less 1% p.a. pre 2030 and RPI less 0% post 2030. At 31 March 2020 this was approximately equivalent to a single equivalent CPI assumption of 2.25% p.a. over the term of the liabilities
	Long Term Salary increases	CPI+0.5% p.a. First Aberdeen, CPI+1.375% p.a. First Glasgow
	Pension increases/indexation of CARE benefits	In line with CPI assumption above

Life expectancy assumptions

The post retirement mortality tables adopted for this valuation are set out below:

The post retirement assumptions adopted use S3PA tables ("middle" tables for females), other than for female dependants, where the S3DA tables have been used and for members retiring in ill-health, where the S3IA tables have been used. The future improvements assumptions adopted are in line with the CMI 2019 model with Sk=7.5, long term rate of 1.75% and weightings as set out below:

Current Status	Retirement Type	Weighting – First Aberdeen members	Weighting – First Glasgow members
Annuitant	Normal Health	108% males, 88% females	117% males, 94% females
	Dependant	100% males, 104% females	145% males, 111% females
	Ill Health	132% males, 149% females	137% males, 150% females
	Future Dependant	128% males, 112% females	139% males, 119% females
Active	Normal Health	112% males, 115% females	112% males, 86% females
	Ill Health	128% males, 169% females	128% males, 131% females
Deferred	All	143% males, 102% females	136% males, 110% females
Active/deferred	Future Dependant	137% males, 121% females	140% males, 120% females

All life expectancies are normal health "cohort" expectancies from age 65 in 2020 and non-pensioners' current age assumed to be 45.

Other demographic assumptions are set out in the Actuary's formal report.

Appendix B – Employer Deficit Recovery / Surplus Spreading Plan

If the assets of the employer are less than the liabilities at the effective date, a deficit recovery plan needs to be adopted such that additional contributions are paid into the Fund to meet the shortfall.

It is the Fund's objective that any funding deficit is eliminated as quickly as the employer can reasonably afford based on the Administering Authority's view of the employer's covenant and risk to the Fund. This will determine the minimum contribution requirement and the employer will be free to select higher contributions if they wish.

The recovery period is determined by ensuring overall contributions are reasonably stable relative to the current funding plan allowing for any affordability constraints.

If the assets of the employer are greater than the liabilities, a surplus spreading plan will be implemented in order for the Fund to release any surplus at an appropriate rate back to the employer. This may include using surplus to meet the primary accrual costs over the inter-valuation period.

In determining the actual spread period to apply for the employer, the Administering Authority may take into account some or all of the following factors:

- The size of the funding shortfall / surplus;
- The business plans of the employer;
- The assessment of the financial covenant of the employer, and security of future income streams;
- Any contingent security available to the Fund or offered by the employer such as guarantor or bond arrangements, charge over assets, etc.
- Any insurance arrangement in place (e.g. the buy-in with Rothesay Life)

The objective is to recover any deficit (or remove any surplus) over a reasonable timeframe, and this will be periodically reviewed.

Other factors affecting the Employer Recovery Plan

As part of the process of agreeing funding plan with the employer, the Administering Authority will consider the use of contingent assets and other tools such as bonds or guarantees that could assist the employer in managing the cost of their liabilities or could provide the Fund with greater security against outstanding liabilities. All other things equal this could result in lower cash contributions being acceptable to the Administering Authority.

Appendix C – Termination Policy for employers exiting the Fund

When an employer ceases to participate within the Fund, it becomes an exiting employer under the Regulations. The Fund is then required to obtain an actuarial valuation of that employer's liabilities in respect of the benefits of the exiting employer's current and former employees, along with a termination contribution certificate.

In this situation, if the other employer is remaining in the Fund, due to the structure of the guarantees in place, the remaining employer would subsume the exiting employer's liabilities and assets as agreed with the Administering Authority.

Where both employers exit the Fund, the liabilities will be orphaned. In this situation, the Fund's policy is that either:

1. the liabilities will be calculated on assumptions which the Actuary deems reasonable as a proxy for the likely cost of securing the benefits with an insurer (with regard to existing buy-in arrangements)
2. the liabilities could be secured with an insurer (to the extent that they are not already insured)
3. at the discretion of the Administering Authority, a suspension notice may be agreed to in certain circumstances. The Fund reserves the right to require a side legal agreement alongside any suspension notices detailing the specifics of the arrangement including for example the length of such a notice.

With the exception of where a suspension notice has been issued, any exit payments due should be paid immediately, although instalment plans will be considered by the Administering Authority on a case by case basis.

Any exit credits (surplus assets over liabilities) will be paid from the Fund to the exiting employer following certification by the Actuary. The Administering Authority also reserves the right to modify this approach on a case by case basis if circumstances warrant it in particular having regard to the covenant and residual investment risk.

<u>Allowing for the McCloud Judgment in Termination Valuations</u>

The government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. A consultation was issued in July 2020, which confirms that the remedy will have the effect of removing the current age criteria applied to the underpin implemented in 2015 for the Scottish LGPS, which would then apply to all members who were active as at 1 April 2012.

As part of any termination assessment, a reasonable estimate for the potential cost of McCloud will be included.

The allowance will be calculated in line with the treatment set out in this Funding Strategy Statement for all members of the outgoing employer using the termination assessment assumptions. For the avoidance of doubt, there will be no recourse for an employer with regard to McCloud, once the final termination has been settled and payments have been made. Once the remedy is known, any calculations will be performed in line with the prevailing regulations and guidance in force at the time.

The Administering Authority can vary the treatment on a case-by-case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary.

Appendix D – Glossary

Actuarial Valuation: an investigation by an actuary into the ability of the Fund to meet its liabilities. For the LGPS the Fund Actuary will assess the funding level of each participating employer and agree contribution rates with the administering authority to fund the cost of new benefits and make good any existing deficits as set out in the separate Funding Strategy Statement. The asset value is based on market values at the valuation date.

Administering Authority: the council with a statutory responsibility for running the Fund and that is responsible for all aspects of its management and operation.

Best Estimate Assumption: an assumption where the outcome has a 50/50 chance of being achieved.

Bonds: loans made to an issuer (often a government or a company) which undertakes to repay the loan at an agreed later date. The term refers generically to corporate bonds or government bonds (gilts).

Buy-in: A buy-in policy is a bulk annuity policy held as a scheme investment, which serves to provide payments that exactly match those due to the members which it covers. Some schemes seek to remove risk in relation to a certain group of members through this type of policy, usually just the pensioner membership. The Fund entered in to a Buy-in with Rothesay Life in respect of the pensioner population in November 2020.

Career Average Revalued Earnings Scheme (CARE): with effect from 1 April 2015, benefits accrued by members in the LGPS take the form of CARE benefits. Every year members will accrue a pension benefit equivalent to 1/49th of their pensionable pay in that year. Each annual pension accrued receives inflationary increases (in line with the annual change in the Consumer Prices Index) over the period to retirement.

Contingent Assets: assets held by employers in the Fund that can be called upon by the Fund in the event of the employer not being able to cover the debt due upon termination. The terms will be set out in a separate agreement between the Fund and employer.

Covenant: the assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term or affordability constraints in the short term.

CPI: acronym standing for “Consumer Prices Index”. CPI is a measure of inflation with a basket of goods that is assessed on an annual basis. The reference goods and services differ from those of RPI. These goods are expected to provide lower, less volatile inflation increases. Pension increases in the LGPS are linked to the annual change in CPI.

CPIH: An alternative measure of CPI which includes owner occupiers’ housing costs and Council Tax (which are excluded from CPI).

Deficit: the extent to which the value of the Fund’s past service liabilities exceeds the value of the Fund’s assets. This relates to assets and liabilities built up to date, and ignores the future build-up of pension (which in effect is assumed to be met by future contributions).

Discount Rate: the rate of interest used to convert a cash amount e.g. future benefit payments occurring in the future to a present value.

Employing bodies: any organisation that participates in the LGPS, including admission bodies and Fund employers.

Employer's Future Service Contribution Rate (Primary Rate): the contribution rate payable by an employer, expressed as a % of pensionable pay, as being sufficient to meet the cost of new benefits being accrued by active members in the future. The cost will be net of employee contributions and will include an allowance for the expected level of administrative expenses (either as a % of pensionable pay or a fixed £ amount).

Exit Credit: the amount payable from the Fund to an exiting employer in the case where the exiting employer is determined to be in surplus at the point of cessation based on a termination assessment by the Fund Actuary.

Funding or solvency Level: the ratio of the value of the Fund’s assets and the value of the Fund’s liabilities expressed as a percentage.

Funding Strategy Statement: this is a key governance document that outlines how the administering authority will manage employer’s contributions and risks to the Fund.

Government Actuary's Department (GAD): the GAD is responsible for providing actuarial advice to public sector clients. GAD is a non-ministerial department of HM Treasury.

Guarantee / guarantor: a formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer’s covenant to be as strong as its guarantor’s.

Hedging: a strategy that aims to reduce funding volatility. This is achieved by investing in assets that capture levels of yields based on agreed trigger levels so the change in assets mimics the change in liabilities.

Investment Strategy: the long-term distribution of assets among various asset classes that takes into account the Fund's objectives and attitude to risk.

LGPS: the Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility, members' contribution rates, benefit calculations and certain governance requirements.

Liabilities: the actuarially calculated present value of all benefit entitlements i.e. Fund cashflows of all members of the Fund, built up to date or in the future. The liabilities in relation to the benefit entitlements earned up to the valuation date are compared with the present market value of Fund assets to derive the deficit and funding/solvency level. Liabilities can be assessed on different set of actuarial assumptions depending on the purpose of the valuation.

Maturity: a general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.

McCloud Judgment: This refers to the linked legal cases of Sargeant and McCloud, and which found that the transitional protections (which were afforded to older members when the public service pension schemes were reformed in 2014/15) constituted unlawful age discrimination.

Members: the individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).

Orphan liabilities: liabilities in the Fund for which there is no sponsoring employer within the Fund. Ultimately orphan liabilities must be underwritten by all other employers in the Fund.

Percentiles: relative ranking (in hundredths) of a particular range. For example, in terms of expected returns a percentile ranking of 75 indicates that in 25% of cases, the return achieved would be greater than the figure, and in 75% cases the return would be lower.

Prepayment: the payment by employers of contributions to the Fund earlier than that certified by the Actuary. The amount paid will be reduced in monetary terms compared to the certified amount to reflect the early payment.

Present Value: the value of projected benefit payments, discounted back to the valuation date.

Primary rate: the contribution rate required to meet the cost of future accrual of benefits, ignoring any past service surplus or deficit but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer's covenant.

Profile: the profile of an employer's membership or liability reflects various measurements of that employer's members, i.e. current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc.

Prudent Assumption: an assumption where the outcome has a greater than 50/50 chance of being achieved i.e. the outcome is more likely to be overstated than understated. Legislation and Guidance requires the assumptions adopted for an actuarial valuation to be prudent.

Rates and Adjustments Certificate: a formal document required by the LGPS (Scotland) Regulations, which must be updated at least every three years at the conclusion of the formal valuation. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three year period until the next valuation is completed.

Recovery period: the target length of time over which the current deficit is intended to be paid off or the current surplus is intended to be refunded.

Recovery Plan: a strategy by which an employer will make up a funding deficit or run off surplus over a specified period of time ("the recovery period"), as set out in the Funding Strategy Statement.

Secondary rate: the adjustment to the Primary rate to arrive at the total contribution each employer is required to pay. It is essentially the additional contribution (or reduction in contributions) resulting from any deficit (or surplus) attributable to the employer within the Fund.

Section 13 Valuation: in accordance with Section 13 of the Public Service Pensions Act 2014, the Government Actuary's Department (GAD) have been commissioned to advise the Scottish Public Pensions Agency (SPPA) in connection with reviewing the 2020 LGPS actuarial valuations. All LGPS Funds therefore will be assessed on a standardised set of assumptions as part of this process.

Solvency Funding Target: an assessment of the present value of benefits to be paid in the future. The desired funding target is to achieve a solvency level of a 100% i.e. assets equal to the accrued liabilities at the valuation date assessed on the ongoing concern basis.

Suspension Notice: A notice that may be issued to an employer to suspend that employer's liability to pay an exit payment in circumstances where the employer would otherwise exit. Should a notice be made, the employer must continue to make such contributions towards the liabilities of the fund in respect of benefits for the employer's current and former employees until a new and satisfactory valuation is carried out and the suspension notice is withdrawn. A side legal agreement may be required alongside such notices.

Valuation funding basis: the financial and demographic assumptions used to determine the employer's contribution requirements. The relevant discount rate used for valuing the present value of liabilities is consistent with a prudent estimate of the expected rate of return of the Fund's investments.

50/50 Scheme: in the LGPS, active members are given the option of accruing a lower personal benefit in the 50/50 Scheme, in return for paying a lower level of contribution.

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Report on the Actuarial Valuation as at 31 March 2020

DRAFT

Aberdeen City Council Transport Fund

March 2021

welcome to brighter

Contents

Appendices

Introduction

This report is addressed to the Administering Authority of the Aberdeen City Council Transport Fund ("the Administering Authority") and is provided to meet the requirements of Regulation 60 of the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended) ("the Regulations"). It describes the factors considered by the Administering Authority when carrying out the actuarial valuation as at 31 March 2020 and the decisions reached as a result.

The purpose of the actuarial valuation is for the Administering Authority to determine:

1. The expected cost of providing the benefits built up by members at the valuation date (the 'liabilities'), and compare this against the funds held by the Fund (the 'assets').

2. The contributions needed to cover the cost of the benefits that active members will build up in the future and other costs incurred in running the Fund (the 'Primary Contribution Rate').

3. An appropriate plan for making up the shortfall if the Fund has less assets than liabilities or refunding the surplus if the Fund has more assets than liabilities. This plan will cover the amounts which will need to be paid (the 'Secondary Contribution Rate') and the timeframe over which they will be paid ('the Spread Period').

Signature		
Name	Paul Middleman	Laura Evans
Qualification	Fellow of the Institute and Faculty of Actuaries	Fellow of the Institute and Faculty of Actuaries
Date	29 March 2021	

This report uses various technical terms. These are explained in more detail in the explanatory boxes which appear throughout this report, and in the Glossary at Appendix H.

This report has been prepared in accordance with Technical Actuarial Standards TAS 100: Principles for Technical Actuarial Work and TAS 300: Pensions which are issued by the Financial Reporting Council. The calculations referred to in the report use methods and assumptions appropriate for reviewing the financial position of the Fund and determining a contribution rate for the future. Mercer does not accept liability to any third party in respect of this report; nor do we accept liability to the Administering Authority if the information provided in this report is used for any purpose other than that stated. The report may be disclosed to members and others who have a statutory right to see it. It may also be disclosed to any participating employer and, if the Administering Authority and Mercer consent, it may be disclosed to other third parties.

1

Funding Strategy – Key Elements

Fundamental to the valuation results is the funding strategy adopted by the Fund. This funding strategy is set out in a specific document (the Funding Strategy Statement or FSS for short) which is one of the Administering Authority's key governance documents for the Fund. In essence, the FSS sets out an overview of the approach to be used for the actuarial valuation. Amongst other things it outlines the assumptions, both economic and demographic, to be used in calculating the value of the liabilities built up, the contributions required to correct any funding shortfall or surplus, and the contribution rate required to fund the benefits for future service. It also sets out the strategy for making good any funding shortfall, in particular how any shortfall is expected to be financed in terms of the balance between future contributions and future investment returns, and the period over which any surplus or shortfall is expected to be recovered.

The FSS is the Administering Authority's key governance document in relation to the actuarial valuation. It sets out the funding policies adopted, the actuarial assumptions used, and the timescales over which deficits will be paid off. Employers are consulted about the FSS as part of the actuarial valuation process.

The principal elements of the funding strategy adopted for this actuarial valuation are as follows:

- The McCloud judgment (see Appendix D for details) – the valuation results as set out in Section 2 of this report include an allowance in relation to the potential cost of the McCloud judgment. An estimate of the effect of the judgment, based on the proposed remedy in the consultation launched in July 2020 for the Whole Fund is shown at the end of that section. Each employer has been notified of the estimate of the potential cost of the proposed remedy which has been included in their liabilities (expected to be minimal for both employers) and the additional contributions over 2021/24 in respect of this. For simplicity, although the proposed remedy would lead to the underpin no longer applying to accrual post 31 March 2022, the estimated cost of future accrual up to that point has been spread over the three years of the certification period i.e. 1 April 2021 – 31 March 2024.

The "McCloud judgment" refers to the legal decisions in the Sargeant/McCloud cases for the Fire and Judiciary pension arrangements. The courts ruled that the transitional protections afforded to older members when these schemes were amended constituted unlawful age discrimination. Remedial action, in the form of benefit changes for these schemes, will therefore be required. Although the above cases did not relate directly to the LGPS, the UK Government has accepted that remedies will need to apply to all the public service pension schemes, including the LGPS. For the LGPS the transitional protections took the form of an underpin, where older members got the better of the benefits payable under the new and old schemes. At this stage it seems likely that the remedy will be to extend this underpin to younger members (see Appendix D for more details), and we have allowed for this in our calculations.

- Following the Government's recent consultation, the liabilities also allow for the "Interim solution" for GMP to be extended in order to provide full CPI indexation on GMP benefits in payment for all members with a state pension age after 5 April 2016. The cost of this (combined with the cost of the McCloud judgment) is set out in Section 2.
- Assumed rate of future long term average CPI inflation – based on the yields available on gilts and index-linked gilts of appropriate duration less an adjustment of 1% p.a. before 2030 and 0% after 2030 to allow for the difference between market-implied future RPI and estimated future CPI inflation (see comment regarding RPI reform below). This is broadly equivalent to 2.25% p.a. over the term of the liabilities.
- Since the valuation date, it has been announced that RPI inflation will be reformed with effect from 2030 to align the index with the CPIH inflation measure. At the valuation, we have allowed for a variable RPI CPI gap as set out above in order to incorporate the impact of this change on market implied inflation.
- Investment returns linked to the return on UK Government gilts for past and future service – 0.7% p.a. at the valuation date, based on a prudent estimate of long term returns on the Fund's assets.
- Future pay growth – 0.5% p.a. over and above CPI in the longer term in respect of members of First Aberdeen Limited and 1.375% p.a. over and above CPI in the longer term in respect of members of First Glasgow Limited.
- Baseline life expectancy based on a scheme-specific mortality study with separate assumptions for each employer
- Future mortality improvements based on the CMI 2019 model with a long-term improvement trend of 1.75% p.a.
- The surplus at the valuation date is sufficient to offset the primary contribution requirements for the projected future working lifetime of the active membership. Therefore the Administering Authority and employers have agreed that no employer contributions will be required for the period of the rate certificate.
- There have been a number of significant events, specifically a fund merger and buy-in effective as at 19 November 2020. This doesn't affect the conclusions in this report but we have included further commentary on the buy-in within the report.
- Throughout this report, unless specified otherwise, references to the 31 March 2017 are solely in respect of the Aberdeen City Council Transport Fund and have no regard to the position of the Strathclyde No3. Pension Fund (the Fund from which First Glasgow Limited transferred).

2
Key results of the funding assessment

Solvency funding position

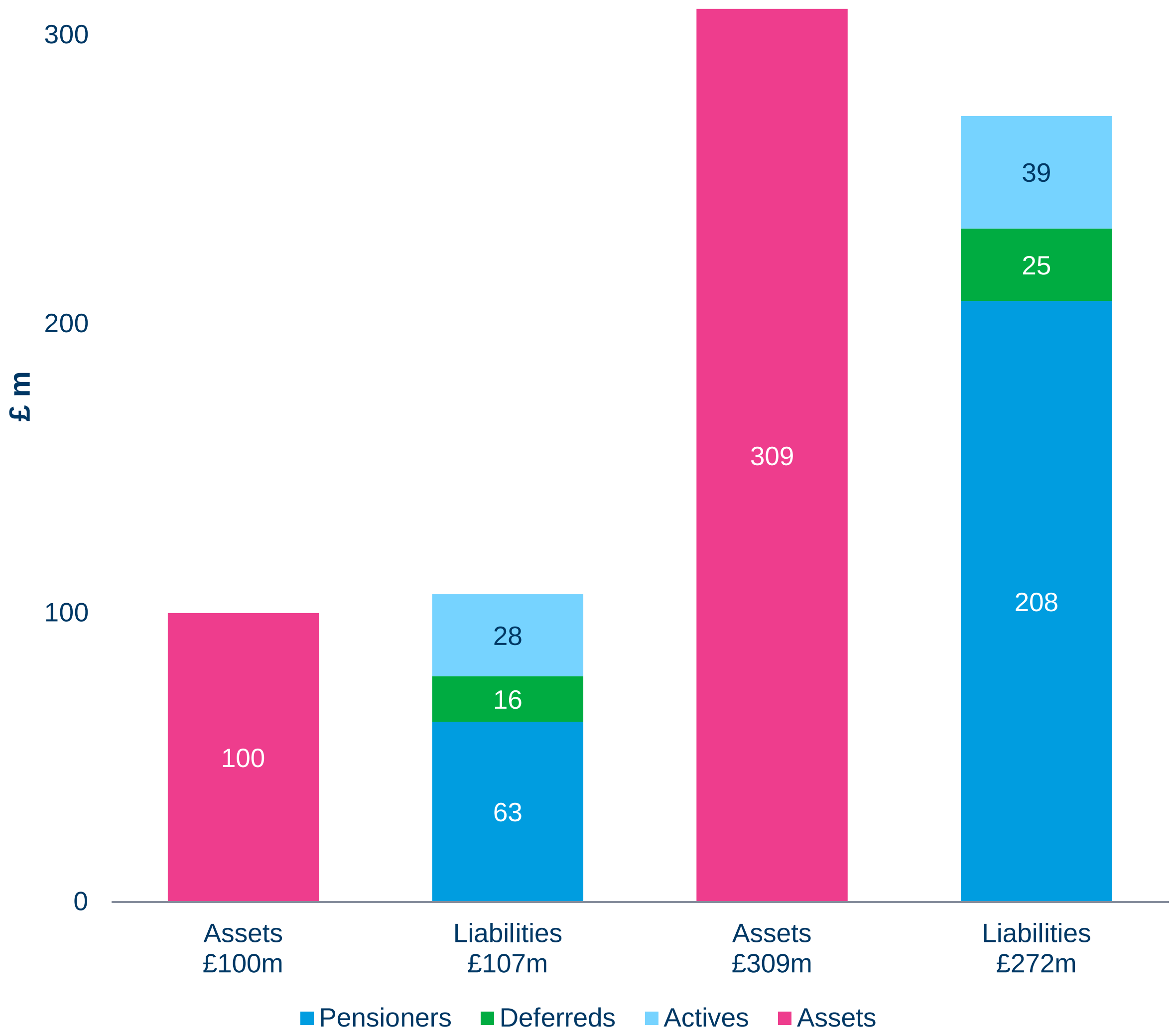
The table below compares the assets and liabilities of the Fund at 31 March 2020. Figures are also shown for the last valuation (solely for First Aberdeen as the sole employer within the ACCTF at that time) as at 31 March 2017 for comparison. Please note that the liabilities at both dates **exclude** the present value of pre 1986 recharges that are the responsibility of the NESPF.

31 March 2017

Solvency funding level 94%
Deficit £7m

31 March 2020

Solvency funding level 114%
Surplus £37m



The liability value at 31 March 2020 shown in the chart above is known as the Fund's "solvency funding target". The solvency funding target is calculated using assumptions that the Administering Authority has determined are appropriate having consulted with the actuary, and are also set out in the FSS.

The LGPS Regulations require the contributions to be set so as to secure the Fund's solvency and long-term cost efficiency. In this context solvency means being able to meet the liabilities as and when they arise, with long-term cost efficiency meaning that contribution levels should not be set so as to give rise to additional costs at a later date. In practice, contribution levels have been set so as to target a solvency funding level of 100%, based on the funding parameters outlined in Section 1 above.

The chart shows that **at 31 March 2020 there was a surplus of £37m** against the Fund's solvency funding target. An alternative way of expressing the position is that **the Fund's assets were sufficient to cover 114% of its liabilities** – this percentage is known as the solvency funding level of the Fund.

At the previous valuation at 31 March 2017 the deficit was £7m, equivalent to a solvency funding level of 94%. The key reasons for the changes between the two valuations are considered in Section 3.

Further details of the way in which the solvency funding target has been calculated are set out in Appendix A.

Primary Contribution Rate

The "Primary rate" of the employers' contribution is the contribution rate required to meet the cost of the future accrual of benefits including ancillary, death in service and ill health benefits together with administration costs.

The valuation looks at the normal employer contribution rate required to cover the cost of the benefits (including death benefits and expenses) that will be built up over the year after the valuation date (the "Primary Contribution Rate"). A summary of the assumptions used is provided in Appendix A.

The table below gives a breakdown of the Primary Contribution Rate at 31 March 2020 and also shows the corresponding rate at 31 March 2017 for comparison. In calculating the average Primary Contribution Rate we have not made any allowance for future members to opt for the 50:50 scheme.

Active members pay contributions to the Fund as a condition of membership in line with the rates required under the governing Regulations (see Appendix D).

	% of Pensionable Pay plus £ amount*	
PRIMARY CONTRIBUTION RATE	**31 March 2020**	**31 March 2017**
Normal Contribution rate for retirement and death benefits including expenses	50.0% plus £140,000 p.a.**	64.6%
Average member contribution rate	6.3%	6.1%
Primary contribution rate	43.7% plus £140,000 p.a.**	58.5%

**In line with updated CIPFA guidance, the 2020 Primary Contribution Rate is the weighted average of the individual employer Primary Contribution Rates as derived based on their individual circumstances*

***Due to the rapidly declining payroll we have certified the administration expenses as a £ amount rather than a % of pensionable pay.*

Correcting the imbalance – Secondary Contribution Rate

The funding objective as set out in the FSS is to achieve and maintain a solvency funding level of 100% of liabilities (the solvency funding target). In line with the FSS, where a shortfall exists at the effective date of the valuation a recovery plan will be put in place which requires additional contributions to correct the shortfall. Equally, where there is a surplus it is usually appropriate to offset this against contributions for future service, in which case contribution reductions will be put in place to allow for this.

The FSS sets out the process for determining the recovery plan in respect of each employer.

The surplus at the valuation date (including allowance for the estimated costs in relation to the McCloud judgment) is sufficient to offset the primary contribution requirements for the projected future working lifetime of the active membership. Therefore the Administering Authority and employers have agreed that no employer contributions will be required for the period of the rate certificate.

> The “Secondary rate” of an individual employers’ contribution is an adjustment to the Primary Contribution Rate to reflect any past service deficit or surplus, to arrive at the rate the employers are required to pay.

The McCloud Judgment and GMP indexation

As described in Section 1 of this report, the above figures include an allowance for the estimated cost of the McCloud judgment. Additionally, they also assume that full CPI indexation of GMP benefits in payment will be extended to cover all members with a state pension age after 5 April 2016. At the overall Fund level we estimate that the cost of both these factors could be an increase in past service liabilities of broadly £2 million and an increase in the Primary Contribution rate in respect of the McCloud Judgment of <0.1% of Pensionable Pay per annum from 2020 until 2022. For the purpose of contribution setting, we have spread this over the three years in the certification period resulting in a cost of <0.1% of Pensionable pay per annum from 1 April 2021 – 31 March 2024.

> The "McCloud judgment" refers to a legal challenge in relation to historic benefit changes for all public sector schemes being age discriminatory. The Government announced in 2019 that this needs to be remedied for all schemes including the LGPS. This is likely to result in increased costs for some employers. This remedy is not yet agreed but the consultation in 2020 set out the Government's intended approach to address the implications.

Fund Merger and buy-in events

First Glasgow Limited was admitted as an employer to the Fund in late 2019 and this is therefore the first valuation of the ACCTF as a multi-employer Scheme.

The Fund subsequently completed a c£230m pensioner buy-in transaction with the Rothesay Life in November 2020. This transaction insures the pension payments of 1,371 pensioners across both employers through a pensioner-only buy-in. This was a significant de-risking step for Fund and its employers as a number of risks have been mitigated.

In relation to existing and former employees of First Aberdeen Ltd, pension increases in deferment and payment in respect of benefits accrued prior to 26 October 1986 are recharged monthly on a £ for £ basis to the North East Scotland Pension Fund (NESPF). This is because as part of the deregulation of transport services the liability currently remains with the Grampian Regional Transport Authority (a historic employer in the NESPF) and not First Aberdeen Ltd. For the year to 31 March 2021, recharges passed to the NESPF are projected to be around £350,000. The liabilities quoted at the valuation date in this report are shown net of the liabilities which are recharged to the NESPF in respect of the pre 1986 pension increases.

3

Experience since last valuation

Summary of key inter-valuation experience

The outcomes from the valuation are determined both by the assumptions adopted for the future, and the Fund's historic experience relative to assumptions made in the past. In this section we consider the effect of the Fund's experience over the last three years.

The last actuarial valuation was carried out with an effective date of 31 March 2017. With effect from 1 April 2015 the scheme's benefit structure changed from a Final Salary Scheme to a Career Average Revalued Earnings (CARE) Scheme, and the 2017 actuarial valuation took these changes into account.

The average Pensionable Salary increase for the Fund members who were in service for the whole of the inter-valuation period was 2.2% per annum.

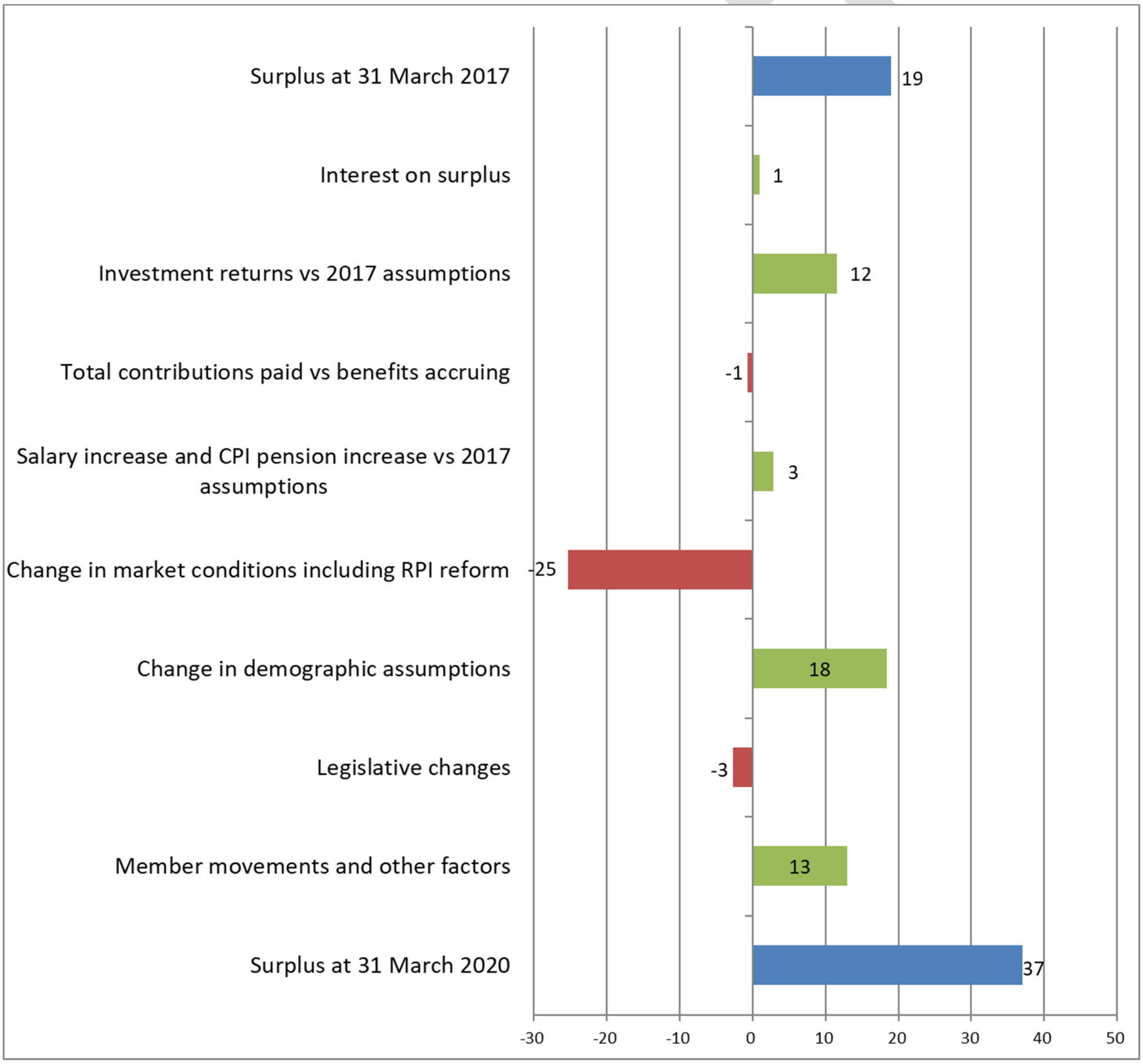
Pensions in payment (in excess of Guaranteed Minimum Pensions (GMPs) were increased as guaranteed under the Fund as follows:

- April 2018 3.0%
- April 2019 2.4%
- April 2020 1.7%

Over the inter-valuation period, benefit inflation has averaged 2.4% p.a.

Reasons for the change in funding position since the last actuarial valuation

The chart below sets out the main reasons for the change in the position between 31 March 2017 and 31 March 2020 of the now combined Fund, starting from the combined valuation positions at the 2017 valuations. The position at 31 March 2017 is taken from the Strathclyde No3. Pension Fund Valuation report. Figures shown in £m.



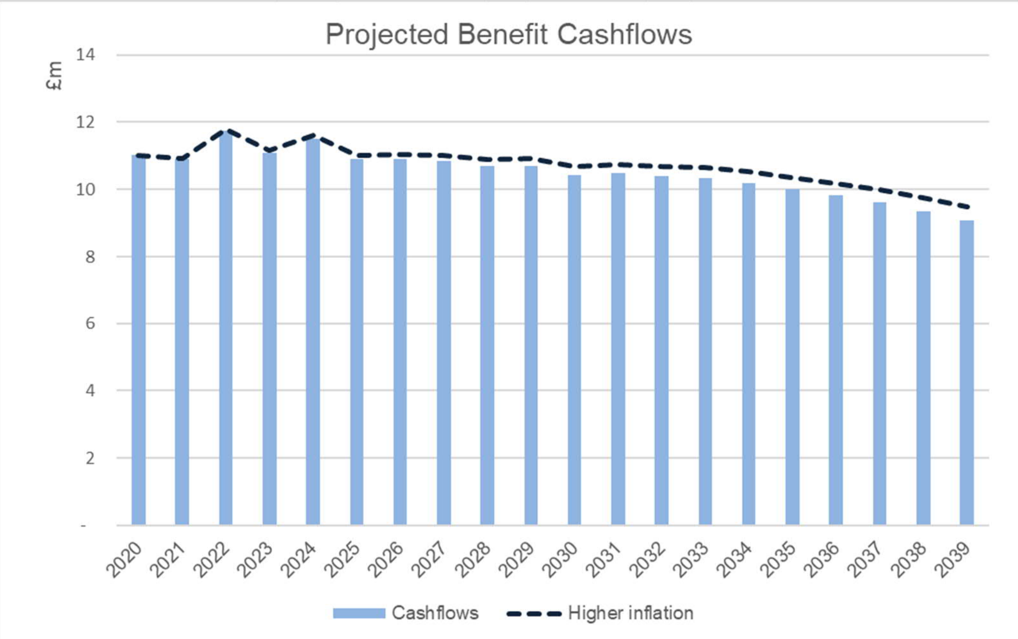
4

Cash flows, risks and alternative funding positions

Benefit cash flows

> The actuarial valuation process is principally concerned with projecting all the expected benefit cash flows into the future, and then converting them into present day values by discounting them to allow for assumed future investment returns. The chart shows those projected cash flows, and also illustrates how sensitive they are to the future inflation assumption.

The projected benefit cash flows which result from applying the assumptions as set out in Appendix A are shown in the chart below (gross of the benefits which are recharged to the North East Scotland Pension Fund). The additional trendline sets out how those total projected benefit cash flows would change if we were to assume inflation of 0.25% p.a. higher than the assumption used for the actuarial valuation as set out earlier and in Appendix A.
Over the 20 years following the valuation date, the extra benefit payments (including the recharges referenced above) which would result from the extra 0.25% p.a. inflation assumption are projected to be £4.4m.



Projected funding position at next actuarial valuation

The surplus at the valuation date is sufficient to offset the primary contribution requirements for the projected future working lifetime of the active membership. Therefore the Administering Authority and employers have agreed that no employer contributions will be required for the period of the rate certificate

The next actuarial valuation will take place with an effective date of 31 March 2023. If experience up to that date were to be in line with the assumptions made for this current actuarial valuation and contributions are paid at the agreed rates or amounts, there would be a surplus at 31 March 2023 of £31m, equivalent to a funding level of 114%. This is based on a roll forward from 30 November 2020 i.e. after taking into account the buy-in. This does not make any allowance for termination of either of the employers with any exit credits becoming payable.

Material risks faced by the Fund

The Fund is subject to some potentially material risks that are, to an extent, outside the Administering Authority's control, but could affect the funding level and ultimately the employer contribution requirements. Any material worsening of the funding level may mean employer contributions need to be recommenced to be able to provide the benefits built up in the Fund – unless experience acts in other ways to improve the funding level. Examples of such risks, and how the Administering Authority manages them, are:

> Funding a defined benefit pension scheme such as the LGPS is by its nature uncertain, and involves some level of risk. The principal funding risks are investment (e.g. whether the Fund earns the desired level of long-term real returns) and demographic (e.g. whether longevity of members is longer or shorter than anticipated). In practice, the key is whether such risks can be managed and mitigated.

- If an Employer becomes unable to pay contributions (when required) or to make good deficits in the future, the Fund's assets will be lower than expected and the funding level will be worse than expected. The Administering Authority regularly monitors the financial strength of the Employers so that actions can be taken to mitigate (but not fully remove) the risk.
- If future investment returns on assets are lower than assumed in the valuation, the Fund's assets will be lower, and the funding level worse, than expected. The Administering Authority has a process in place to monitor investment performance quarterly, and it reviews the Fund's investment strategy alongside each actuarial valuation. In practice given the low risk strategy and prudent discount rate, this risk is predominantly mitigated.
- If improvements in life expectancy are greater than assumed for non-insured members, the cost of benefits will increase because members are living longer than expected. This will mean the funding level will be worse than expected. The Administering Authority regularly reviews the Fund's experience and ensures that the assumptions it makes about members' life expectancy take the most recent information available into account.

- If members make decisions about their options which increase the Fund's liabilities, the funding level will be worse than expected. An example would be if members commute less pension for cash, than is being assumed. The Administering Authority reviews the Fund's experience at each valuation to ensure that their treatment of member options remains appropriate.

The pensioner buy-in entered during November 2020 significantly reduces the Fund's exposure to interest rate, inflation and longevity risks and therefore reduces reliance on the employer covenant substantially.

Impact of COVID-19

The valuation results and employer contributions shown in this report are assessed as at 31 March 2020. In March 2020 we saw significant falls in equity markets around the world in relation to the COVID-19 pandemic (in practice given the low risk investment strategy, the impact on the Fund in this respect was limited), though markets subsequently rebounded strongly over the year. This potentially has consequences in terms of funding and risk which have been considered when discussing contribution requirements with employers. As the position continues to evolve, this will be kept under review by the Administering Authority, who will monitor the development of the situation and keep all stakeholders informed of any potential implications so that the outcome can be managed effectively.

Sensitivity of funding position to changes in key assumptions

The value placed on the Fund's liabilities is critically dependent on the assumptions used to carry out the calculations. If future experience differs from the assumptions the Administering Authority has used after consulting with the Employers, then the projected future funding level will be different from the level described above.

To illustrate how sensitive the funding level is to experience being different from assumed, the table below shows how the valuation results at 31 March 2020 would have differed given small changes in the key assumptions. These sensitivities have no regard to the subsequent buy-in.

Assumption change	Increase/(Reduction) in surplus at 31 March 2020 (£m)	Resultant surplus /(deficit) at 31 March 2020 (£m)
Original solvency funding position	**-**	**37**
Real investment return 0.25% lower than assumed	-10	27
Long term improvement rate in life expectancy increased by 0.25% per annum	-2	35
Fund Assets at valuation date fall by 5%	-15	22

Appendices

Appendix A
Assumptions

How the benefits are valued

In order to calculate the liabilities, there is a need to make assumptions about various factors that affect the cost of the benefits provided by the Fund – for example, how long members will live, or the future level of inflation. The table below explains the key assumptions being made in the valuation.

Assumption	Why it is important and how it impacts on the liabilities
Discount rate	The majority of benefits in a pension fund are paid many years in the future. In the period before the benefits are paid, the Administering Authority invests the funds held by the Fund with the aim of achieving a return on those funds. When calculating how much money is needed now to make these benefit payments, it is appropriate to make allowance for the investment return that is expected to be earned on these funds. This is known as “discounting”. The higher the investment return achieved, the less money needs to be set aside now to pay benefits. The calculation reflects this by placing a lower value on the liabilities if the “discount rate” is higher.
Inflation	Pensions in payment increase in line with Consumer Price Inflation (CPI). Salary growth is also normally linked to price inflation in the long term. A higher inflation assumption will, all other things being equal, lead to a higher value being placed on the liabilities.
Pensionable Salary growth	Benefits earned prior to 1 April 2015 for active members are based on their salaries immediately before retirement, so it is necessary to make an assumption about future Pensionable Salary growth. The higher this assumption, the higher the value placed on the liabilities for active members.
Life expectancy	Pensions are paid while the member (and potentially their spouse or partner) is alive. The longer people live, the greater is the cost of providing a pension. Allowing for longer life expectancy therefore increases the liabilities.

The liabilities of the Fund are calculated by projecting forward all of the future benefit cash flows and discounting them back to the effective date of the valuation, using these assumptions. For example, the liability for a single pensioner is calculated by estimating the amount of each pension payment they will receive in the future, multiplying by the probability that the member will still be alive by the date of each payment, and then discounting each payment back to the effective date of the valuation using the appropriate discount rate, and then summing up all of these discounted amounts. The liabilities for the whole Fund are calculated by summing the liabilities for each of the individual members.

Financial assumptions used to calculate the solvency funding target

The table below summarises the key financial assumptions used in the calculation of the solvency funding target at whole Fund level and those used for the 31 March 2017 actuarial valuation. Section 1 of this report sets out how these assumptions might vary from one employer to another.

Financial assumptions	31 March 2020	31 March 2017*
Discount rate	0.7% p.a.	1.6% p.a.
Price inflation (CPI)	Set equal to RPI less 1% p.a. pre 2030 and RPI post 2030, this is broadly equivalent to a single equivalent CPI over the term of the liabilities of 2.25% p.a.	First Aberdeen 2.9% p.a. First Glasgow 2.4% p.a.
Salary increases (short term)	n/a	First Aberdeen 2.4% p.a. until 31 March 2018 First Glasgow n/a
Salary increases (long term)	First Aberdeen CPI plus 0.5% First Glasgow CPI plus 1.375% Broadly equivalent to: First Aberdeen 2.75% p.a. First Glasgow 3.625% p.a.	First Aberdeen 3.4% p.a. First Glasgow 3.775% p.a.
Pension increases in payment:	Broadly 2.25% p.a.	First Aberdeen 2.9% p.a. First Glasgow 2.4% p.a.

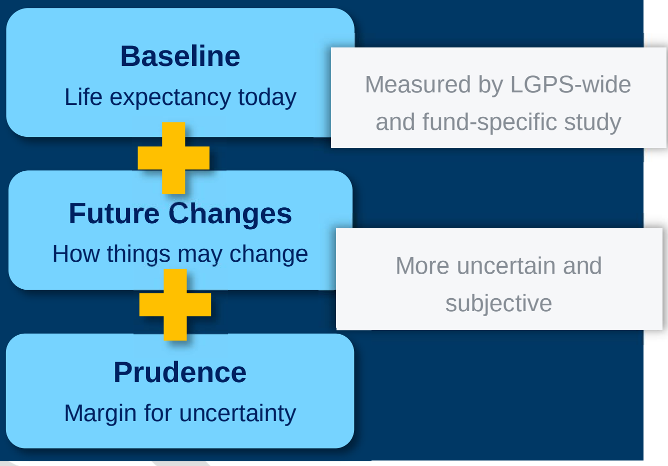
**approximate for First Glasgow -see the valuation report for the Strathclyde No3 Pension Fund for further details*

Demographic assumptions used

Post-retirement Mortality

There are two separate decisions on mortality assumptions:

- The baseline table for the current rates of mortality; and
- The allowance for future improvements.



Mortality (or life expectancy) tables are typically made up of three elements: a baseline table (equivalent to the expected current mortality), an allowance for future improvements, and a margin for prudence. Very few pension funds are large enough for them to be able to determine a bespoke set of baseline assumptions based purely on the fund's own membership experience. Typically, the life expectancy assumptions are set by benchmarking a fund's membership profile and mortality experience against larger external datasets. For this actuarial valuation, we have benchmarked the Fund's membership profile and experience against the "S tables" published by the CMI. We have applied weightings as appropriate to adjust the standard tables so as to arrive at assumptions which are appropriate for the Fund. We have generally used the S3PA tables ("middle" tables for females), other than for female dependants where the S3DA tables have been used and for members retiring in ill health where the S3IA tables have been used. At the ACCTF 2017 actuarial valuation the S2PA tables were used (S2DA tables for female dependants).

Future improvements are assumed to follow the CMI 2019 model with a 1.75% p.a. long-term improvements trend. At the 2017 actuarial valuation the CMI 2015 model with 1.75% p.a. long-term trend was used.

The weightings and age ratings applied to the above are set out in the table below.

Current Status	Retirement Type	Weighting – First Aberdeen members 31 March 2020	Weighting – First Glasgow members 31 March 2020	Weighting/age rating 31 March 2017 ACCTF valuation*
Annuitant	Normal Health	108% males, 88% females	117% males, 94% females	109% males, 87% females
	Dependant	100% males, 104% females	145% males, 111% females	136% males, 118% females
	Ill Health	132% males, 149% females	137% males, 150% females	109% males, 87% females (+3 age rating)
	Future Dependant	128% males, 112% females	139% males, 119% females	128% males, 100% females
Active	Normal Health	112% males, 115% females	112% males, 86% females	99% males, 109% females
	Ill Health	128% males, 169% females	128% males, 131% females	99% males, 109% females (+4 age rating)
Deferred	All	143% males, 102% females	136% males, 110% females	135% males, 97% females
Active/ deferred	Future Dependant	137% males, 121% females	140% males, 120% females	128% males, 100% females

** Only in respect of First Aberdeen Limited as a participating employer in the ACCTF. See the valuation report for the Strathclyde No3 Pension Fund in respect of First Glasgow Limited.*

A weighting applied to an actuarial table has the effect of increasing or reducing the chance of survival at each age, which increases or reduces the corresponding life expectancy. Similarly, an age rating applied to an actuarial table has the effect of assuming that beneficiaries have a life expectancy equal to those older (or younger) than their actual age.

The mortality assumptions used for the 31 March 2020 valuation result in the following life expectancies:

	Male Life Expectancy at 65		Female Life Expectancy at 65	
	First Aberdeen	First Glasgow	First Aberdeen	First Glasgow
Pensioners	21.9	21.3	25.2	24.7
Actives aged 45 now	23.6	23.6	25.3	27.4
Deferreds aged 45 now	21.7	22.1	26.2	25.6

Pre-retirement Mortality

The following mortality tables (together with any appropriate weightings) have been adopted for mortality rates in the period up to retirement.

	31 March 2020	31 March 2017
Base Table	DxL08 tables with adjustments of 80% (male) 50% (female) to reflect the Fund's membership profile	DxL08 tables with adjustments of 80% (male) 50% (female) to reflect the Fund's membership profile
Allowance for Future Improvements	CMI_2015 [1.5%]	CMI_2015 [1.5%]

Commutation

It has been assumed that, on average, 50% of retiring members will take the maximum tax-free cash available at retirement and 50% will take a 3/80ths cash sum (the standard for pre April 2008 service). Members have the option to commute part of their pension at retirement in return for a lump sum at a rate of £12 cash for each £1 per annum of pension given up.

Retirement lump sums are less costly for the Fund to provide than the alternative pension, as members receive only £12 of each £1 p.a. of pension given up. If members take the cash sum option at a higher rate than has been assumed then this will normally lead to an improvement in the funding level.

Early retirement

If members take early retirement to a greater extent than has been assumed then this will typically lead to a worsening of the funding level. This is because many members are able to take substantial parts of their benefits from age 60 without them being reduced for early payment.

Some members are entitled to receive their benefits (or part of their benefits) unreduced from an age prior to the Fund's normal pension age under the "Rule of 85" provisions of the Regulations. This age will be at some point between ages 60 and 65, depending on the length of a member's pensionable service.
The calculations in respect of the relevant service to which these terms apply (basically pre April 2008 service but with transitional protections for certain members) allow for members to retire at this age.

For post April 2008 service (other than protected service) the situation is different since the "Rule of 85" has been removed (and for post December 2006 service for new entrants to the Scheme from that date). For this service we have assumed the earliest age at which unreduced benefits become an entitlement is 65, except for those members who have protected status under the transitional provisions.

For post April 2015 service, early retirement factors are applied where the retirement age described above is below the member's eligible retirement age for unreduced benefits for post April 2015 service. Factors are in line with the standard scheme factors produced by the Government Actuary's Department.

No allowance has been made for non-ill health early retirements prior to the ages specified above. Additional capital contributions will be paid by employers in respect of the cost of these retirements.

However, for those members who are entitled to receive their accrued benefits (or part of those benefits) prior to the retirement age described above and who are over this age but under 65, a proportion of the active membership is assumed to retire in normal health prior to age 65, as set out below:

	% retiring per annum	% retiring per annum
Age	Males	Females
60	10	20
61	8	15
62	8	15
63	8	15
64	8	15
65	100	100

The appropriate early retirement factors applied to the relevant tranche of benefits are in line with the Government Actuary's Department (GAD) guidance.

Ill health retirement

A small proportion of the active membership has been assumed to retire owing to ill health. As an example of the rates assumed, the following is an extract from the decrement table used:

The level of ill-health retirement benefit provided for a member falls into one of two “tiers”, depending on whether and when the member might be expected to resume gainful employment. Tier 1, for example, is on the basis that the member is unlikely to be able to do so before Normal Pension Age. Full details are set out in the LGPS (Scotland) Regulations and associated guidance.

	% retiring per annum	% retiring per annum
Age	Males	Females
35	0.09	0.08
45	0.26	0.24
55	1.14	1.00

The proportion of ill health early retirements falling into each tier category, split by males and females, has been assumed to be as set out below:

Tier 1	Tier 2
86%	14%

Withdrawal

This assumption relates to those members who leave the scheme with an entitlement to a deferred pension or transfer value. It has been assumed that active members will leave the Scheme at the following sample rates:

In relation to pre 2015 benefits, deferred benefits tend to be less costly for the Fund to provide than if the member had remained in the Fund until retirement. If the number of members leaving the Fund is greater than expected then this will typically lead to a slight improvement in the funding level.

	% leaving per annum	% leaving per annum
Age	Males	Females
25	20.25	22.38
35	5.09	6.27
45	2.54	3.89

Partners' and Dependants' Proportions

It has been assumed that the proportions of members below will
on death give rise to a dependant's pension (spouse's and partner's), and that spouses/partners of female (male) members are three years older (younger), on average than the member.

	% spouse/partner	% spouse/partner
Age	Males	Females
25	45	57
35	73	75
45	76	75
55	78	75
65	80	69

> If more members than assumed have partners then this will lead to an increase in the number of dependants pensions coming into payment over and above that expected. This would lead to a worsening of the funding level.

Assumptions used to calculate the Primary Contribution Rate

The cost of future accrual (the Primary Contribution Rate) has been calculated using the same actuarial assumptions as used to calculate the solvency funding target and recovery plan as set out above.

Appendix B
Summary membership data

The membership data is summarised in the tables, with figures at the previous valuation shown for comparison.

Data in relation to members of the Fund were supplied by the Fund's administrator on behalf of the Administering Authority (2017 First Glasgow data taken from the Strathclyde No3 Pension Fund valuation report). The accuracy of the data provided has been relied on. While reasonableness checks on the data have been carried out, they do not guarantee the completeness or the accuracy of the data. Consequently, Mercer does not accept any liability in respect of its advice where it has relied on data that is incomplete or inaccurate.

First Aberdeen Limited

	31 March 2017	31 March 2020
Active members		
Number	61	32
Total Pensionable Salaries (£000s p.a.)	1,695	932
Average Pensionable Salary (£ p.a.)	27,788	29,124
Average age (weighted by pension)	55.7	56.5
Deferred pensioners (including undecideds)		
Number	132	109
Total deferred pensions revalued to valuation date (£000s p.a.)	391	331
Average deferred pension (£ p.a.)	2,964	3,039
Average age (weighted by pension)	53.9	54.5
Current Pensioners and Dependants		
Number	424	428
Total pensions payable (£000s p.a.)	3,078	3,416
Average Pension	7,259	7,982
Average age (weighted by pension)	70.9	72.1

Pensions are gross of the pre 86 pension increases recharged to the North East Scotland Pension Fund.

First Glasgow Limited

	31 March 2017	31 March 2020
Active members		
Number	118	45
Total Pensionable Salaries (£000s p.a.)	2,983	1,372
Average Pensionable Salary (£ p.a.)	25,280	30,498
Average age (weighted by pension)	57.8	57.9
Deferred pensioners (including undecideds)		
Number	114	79
Total deferred pensions revalued to valuation date (£000s p.a.)	430	317
Average deferred pension (£ p.a.)	3,772	4,007
Average age (weighted by pension)	56.3	58.6
Current Pensioners and Dependants		
Number	897	944
Total pensions payable (£000s p.a.)	5,340	6,196
Average Pension	5,953	6,563
Average age (weighted by pension)	66.3	70.0

Appendix C
Assets

The market value of the Fund's assets was c£309m on the valuation date.

The Administering Authority's investment strategy is to proportion the Fund's assets by asset class as shown in the table below (this is subject to a strategy review following the buy-in which occurred after the valuation date). The actual distribution of assets will vary over time due to changes in financial markets.

	Investment strategy
	%
Index linked Gilts	70%
Cash	30%
Total	100%

The Administering Authority also holds additional voluntary contributions (AVCs) which are separately invested. These assets have been excluded from the market value shown as they exactly match the value of the benefits they cover.

The details of the assets at the valuation date and the financial transactions during the inter-valuation period have been obtained from the audited accounts for the Fund.

Appendix D
Scheme Benefits

The benefits valued within our calculations are those in force at the effective date of the valuation. Full details of these can be found in the Local Government Pension Scheme (Scotland) Regulations 2018 (as amended). The principal details are as follows:

The Local Government Pension Scheme (Scotland) Regulations 2018 (https://www.legislation.gov.uk/ssi/2018/141/contents)

The Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014 (https://www.legislation.gov.uk/ssi/2014/233/contents/made)

Directions made by the Treasury under Section 59A of the Social Security Pensions Act 1975 (https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/761639/Treasury_Direction_under_section_59A_Social_Security_Pensions_Act_1975.pdf) and recent consultation on future treatment (https://www.gov.uk/government/consultations/public-service-pensions-guaranteed-minimum-pension-indexation-consultation). We have also assumed that that the directions will ultimately be extended to require the LGPS to become responsible for increases to GMPs for **all** members reaching State Pension Age after 5 April 2016.

The Fund is also responsible for paying and, where appropriate, recharging to employers the benefits arising from the award of compensatory added years (CAY) of service on premature retirement. Unless these CAY benefits have been converted into “funded” benefits, they are normally recharged to the relevant employer (together with associated pension increases), and so are excluded from the valuation.

The benefits that will emerge from money purchase AVCs paid by members, and SCAVCs paid by employers, and the corresponding invested assets in respect of these AVCs and SCAVCs, have been excluded from the valuation.

UK and European law requires pension schemes to provide equal benefits to men and women in respect of service after 17 May 1990 (the date of the “Barber” judgment) and this includes providing equal benefits accrued from that date to reflect the differences in GMPs. Following the Lloyds Bank case in 2018, HM Treasury has issued a consultation on equalising and indexation of GMPs in all the public service pension schemes, including the LGPS, and discussions are ongoing about the extent of any inequalities and how these might be addressed.

The valuation makes no allowance for removal of these inequalities. It is consequently possible that additional funding will be required for equalisation once the law has been clarified. It is recommended that the Administering Authority seek further legal advice if it is concerned about this issue.

The McCloud Judgment

The McCloud judgment in the LGPS refers to the legal decisions (initially by the Employment Appeal Tribunal and then ratified by the Court of Appeal) in the Sargeant/McCloud cases for the Fire and Judiciary pension arrangements. The Court ruled that transitional protections afforded to older members when these schemes were amended constituted unlawful age discrimination. Remedial action, in the form of benefit changes for these schemes, will therefore be required.

Although the above cases did not relate directly to the LGPS, the LGPS also put in place protections for older members as part of the reforms which came into effect from 2015. For the LGPS these took the form of an underpin, where older members would get the better of the benefits payable under the new and old schemes. The UK Government set out a proposed remedy in a consultation in July 2020, which broadly would ensure that all members who were in the LGPS before 31 March 2012 would be granted the statutory underpin protection for all service up to 31 March 2022.

As advised by the SPPA and following discussions with the Administering Authority, in order to consider a reasonable provision for the potential costs in employer contributions we have valued the cost of McCloud to be the estimated cost of providing the underpin set out above to all members. More specifically we have agreed with the Administering Authority to:

- Estimate the underpin benefits for members for service after 31 March 2015 (when the new scheme took effect) who joined the Fund before 2012.
- Compare this to the actual post 31 March 2015 benefits.
- Calculate the cost for each member as the value of the underpin benefits less the value of the actual benefits (ignoring members where the value of the actual benefits is higher).
- Sum these costs across all members to give the impact of the underpin for each employer.

We have calculated this cost across all benefits (including deferred benefits for active members who are assumed to leave the scheme before retirement in the future).

Further detail on the proposed remedy can be found in the below consultation document:

https://www.lgpslibrary.org/assets/cons/lgpsscot/20200731CD.pdf

Appendix E

Analysis of Membership Experience

The analysis below compares the actual experience over the 3 year period for both employers with the assumptions used for the 2020 valuation.

	Actual	Expected	%
Ill Health Retirements	4	9	43
Withdrawals	15	2	750
Pensioner Deaths (lives)	142	93	152
Pensioner Deaths (£000 p.a. of pension)	635	501	127

Note that actual withdrawals can include members moving to another LGPS Fund, bulk transfers and also transfers under the special transfer club terms.

Appendix F
Rates and Adjustments Certificate issued in accordance with Regulation 60

Name of fund	Aberdeen City Council Transport Fund

Primary Contribution Rate

I hereby certify that, in my opinion, the primary rate of the employers' contribution for the whole Fund for each of the three years beginning 1 April 2021 is 43.7% of pensionable pay plus £140,000 p.a. in respect of expenses.

The primary rate of contribution for each employer for the three year period beginning 1 April 2021 is set out in the attached schedule.

Secondary Contribution Rate

I hereby certify that, in my opinion, the secondary rate of the employer's contribution for the whole Fund for each of the three years beginning 1 April 2021 is as follows:

2021/22 -43.7% of pensionable pay less £140,000

2022/23 -43.7% of pensionable pay less £140,000

2023/24 -43.7% of pensionable pay less £140,000

The secondary rate of contribution for each employer for each of the three years beginning 1 April 2021 is set out in the attached schedule. The above secondary rates, and the secondary rates for each employer, include a provision for the costs of the McCloud judgment as set out in the notes to Appendix G.

Contribution amounts payable

The total contribution payable for each employer is the total of the primary and secondary rates as detailed in the attached schedule. Contributions will be paid monthly in arrears with each payment normally being due by the 19th of the following month (or the 22nd if paid electronically) or at intervals agreed with the Administering Authority unless otherwise noted in the schedule.

Further adjustments

A further individual adjustment shall be applied in respect of each non-ill health early retirement occurring in the period of three years covered by this certificate. This further individual adjustment will be calculated in accordance with methods agreed from time to time between the Fund's Actuary and the Administering Authority.

The contributions set out in the attached schedule represent the minimum contribution which may be paid by each employer in total over the 3 years covered by the certificate. Additional contributions or a different pattern of contributions may be paid if requested by the employer concerned at the sole discretion of the Administering Authority as agreed with the Actuary. The total contributions payable by each employer will be subject to a minimum of nil%.

The individual employer contributions may be varied as agreed by the Actuary and Administering Authority to reflect any changes in contribution requirements as a result of the McCloud judgment remedy as set out in this report and/or any benefit costs being insured with a third party or parties including where the third party or parties participate in the Fund.

In cases where an element of an existing employer's surplus or deficit is transferred to a new employer on its inception, the existing employer's secondary contributions, as shown on the schedule to this Certificate in Appendix G, may be reallocated between the existing employer and the new employer to reflect this, on the advice of the Actuary and as agreed with the Administering Authority so that the total payments remain the same overall.

The Administering Authority and employer with advice from the Fund's Actuary can agree that contributions payable under this certificate can be sourced under an alternative financing arrangement which provides the Fund with equivalent cash contributions.

Regulation 60(8)

No allowance for non-ill health early retirements has been made in determining the results of the valuation, on the basis that the costs arising will be met by additional contributions. Allowance for ill health retirements has been included in each employer's contribution rate, on the basis of the method and assumptions set out in the report.

Signature:		
Name:	Paul Middleman	Laura Evans
Qualification:	Fellow of the Institute and Faculty of Actuaries	Fellow of the Institute and Faculty of Actuaries
Date of signing:	29 March 2021	

Appendix G

Schedule to the Rates and Adjustments Certificate dated 31 March 2021

Employer	Primary rate 2021/22 to 2023/24	Secondary rates			Total Contribution rates		
		2021/22	2022/23	2023/24	2021/22	2022/23	2023/24
First Aberdeen Limited (801)	44.6% plus £60,000	-44.6% plus £60,000			nil	nil	nil
First Glasgow Limited (802)	43.2% plus £80,000	-43.2% plus £80,000			nil	nil	nil

Important notes to the Certificate:

1. The percentages shown are percentages of pensionable pay and apply to all members, including those who are members under the 50:50 option under the LGPS.

2. Where the secondary rate is a deduction to the primary rate due to an employer being in surplus, the total annual contributions payable by each employer will be subject to a minimum of nil % i.e. no monies can be refunded to an employer whilst they participate in the Fund.

3. The above primary and secondary contributions include provision for the estimated effect of the McCloud judgment based on the proposed remedy set out in the 2020 Government consultation. Once the final remedy for McCloud is known, the position will be reviewed.

4. Separate payments will be made from the North East Scotland Pension Fund to the Aberdeen City Council Transport Fund in relation to pension increases payable to retired members relating to benefits accrued prior to 26 October 1986, unless capitalised via a one off payment as agreed with the Administering Authority of both Funds and First Aberdeen Limited which results in the ceasing of the arrangement. Any required recharge amounts will be calculated by the Fund separately where appropriate.

Appendix H

Glossary

Actuarial Valuation: an investigation by an actuary into the ability of the Fund to meet its liabilities. For the LGPS the Fund Actuary will assess the funding level of each participating employer and agree contribution rates with the administering authority to fund the cost of new benefits and make good any existing deficits as set out in the separate Funding Strategy Statement.

Administering Authority: the council with a statutory responsibility for running the Fund and that is responsible for all aspects of its management and operation.

Best Estimate Assumption: an assumption where the outcome has a 50/50 chance of being achieved.

Bonds: loans made to an issuer (often a government or a company) which undertakes to repay the loan at an agreed later date. The term refers generically to corporate bonds or government bonds (gilts).

Career Average Revalued Earnings Scheme (CARE): with effect from 1 April 2015, benefits accrued by members in the LGPS take the form of CARE benefits. Every year members will accrue a pension benefit equivalent to 1/49th of their pensionable pay in that year. Each annual pension accrued receives inflationary increases (in line with the annual change in the Consumer Prices Index) over the period to retirement.

CPI: acronym standing for "Consumer Prices Index". CPI is a measure of inflation with a basket of goods that is assessed on an annual basis. The reference goods and services currently differs from those of RPI. These goods are expected to provide lower, less volatile inflation increases. Pension increases in the LGPS are linked to the annual change in CPI.

CPIH: An alternative measure of CPI which includes owner occupiers' housing costs and Council Tax (which are excluded from CPI).

Deficit: the extent to which the value of the Fund's past service liabilities exceeds the Fund's assets.

Discount Rate: the rate of interest used to convert a cash amount e.g. future benefit payments occurring in the future to a present value.

Employer Covenant: the degree to which an employer participating in an occupational pension scheme is willing and able to meet the funding requirements of the scheme.

Employer's Future Service Contribution Rate: the contribution rate payable by an employer, expressed as a % of pensionable pay, as being sufficient to meet the cost of new benefits being accrued by active members in the future. The cost will be net of employee contributions and will include an allowance for the expected level of administrative expenses. It is normally the same as an employer's Primary Contribution Rate under the Regulations.

Employer's Primary Contribution Rate: the contribution rate required to meet the cost of the future accrual of benefits including ancillary, death in service and ill health benefits together with administration costs. It is expressed as a percentage of pensionable pay, ignoring any past service surplus or deficit, but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer's covenant. The Primary Contribution Rate for the whole Fund is the weighted average (by payroll) of the individual employers' Primary Contribution Rates.

Employer's Secondary Contribution Rate: an adjustment to the Primary Rate to reflect any past service deficit or surplus, to arrive at the rate each employer is required to pay. The Secondary Rate may be expressed as a percentage adjustment to the Primary Rate, and/or a cash adjustment in each of the three years beginning 1 April in the year following that in which the valuation date falls. The Secondary Rate is specified in the Rates and Adjustments Certificate. For any employer, the rate they are actually required to pay is the sum of the Primary and Secondary Rates. Secondary Rates for the whole fund in each of the three years shall also be disclosed. These will be calculated as the weighted average based on the whole fund payroll in respect of percentage rates and as a total amount in respect of cash adjustments.

Equities: shares in a company which are bought and sold on a stock exchange.

Funding or solvency Level: the ratio of the value of the Fund's assets and the value of the Fund's liabilities expressed as a percentage.

Funding Strategy Statement (FSS): This is a key governance document that outlines how the Administering Authority will manage employer's contributions to the Fund.

Guaranteed Minimum Pension (GMP): This part of a member's pension which was earned between 6 April 1978 and 5 April 1997 and which replaces part of that member's State Scheme benefits in respect of that period.

Investment Strategy: the long-term distribution of assets among various asset classes that takes into account the Funds objectives and attitude to risk.

Liabilities: the actuarially calculated present value of all benefit entitlements i.e. Fund cashflows of all members of the Fund, built up to date or in the future. The liabilities in relation to the benefit entitlements earned up to the valuation date are compared with the present market value of Fund assets to derive the deficit and funding/solvency level. Liabilities can be assessed on different set of actuarial assumptions depending on the purpose of the valuation.

McCloud Judgment: This refers to the linked legal cases of Sargeant and McCloud, and which found that the transitional protections (which were afforded to older members when the public service pension schemes were reformed in 2014/15) constituted unlawful age discrimination.

Past Service Liabilities: this is the present value of the benefits accrued by members up to the valuation date. It is assessed based on a set of assumptions agreed between the Administering Authority and the Actuary.

Percentile: A method of ranking a series of outcomes. For example, a 10th percentile outcome means that only 10% of results would be expected to be as good as or better than the 10th percentile and 90% of results would be expected to be worse.

Present Value: the value of projected benefit payments, discounted back to the valuation date.

Prudent Assumption: an assumption where the outcome has a greater than 50/50 chance of being achieved i.e. the outcome is more likely to be overstated than understated. Legislation and guidance requires the assumptions adopted for an actuarial valuation overall to be prudent.

Real Return or Real Discount Rate: a rate of return or discount rate net of CPI inflation.

Recovery Plan: a strategy by which an employer will make up a funding surplus/deficit over a specified period of time (“the spread period”), as set out in the FSS.

SAB Funding Basis or SAB Basis: a set of actuarial assumptions determined by the LGPS Scheme Advisory Board (SAB). Its purposes are to set out the funding position on a standardised approach so that comparisons can be made with other LGPS Funds, and to assist with the “Section 13 review” as carried out by the Government Actuary’s Department. As an example, the real discount rate over and above CPI used in the SAB Basis as at 31 March 2020 was 2.4% p.a., so it can be substantially different from the actuarial assumptions used to calculated the Fund’s solvency funding position and contribution outcomes for employers.

Solvency/Funding Level: the ratio of the value of the Fund’s assets and the value of the Fund’s liabilities expressed as a percentage.

Solvency Funding Target: an assessment of the present value of benefits to be paid in the future. The desired funding target is to achieve a solvency level of a 100% i.e. assets equal to the past service liabilities assessed on the ongoing concern basis.

Spread Period: a strategy by which the Fund will remove a funding surplus via contribution adjustments over a specified period of time (“the spread period”), as set out in the FSS.

50/50 Scheme: in the LGPS, active members are given the option of accruing a lower benefit in the 50/50 Scheme, in return for paying a lower level of contribution.

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ABERDEEN CITY COUNCIL

COMMITTEE	Pensions Committee
DATE	26 March 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	Statement of Accounts 2020/21 – Action Plan
REPORT NUMBER	PC/MAR21/ACCOUNTS
DIRECTOR	Steven Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHOR	Laura Colliss
TERMS OF REFERENCE	3.1

1. PURPOSE OF REPORT

1.1 The purpose of this report is to provide Elected Members with high level information and key dates to the 2020/21 Statement of Accounts including linkages to the plans and timetables of the Council's External Auditors.

2. RECOMMENDATION

2.1 That the Committee note the report for assurance.

3. BACKGROUND

3.1 The Statement of Accounts 2020/21 will summarise the Pension Fund's transactions for the period 1 April to 31 March and its financial position at the year end 31 March 2021. It will be prepared in accordance with the Internal Financial Reporting Standards (IFRS) based Code of Practice on Local Authority Accounting in the United Kingdom (the Code) and the Service Reporting Code of Practice (SeRCOP). There are no changes to either of the codes in 2020/21 which will have any significant impact on the Statement of Accounts.

3.2 There are a number of key dates and these are summarised as follows:

31 March 2021	End of Financial Year 2020/21
17 June 2021	Deadline for giving notice to the public of the right to inspect and object to Accounts
25 June 2021	Pensions Committee
30 June 2021	Statutory deadline for submission of Draft Statement of Accounts to the Controller of Audit
July 2021	Advertising and Inspection of Accounts
31 July 2021	Deadline for submission of the Whole of Government Accounts (WGA) to the Scottish Government
17 September 2021	Pensions Committee
30 September 2021	Deadline for submission of Audited Statement of Accounts to the Controller of Audit

31 October 2021	Deadline for submission of the Audited WGA to the Scottish Government
10 December 2021	Pensions Committee

3.3 25 June 2021

The Pensions Committee will receive the Draft Statement of Accounts 2020/21, including the Annual Report for overall scrutiny.

3.4 July 2021

This is the period within which the Council must give public notice of the rights of interested parties to inspect and object to its accounts. There are statutory requirements currently under The Local Authority Accounts (Scotland) Regulations 2014 which define the notice period, the inspection period, deadline for submission of any objections and the information which must be made available for inspection.

3.5 17 September 2021

The Pensions Committee will receive Audit Scotland's combined ISA260 and 'Report to those charged with the governance of the 2020/21 audit' for debate and consideration, together with the Audited Statement of Accounts 2020/21 for signing.

4. FINANCIAL IMPLICATIONS

4.1 There are no direct financial implications arising from the recommendation in this report.

5. LEGAL IMPLICATIONS

5.1 There is a statutory requirement for the Council to produce both a draft and audited Statement of Accounts within certain timescales and to a high standard. This is a major task which requires co-operation and input from a large number of people across all services of the Council. It is only with the commitment of all staff that these high standards and deadlines can be met.

6. MANAGEMENT OF RISK

6.1 The Pension Fund maintains its own Risk Management Policy and regularly updates its Risk Register in line with change. This is reported quarterly to the Pensions Committee.

7. OUTCOMES

7.1 The proposals in this report have no impact on the Council Delivery Plan.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

None

10. APPENDICES

None

11. REPORT AUTHOR CONTACT DETAILS

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ABERDEEN CITY COUNCIL

COMMITTEE	Pensions Committee
DATE	26 March 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	Review of NESPF Compliance with the Public Service Pensions Act 2013 (PSPA 2013) and Pension Regulator Requirements
REPORT NUMBER	PC/MAR21/GOV
DIRECTOR	Steven Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHOR	Mairi Suttie
TERMS OF REFERENCE	4.1 and 4.2

1. PURPOSE OF REPORT

1.1 To provide Elected Members with a review of the North East Scotland Pension Fund's (the 'Fund') compliance with the Public Service Pensions Act 2013 (PSPA) and the Pensions Regulator ('tPR') requirements during the financial year 2020/21.

2. RECOMMENDATION

2.1 That the Committee note the assurance provided in the report.

3. BACKGROUND

GOVERNANCE FRAMEWORK REVIEW

3.1 A review of the Fund's governance framework is conducted on an annual basis. The purpose of the review is to assess current practices and procedures; ensuring the Fund has in place a robust governance framework and complies with legislation and best practice guidance.

3.2 In terms of Scheme compliance with legislation such as the Local Government Pension Scheme (Scotland) Regulations, the Public Sector Pensions Act 2013 and tPR requirements (as set out in Code of Practice 14 Governance and Administration of Public Sector Pension Schemes) a review is carried out on a six monthly basis by Fund officers with annual reporting to the Pensions Committee.

Pension Board

3.3 The NESPF Pension Board is made up of equal numbers of member (4) and employer (4) representatives as follows:

- 1 x Aberdeen City Council

- 1 x Aberdeenshire Council
- 1 x The Moray Council
- 1 x Scheduled/Admitted Bodies
- 1 x Unison
- 1 x Unite
- 1 x GMB
- 1 x UCATT

3.4 The role of the local pension board is to assist the Scheme Manager to:

- ensure effective and efficient governance and administration of the Local Government Pension Scheme (LGPS); and
- ensure compliance with the LGPS (Scotland) Regulations and other relevant legislation, together with any requirements imposed by tPR.

3.5 The Pension Board has a monitoring, assisting and reviewing purpose rather than being a decision-making body. In so doing, the Pension Board is helping to manage the reputational risk of the Fund, and of the administering authority.

Meeting Attendance

3.6 During 2020/21 the Pension Board met formally (and concurrently with the Pensions Committee on):

11 September 2020
11 December 2020
26 March 2021

Following the COVID 19 outbreak, all Council Committees were suspended with effect from March 2020. This included the scheduled June meeting of the Pensions Committee and Board. Instead Urgent Business Committees were held to determine business of an urgent nature. The June meeting of the UBC was attended by a number of Pensions Committee members for the consideration of the NESPF Unaudited Annual Report and Accounts 2019/20 but due to the unprecedented times, Board members were not present. However they were kept up to date on what was agreed during the UBC by Officers. Pensions Committee and Board meetings resumed from September 2020, taking place in a hybrid manner to allow virtual participation in line with Scottish Government travel restrictions and work from home guidance.

3.7 During 2020/21 there was an overall **94%** attendance rate at meetings (up to December 2020).

High attendance levels, and active participation at both the quarterly meeting and training events, demonstrate a strong commitment to the ongoing effectiveness of the NESPF Pension Board. In addition, low turnover of members ensures knowledge and experience is retained.

3.8 The table below details meeting attendance during 2020/21:

	29/09/2020	11/12/2020	26/03/2021*	Individual
Cllr Allan	✓	✓	✓	**100%**
Cllr McKelvie	✓	✓	✓	**100%**
Cllr Cowe	✓	✓	✓	**100%**
Morag Lawrence	✓	✓	✓	**100%**
Ian Hodgson	X	✓	✓	**50%**
Alan Walker	✓	✓	✓	**100%**
Neil Stirling	✓	✓	✓	**100%**
Liam Knox	✓	✓	✓	**100%**

*projected attendance, to be confirmed in Committee Effectiveness Report to December 2021 meeting
** Mr Hodgson joined the Board on 8 September 2020.

Training Attendance 2020/21

3.9 It is a statutory requirement under Schedule 4 of the PSPA 2013 that members of local pension boards have ‘knowledge and understanding’ of pensions law and are ‘conversant’ with Scheme regulations and Fund documents. The issue of training is approached carefully by both the administering authority and individual Board members.

3.10 The Board normally meets in June to review their annual report. This provides an opportunity for any issues around attendance to be addressed or gaps in training knowledge to be discussed. Due to COVID-19 the June meeting of the Pension Board did not take place in person. Instead the annual report was issued electronically for review and approval and members were given the opportunity to appoint a new Chair and Vice Chair for 2020/21.

3.11 During 2020/21 Pension Board members have continued to demonstrate a commitment to developing their ‘knowledge and understanding’ by attending training events virtually covering key areas, with particular focus on ESG (environmental, social and governance) and Scheme governance.

3.12 Fund officers maintain a training register to allow attendance to be monitored on an ongoing basis. The Training Policy, approved by Committee and reviewed annually, sets out review arrangements to address poor attendance or failure to achieve/maintain the required level of knowledge and understanding.

3.13 The table below details training attendance for 2020/21 to date:

	Intro	22/23 Oct	1 Oct	8 Oct	Total
Cllr Allan		x	x	x	0
Cllr McKelvie		✓	✓	✓	3
Cllr Cowe		x	✓	✓	2
Ian Hodgson	✓	x	x	x	1
Morag Lawrence		✓	✓	✓	3
Alan Walker		✓	x	✓	2
Neil Stirling		✓	✓	✓	3
Liam Knox		x	✓	x	1

3.14 Board members are expected to carry out an annual personal assessment of their knowledge and understanding and ensure they are meeting the requirements of the Training Policy.

Costs of Operation 2020/21

3.15 The costs and expenses of the Pension Board are met as part of the administration costs of the Fund. The Pension Board carries out its role in a cost effective manner, mindful of delivering value for money.

3.16 Under normal circumstances the costs and expenses of the Pension Board are principally travel related expenses to attend meetings and training events. Due to COVID-19 all training in 2020/21 took place virtually, with the joint Pensions Committee and Board meetings also taking place in a hybrid manner (in person and virtually).

3.17 As a result there were no costs associated with the Pension Board during 2020/21.

3.2 **COMPLIANCE REVIEW**

3.2.1 A compliance review is carried out by the Pension Funds on a six monthly basis, with annual reporting to the Pensions Committee.

3.2.2 Again the review found that the key internal controls for monitoring the ongoing compliance with legislation and tPR requirements are in place and working effectively with the latest compliance review taking place in December 2020. A further review using tPR's Scheme Assessment Tool confirmed there are no areas for concern.

3.2.3 Work is ongoing within the Fund to ensure it continues to meet legislative and tPR requirements.

<u>Elected Member and Board Knowledge and Understanding</u>

3.2.4 As per the Pensions Regulator Code of Practice 14, Pension Board members must have knowledge and understanding of the law relating to pensions, and any other matters which are prescribed in regulations. The degree of knowledge and understanding required is that appropriate for the purposes of enabling the individual to properly exercise the functions of a member of the Pension Board.

3.2.5 The Pension Fund launched a brand new website in Summer 2020, which included a redesigned secure area for the Pensions Committee and Board to access information and training materials. This resource will continue to be developed during 2021/22 to assist members to maintain and further their knowledge and understanding.

GOING FORWARD

Scheme Structure Review

3.2.6 While work progresses on the scheme structure review, elected members remain committed to delivering a well run and well governed scheme. The Pension Board will continue to assist and constructively challenge officers to deliver effective management and administration within their existing remit.

Covid-19

3.2.7 The global pandemic will continue to be a focus in 2021, however current governance arrangements are working effectively with Pensions Committee and Board meetings being undertaken in a hybrid fashion and training offered virtually.

TPR Code of Practice

3.2.8 TPR is expected to release a new single Code of Practice in 2021. This will replace the existing 15 Codes of Practice. A full compliance review will be carried out by officers once this new Code is released.

Pensions Administration Review

3.2.9 A review of activities within the pensions administration team was undertaken at the end of 2020 to assess key processes, identify any areas for improvement to meet increasing demands on performance and ensure the Funds continuing ability to comply with legislation and tPR guidance. The review concluded that many of the current key processes were working well, however a number of recommendations were made to help increase efficiency. An update on the outcome of the review is also on the agenda for consideration.

4. FINANCIAL IMPLICATIONS

4.1 Good governance is a crucial element of effective public services. It leads to good management, good performance and good stewardship of public money.

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 maintains its own Risk Management Policy and regularly updates its Risk Register in line with change. This is reported quarterly to the Pensions Committee

7. OUTCOMES

7.1 The proposals in this report have no impact on the Council Delivery Plan.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

None

10. APPENDICES

None

11. REPORT AUTHOR CONTACT DETAILS

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ABERDEEN CITY COUNCIL

COMMITTEE	Pensions Committee
DATE	26 March 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	Administration Review
REPORT NUMBER	PC/MAR21/ADMIN
DIRECTOR	Steven Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHOR	Gary Gray
TERMS OF REFERENCE	4.1

1. PURPOSE OF REPORT

1.1 To provide Committee with details of an administration review carried out by the scheme actuary (Mercer) and the North East Scotland Pension Fund (the Fund) to gain efficiencies and improve member outcomes.

2. RECOMMENDATION

2.1 That the Committee consider the outcome of the review and note the recommendations set out in section 3.6 of the report which will be taken forward over the next 12 to 18 months.

3. BACKGROUND

Reasons for review

3.1 Increasing workload, impact of regulatory change, McCloud age discrimination as well as continuing challenges of homeworking because of Covid-19, details provided in Appendix I.

Review approach

3.2 Scope for the administration review was prepared by Mercer following consideration of a paper provided by the Fund and a meeting with officers on 28 October 2020. Fieldwork was to be carried out remotely with review samples provided by the Fund via a secure portal.

3.3 The review was broken down into 4 key areas:

- *Process (weighted at 80%) – the review sample included a range of the most common administration tasks performed by the team between February and September 2020.*

- *Management information – the review sample included a range of quantitative and qualitative information provided by the NESPF Team Managers.*

- *People – the sample included a variety of job roles, internal communications and related documents provided by NESPF. It also included output from 2 Officer meetings and 1 Assistant Officer meeting as well as other information provided during the Team Manager meetings and process walkthroughs.*

- *Capacity analysis – the analysis was derived from data contained within task completed reports, task created reports and from a list of estimated task completed times.*

3.4 Following 18 Teams calls and 140 document uploads the final report with recommendations was produced by Mercer on 18 December 2020.

Areas of strength

3.5 Mercer observed the following areas of strength during the review:

- *The Fund's common and conditional data scores were very strong, indicating high data quality.*

- *The Altair calculation automation is accurate and efficient for the majority of processes.*

- *The document production routines within Altair for leaver deferred and refund letters are efficient.*

- *I-Connect is an efficient and effective tool for obtaining member data from employers in relation to CARE service and loading this to member Altair records.*

- *The Fund is able to produce strong management information and reports that can provide estimates of effort, staff utilisation and provide an indication of process efficiency.*

Key recommendations

3.6 The following recommendations contained in the review will be implemented by the Fund:

- Work with employers to improve final pay provision through monthly I-Connect interface or a new cessation template.

- Create and maintain a calculation matrix to reduce amount of manual checking by officers of system output which is accurate and efficient.

- Implement bulk processing of deferred leavers and refunds when programs become available and investigate bulk deferred retirals using existing functionality.

- Review processes highlighted in report with a view to simplifying the procedures and reducing the number of chasers where appropriate.

- Reduce manual processes and task creation following automated I-Connect updates for new joiners.

- Review how documentation is uploaded, scanned and retained in Altair.

- Investigate internal and external options for centralised printing to avoid backlogs accumulating if homeworking continues or becomes a requirement for any other reason in the future.

- Create online surveys attached to processes that will encourage members to provide feedback whilst viewing uploaded documentation.

- Investigate ways of measuring work activity other than casework to provide management information for process improvement in other areas.

- Create a formal process for staff to suggest change that will be reviewed at same time as ideas submitted by other funds on system providers ideas portal.

- Set targets for processing any backlog accumulating because of increasing workload and homeworking.

- Carry out a review of system generated documentation and consider moving to Microsoft Word integration.

- Continue to convert manual worksheets to excel templates with built in formula.

- Continue to move processes online with transfer out quotations for deferred members a priority.

- Decide on best way for work allocation going forward taking account of changes made last year and findings of the review.

- Report the number of accesses across all processes quarterly and review steps showing an increase in the average number of accesses to see if the process can be improved.

3.7 The recommendations mentioned are not an exhaustive list of all changes the Fund will make following the findings of the review and work is already underway as part of a project that will take around 12 to18 months to deliver.

Capacity analysis

3.8 A way to measure resource requirement for the Benefits Administration team because of increasing workload was requested as part of the review.

3.9 The solution was to compare time taken for processes (tasks) created and completed during a reporting period to determine resource requirement using estimated allocated time for each process.

3.10 Mercer provided a spreadsheet calculator and the results for two reporting periods contained in Appendix II show a requirement for 3 additional posts.

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 maintains its own Risk Management Policy and regularly updates its Risk Register in line with change. This is reported quarterly to the Pensions Committee.

7. OUTCOMES

The proposals in this report have no impact on the Council Delivery Plan.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

None

10. APPENDICES

Appendix I, Increasing workload
Appendix II, Capacity analysis

11. REPORT AUTHOR CONTACT DETAILS

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APPENDIX I - Administration Review

Increasing workload

Cases and Tasks

Workload can be measured using the number of workflow cases (procedures) created that contain tasks (processes) and the table below shows the increase over last 3 years:

	2017/18	2018/19	2019/20
Cases	11,618	11,816	14,058
Tasks	81,312	87,476	94,994

Retirement processing

Volume of retirements has significantly increased because of regulatory change that reduced retirement age from 60 to 55.

The table below shows the number of retirement cases created during the last 3 years and the percentage increase over the 3 year period:

	2017/18	2018/19	2019/20	Increase
All retirements	1,842	2,053	2,945	60%
Active	633	769	931	47%
Deferred	842	938	1,627	93%

The table below shows the average retirement age reduces in the year the regulations came into force, 2018/19[1] for active members and 2019/20[2] for deferred members:

	2017/18	2018/19	2019/20
Active retirals	62.06	61.05	61.04
Deferred retirals	61.22	61.29	59.82

McCloud

Work on McCloud age discrimination has just commenced with programs received from our supplier to extract members in scope. The draft regulations stated that the date from which protection will no longer apply will be 1 April 2012 and using this date the following data is output:

	Service history extract	Service break extract
Distinct members	16,362	1,664
Distinct employments	17,657	1,751
Rows of data	27,530	3,056

[1] LGPS (Scotland) Regulations 2018 came into force June 2018.
[2] LGPS (Miscellaneous Amendments) (Scotland) Regulations came into force June 2019

If the date from which protection no longer applies changes to cover all members with final salary service then the output will be:

	Service history extract	Service break extract
Distinct members	22,682	2616
Distinct employments	25,321	2834
Rows of data	41,059	5083

The Fund has commenced work in advance of the final regulations being published:

- Started to review output based on draft regulations and are confident that data held on our system is good because we have continued to receive changes in hours and breaks in service for members through I-Connect monthly returns from our employers.
- For those members that we query with employers we will be able to provide data in a template to populate any service amendments required that can be interfaced back into our system.
- For those members that have left that will qualify for protection we do not have recalculation routines for certain statuses that may be in scope.
- Still a significant amount of current active membership have final salary service.
- Irrespective of when the protection date will be all funds will be faced with calculating final salary and care benefits separately for decades to come.

Impact of pandemic

We have established that it takes longer to process benefits while working from home and this is evidenced by our PAS performance for first 3 quarters of 2020/21.

Q1 2020/21	Q2 2020/21	Q3 2020/21
77.6%	79.8%	79.1%

This remains significantly down on overall percentages achieved for previous 3 years.

2017/18	2018/19	2019/20
95.1%	95.9%	93.5%

With no immediate prospect of getting staff safely back in the office it was important to see what further changes to processes could be made to gain efficiencies and improve member outcomes in the short term.

APPENDIX II – Administration Review

Capacity analysis

January to March 2020

Utilisation assumptions

Working hours per day	Working days per year	Assumed Working hours per year	Assumed Annual Leave	Assumed Annual Leave hours	Assumed hours per day spent not working in Altair	Assumed working hours per year spent not working in Altair	Productive hours in Altair per year	Assumed utlisation
7.4	260	1924	30	222	4.1	943	759	0.3944906
37/5	*52x5*	*260 x 7.4*	*30*	*7.4 x 30*	*4.1*	*(260-30) x 4.1*	*1924 - 222 - 943*	*759/1924*

Calculator

Task minutes	33378	(created or completed)
Task hours	556.3	(divide by 60)
Working days effort	190.5638999	(apply utilisation)
FTE required	**2.977560935**	(divide by 63 days)

Description	Tasks	FTE staff
Created	132800	11.85
Completed	99422	8.87
FTE required	**33378**	**2.98**

Benchmark used for assumed working hours not in Altair

Row Labels	Sum of TIME ALLOCATION	Hours	Average hours per day	
Officer 1	12925	215.4166667	3.419312169	
Officer 2	19308	321.8	5.107936508	
Officer 3	11247	187.45	2.975396825	
Officer 4	6599	109.9833333	1.745767196	
Officer 5	12305	205.0833333	3.255291005	7.4
			16.5037037	3.300740741
Benchmark				**4.099259259**
Exclude				
Officer 6	34321	572.0166667	9.07962963	
Trainee 1	4987	83.11666667	1.319312169	

April 2019 to March 2020

Utilisation assumptions

Working hours per day	Working days per year	Assumed Working hours per year	Assumed Annual Leave	Assumed Annual Leave hours	Assumed hours per day spent not working in Altair	Assumed working hours per year spent not working in Altair	Productive hours in Altair per year	Assumed utlisation
7.4	260	1924	30	222	4.2	966	736	0.3825364
37/5	*52x5*	*260 x 7.4*	*30*	*7.4 x 30*	*4.2*	*(260-30) x 4.2*	*1924 - 222 - 966*	*736/1924*

Calculator

Task minutes	139450	(created or completed)
Task hours	2324.166667	(divide by 60)
Working days effort	821.0371377	(apply utilisation)
FTE required	**3.157835145**	(divide by 260 days)

Description	Tasks	FTE staff
Created	537749	12.17
Completed	398299	9.02
FTE required	**139450**	**3.15**

Benchmark for assumed working hours not in Altair

Row Labels	Sum of TIME ALLOCATION	Hours	Average hours per day	
Officer 1	67792	1129.866667	4.345641026	
Officer 2	56560	942.6666667	3.625641026	
Officer 3	51993	866.55	3.332884615	
Officer 4	48996	816.6	3.140769231	
Trainee 1	23207	386.7833333	1.487628205	7.4
			15.9325641	3.186512821
Benchmark				**4.213487179**
Exclude				
Officer 5	116678	1944.633333	7.479358974	
Officer 6	24937	415.6166667	1.598525641	
Trainee 2	12801	213.35	0.820576923	

ABERDEEN CITY COUNCIL

COMMITTEE	Pensions Committee
DATE	26 March 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	Strategy
REPORT NUMBER	PC/MAR21/STRAT
DIRECTOR	Steven Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHOR	Laura Colliss & Mairi Suttie
TERMS OF REFERENCE	1-5

1. PURPOSE OF REPORT

1.1 To inform the Committee and provide recommendations (if applicable) to changes to the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund.

2. RECOMMENDATION

2.1 That the Committee note the updates to Scheme policy documents as part of the annual document review (item 3.9.6).

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
- Systems
- 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).

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 **<u>INVESTMENT</u>**

3.5.1 *Asset & Investment Manager Performance Report*

Separate Report, provided

3.5.3 **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 **<u>ACCOUNTING</u>**

3.6.1 Budget/Forecast and Projected Spend 2020/21 Report
Statement of Accounts 2020/21 – Action Plan

Separate Reports, provided

3.7 **<u>BENEFIT ADMINISTRATION</u>**

3.7.1 **Administration Review**

Final report and recommendations presented following administration review completed by Mercer.

Separate report, provided

3.8 **<u>SYSTEMS</u>**

3.8.1 Performance reporting is provided on a quarterly basis.

Appendix I, Pensions Administration Strategy Update

3.9 **<u>GOVERNANCE</u>**

3.9.1 **Scheme Advisory Board**

Copies of the latest bulletins and meetings are available at http://lgpsab.scot

3.9.2 **Accommodation**

A final update following completion of the NESPF office relocation project.

Separate report, provided

3.9.3 **Pension Fund Staff Training Update**

Individual staff training and development continued during 2020/21. Due to Covid-19 most of this learning took place online through webinars and training sessions. A number of staff across the 6 pensions team virtually attended the Scottish LGPS Conference in October 2020 and all staff completed the mandatory Information Governance refresher online training during the year. Training was also provided in February 2021 by our external legal advisors through Teams, covering a range of investment and administration topics. This training was well attended by pensions staff and feedback has been very positive.

3.9.4 **Annual Governance Review**

Review of NESPF compliance with the Public Service Pensions Act 2013 and the Pensions Regulators Code of Practice 14.

Separate report, provided

3.9.5 **Fraud, Whistleblowing and breaches of the Bribery Act**

There have been no cases during the year. All NESPF staff were asked to familiarise themselves with the Whistleblowing Policy and Procedure and compliance was recorded by the Governance Team.

3.9.6 **Document Review**

A number of Policy documents have been reviewed and updated, including:

- Systems Access Policy
- Governance Policy
- Overpayment of Pensions Policy
- Investment Policy and Myners Statement
- Governance Compliance Policy
- Risk Management Policy

Minor changes have been made around structure and wording to make the policies clearer.

Copies of which are available at www.nespf.org.uk.

3.10 **EMPLOYER RELATIONSHIP**

3.10.1 **Aberdeen City Council Transport – Buy in Update and Completion**

3.10.2 At the Pensions Committee meeting in June 2019 (PC/JUN19/ACCTF), the Committee approved the merger of the Strathclyde No.3 Fund into the Aberdeen City Council Transport Fund and subsequent Buy-In in respect of the combined pensioner liabilities on the basis that a full OJEU procurement would take place.

3.10.3 The procurement of this bulk annuity was very unusual, being only the second one undertaken by a public authority across the entire United Kingdom. Following June's Committee meeting, further discussions took place between Fund officers, legal and procurement colleagues and the scheme actuary on the most suitable procurement route.

3.10.4 Following those discussions, the Pensions Committee approved an alternative procurement route at their meeting in November 2019 (PC/NOV19/ACCTF). Officers submitted a request in writing to the Chief Operating Officer and the Head of Commercial and Procurement Services to suspend the Aberdeen City Council Procurement Regulations:

The Procurement Regulations may be suspended either in whole or in part by the Director of Commissioning and the Head of Commercial and Procurement Services in writing in respect of any contract where the award of that contract is urgently requested to meet the exigencies of the Service.

3.10.5 As per Regulation 33 of The Public Contract (Scotland) Regulations 2015:

33.-(1) A contracting authority may award a public contract following negotiated procedure without prior publication of a contract notice or prior information notice in any of the following cases - (c) where (but only if it is strictly necessary) for reasons of extreme urgency brought about by events unforeseeable by the contracting authority, the time limits for open procedure, restricted procedure or competitive procedure with negotiation cannot be complied with.

33.-(3) For the purposes of paragraph 1(c), the circumstances invoked to justify extreme urgency must not, in any event, be attributable to the contracting authority.

3.10.6 The Chief Operating Officer and the Head of Commercial and Procurement Services were satisfied the criteria to suspend was fulfilled and approved the request. Officers cited the unique nature of the project and the urgency of the procurement to justify the request. The Buy-In had to be completed by the end of March/April 2020 as annuity pricing is very much dependent on timing within the insurance sector and on market movements. Failing to complete the Buy-in within the timeframe would result in financial and reputational risks for the Pension Fund.

3.10.7 In addition, access to the bulk annuity market must be undertaken by a Broker (with Mercer having been appointed through a compliant framework). Mercer advised the Fund that there were only 8 suitable suppliers in the market, and as part of the process they intended to approach each one. This gave assurance that the procurement process would be undertaken in a fair and transparent way by ensuring the entire market had an opportunity to bid.

3.10.8 As reported in December 2020 the Buy-in was completed on the 19th November 2020, while the reasons for the alternative procurement route still very much stand the process was delayed due to COVID-19 and procurement subsequently paused due to market volatility. Once markets had recovered the process to procure commenced with contracts signed with the preferred provider Rothesay. (Appendix II, Press release)

3.10.9 This is a huge achievement for the Fund and a significant step in liability management, however it does bring additional work and complexity to the Fund. The Fund has another relationship to manage, ensuring we fulfil our contractual arrangements will requirement the involvement of all areas of the Pension Fund.

Accounting	reconcile monthly payments, annual accounts, ensuring the insurance policy is accounted for appropriately.
Benefits Administration	additional payrolls, record keeping, monthly reporting requirements including member movements and deaths, mortality screening.
Employer Relationship	additional record reconciliation and ensuring Rothesay data is accurate and up to date (18 month data cleanse project to ensure current data held.) Meeting contractual obligations of sanctions checking, quarterly reconciliation and member communications.
Governance	monitoring contractual compliance.
Investments	managing the remaining assets and custody arrangements for policy.
Systems	ensuring systems are available.

3.10.10 This will be a long term process for the Fund, updates will be provided to committee in due course.

3.10.2 **Valuation**

Report to update on the tri-ennial valuation.

Separate report, provided

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 a number of legal implications arising from implementation of the strategy which have been identified and addressed as set out in this report.

6. MANAGEMENT OF RISK

6.1 The Pension Fund maintains its own Risk Management Policy and regularly updates its Risk Register in line with change. This is reported quarterly to the Pensions Committee.

Appendix III, Copy of Risk Register (February 2021)

7. OUTCOMES

7.1 The proposals in this report have no impact on the Council Delivery Plan.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

None

10. APPENDICES

Appendix I, PAS Update
Appendix II, Press Release
Appendix III, Copy of Risk Register (February 2021)

11. REPORT AUTHOR CONTACT DETAILS

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North East Scotland Pension Fund

nespf

Pension Administration Strategy

Quarterly Reporting December 2020

1. NESPF performance from 1st April to 31st December

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.

		Completed cases during reporting period			Additional targets for completed cases during reporting period				Uncompleted cases during reporting period	
Administration Task	Target	Cases	Achieved	Percentage	+ 5 days	+ 10 days	+ 20 days	> + 20 days	Cases	Revised %
Notification of death in service	5 days	22	21	**95.5%**	95.5%	95.5%	95.5%	1	10	**65.6%**
Notification of retirement estimate	10 days	302	301	**99.7%**	99.7%	99.7%	100.0%	0	14	**95.3%**
Notification of retirement benefits	10 days	1175	1014	**86.3%**	93.7%	96.5%	98.0%	23	177	**75.0%**
Notification of deferred benefits	10 days	1405	1304	**92.8%**	94.6%	95.8%	96.0%	57	318	**75.7%**
Notification of refund	10 days	1025	990	**96.6%**	97.9%	99.4%	99.8%	2	34	**93.5%**
Notification of transfer in value	10 days	33	28	**84.8%**	84.8%	87.9%	90.9%	3	9	**66.7%**
Notification of transfer out value	10 days	206	94	**45.6%**	51.5%	53.0%	57.7%	66	16	**42.3%**
		4168	3752	90.0%				152	578	79.1%

Completed cases during reporting period - reporting output is based on 5 and 10 day targets built into workflow cases for processing administration tasks as declared in the pension administration strategy:

- *Overall percentage and overall revised percentage have both gone down 1% from previous quarter*
- *The only positive is retirement benefit percentages continue to improve from first quarter - 74.3% up to 86.3% and 61.9% up to 75%.*

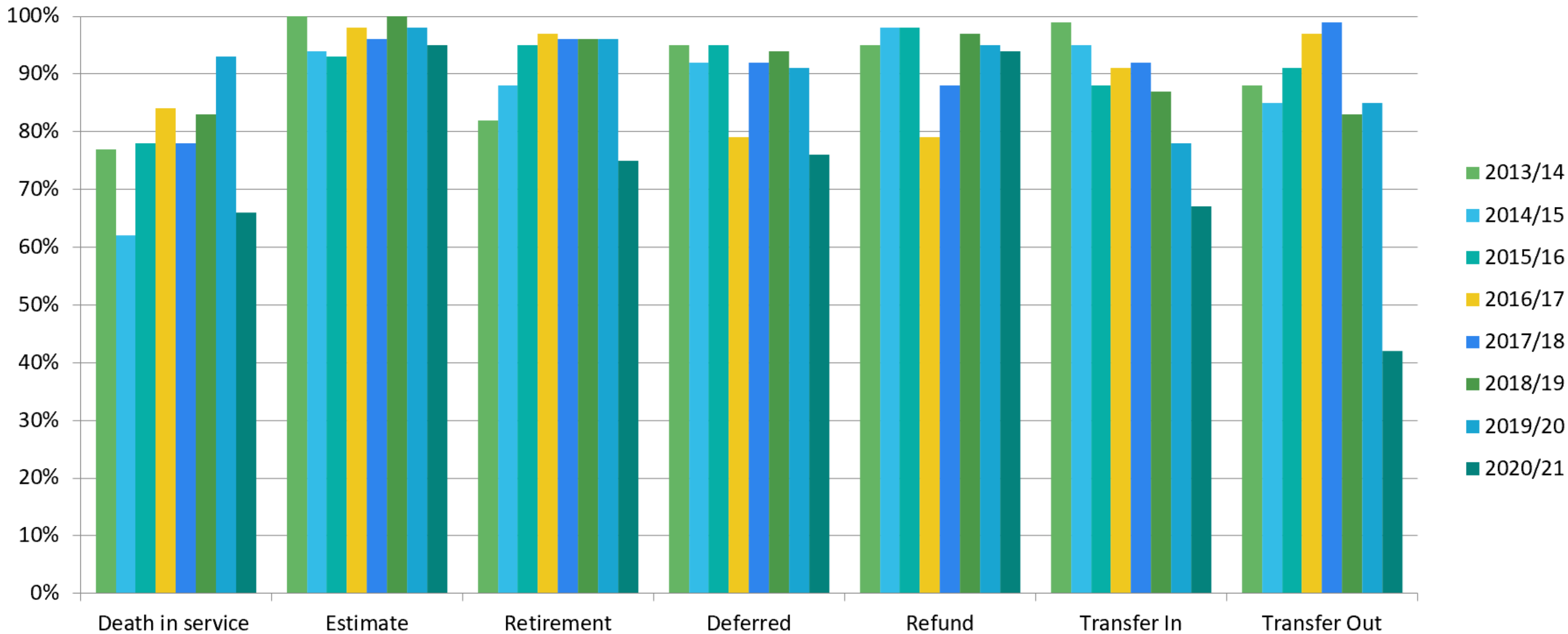
Additional targets for completed cases during reporting period - reporting output is based on adding 5/10/20 days to the 5 and 10 day targets built into workflow cases for processing administration tasks:

- *152 cases taking more than +20 days shows it is still taking longer to complete cases, this time last year 34 were reported.*

Uncompleted cases during reporting period - cases identified that were due to be completed and do not have a Reply Due date set in advance of the end of the reporting period:

- *578 cases were identified and contributed to the revised percentages, this time last year 126 were reported*
- *The impact of Covid-19 and home working was considered as part of the Administration Review with Mercer.*

1.2 Previous years comparison



2. Employer performance from 1st April to 31st December

2.1 Policy on discretions received (85%)

Each Scheme emloyer is required under regulation 58 of the Local Government Pension Scheme (Scotland) Regulations 2018 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	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 regarding 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
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 (710,681)

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)	2,612
Amendments (address, personal details, hours and absence)	13,813
Leavers (exit and opt out)	2,014
Contributions (employee, employer and additional)	232,919
Salary	231,448
Cumulative CARE Pay	224,272
Works Address	3,603

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 2021)

* Moved to another LGPS for administrating or employer has terminated from the fund

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 & Glasgow)	Extract File												
Robert Gordon University	Extract File												
Moray College	Extract File												
North East Scotland 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												
Archway	Online Return												
Citymoves 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	Extract File												
Inspire	Online Return												
Inspire Catering Scotland LLP	Online Return									*	*	*	*
Mental Health Aberdeen	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												
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												

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Risk Register

Pensions Dashboard

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.

This Risk Register is reviewed and updated quarterly, with reporting to the Pensions Committee.

The Pensions Committee is responsible for receiving assurance on the effectiveness of NESPF risk management arrangements as per their Terms of Refence.

Risk Scoring Process

In order to apply an assessment rating (score) to a risk, NESPF implements a 4 x 6 matrix. The 4 scale represents the impact of a risk and the 6 scale represents likelihood of a risk event occurring.

4	Very Serious	4	8	12	16	20	24
3	Serious	3	6	9	12	15	18
2	Marginal	2	4	6	8	10	12
1	Negligible	1	2	3	4	5	6
Impact / Likelihood		1	2	3	4	5	6
		Almost Impossible	Very Low	Low	Significant	High	Very High

Current Heat Map (where risks NESPF001 through 029 fall)

4	Very Serious	○ ○	○ ○ ○	○	○		
3	Serious	○	○ ○ ○	○ ○ ○	○		
2	Marginal	○	○ ○ ○ ○ ○ ○	○ ○ ○ ○ ○	○ ○		○
1	Negligible						
Impact / Likelihood		1	2	3	4	5	6
		Almost Impossible	Very Low	Low	Significant	High	Very High

Red = High Priority (urgent action required)
Orange = Medium Priority (assess adequacy of current controls, consider further action required to mitigate risk)
Green = Low Priority (no immediate action subject to exceptions, continue to review)

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
Pension Fund Level									
NESPF001	**Risk:** COVID-19 **Causes:** Global virus pandemic **Potential Impact:** Failure to pay pensions, loss of staff due to illness, time lost due to connectivity issues while homeworking, ability to meet regulatory requirements, financial impact on investment returns, covenant risk for employers	• Government and regulator guidance • NESPF risk policy and register • Updates/Communication between CO-Finance and Pension Manager • Business Continuity plans in place • Homeworking for Pensions Staff • PAS performance reporting • Internal/External audits • Regular staff comms and training	4	4	16	↔	**TREAT**		**Laura Colliss, ongoing**
NESPF002	**Risk:** Lack of effective risk controls **Causes:** Failure to implement risk management framework **Potential Impact:** Operational, financial and reputational issues	• NESPF risk register is reviewed and updated quarterly by senior management team • Consideration by Pensions Committee & Board at quarterly meetings • NESPF specific Risk Management Policy in place	4	1	4	↔	**TREAT**		**Ongoing**
NESPF003	**Risk:** Poor Governance		2	2	4	↔	**TREAT**		**Ongoing**

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
	Causes: Lack of robust and effective governance framework and supporting policies and procedures **Potential Impact:** Regulatory compliance issues, inability to determine policies and make effective decisions leading to poor service delivery and reputational risk	• Annual review of Funds Governance Compliance Statement and supporting policies and procedures • Adherence to Council's Scheme of Governance • Committee Effectiveness Report to support good governance						Committee Effectiveness Report presented to September 2020 meeting. Normal governance arrangements operating.	
NESPF004	**Risk:** Lack of performance measures **Causes:** Failure to develop performance reporting framework **Potential Impact:** Lack of transparency, poor performance could go unaddressed	• Statutory and local KPI's • Pension Administration Strategy published quarterly • Investment performance (against benchmark) reported to Committee quarterly	2	3	6	↔	**TREAT**		**Ongoing**
NESPF005	**Risk:** Failure of Pensions Committee and Pension Board to operate effectively **Causes:** Poor attendance/commitment to role, high turnover of members, lack of training **Potential Impact:** Non-compliance with regulatory requirements, inability to make decisions or policies, reputational risk	• Publication of Pension Board Annual Report • Training Policy reviewed annually and training register in place • Nomination & Appointment procedure • Annual Committee Effectiveness Report	3	2	6	↔	**TREAT**	Normal Governance arrangements to recommenced from September 2020.	**Ongoing**

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
NESPF006	**Risk:** Operational Disaster; unable to access the workplace **Causes:** Major incident, natural disaster **Potential Impact:** Loss of service delivery, staff downtime	• ACC Disaster Recovery policy in place • NESPF Business Continuity Plan to address loss/disruption to benefit administration system	2	2	4	↔	**TOLERATE**		**Ongoing**
NESPF007	**Risk:** Failure to recruit, retain and develop staff **Causes:** Limited pool of resources/competition with private sector, lack of training/development opportunities, resource drain from wider priorities **Potential Impact:** Loss of service delivery, risk to succession planning	• All staff have individual development plans which are reviewed regularly through CR&D • Training register to monitor • 2 full time training & development staff • Internal 2 year training programme for benefit admin staff • Future-focused staffing structure, subject to ongoing review	4	2	8	↔	**TREAT**	Recruitment underway to fill vacant posts through new Re.cru.it scheme. Staffing and accommodation update to March 2021 Committee meeting.	**Laura Colliss, March 2021**
NESPF008	**Risk:** Pay and price inflation valuation assumptions either higher or lower **Causes:** Economic factors **Potential Impact:** Potential increase in employer contribution rates and liabilities	• Quarterly funding updates to Committee (using FSM) • Tri-ennial valuation • Individual employer contribution rates	2	2	4	↔	**TOLERATE**	Tri-ennial valuation 2020 in progress. Update report to March 2021 Committee meeting.	**Ongoing**
Governance									

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
NESPF009	**Risk:** Failure to adhere to relevant pensions legislation and guidance **Causes:** Political and legislative changes, increased administrative complexity, staff training issue **Potential Impact:** Audit criticism, legal challenge, reputational risk, financial loss and tPR action	• Six monthly compliance review, with annual reporting to Pensions Committee and Board • Active participation at LGPS events, Testing Working Party for administration software updates • Established processes for staff training • Regular benefit admin team meetings to share knowledge	3	3	9	↔	**TREAT**		**Ongoing**
NESPF010	**Risk:** Failure to comply with FOI or SAR requests **Causes:** Missed statutory deadlines due to training or resource issues **Potential Impact:** Audit criticism, legal challenge, reputational risk	• Internal written procedures in place • FOI/SAR log to record & monitor	3	1	3	↔	**TREAT**	New online process through GovServices implemented to manage FOI requests	**Ongoing**
NESPF011	**Risk:** Conflicts of Interest **Causes:** Competing professional and personal interests of staff, Committee and Board members **Potential Impact:** Audit criticism, legal challenge, reputational risk	• Regular discussions between CO-Finance and Pension Fund Manager • Standing agenda item at meetings • Conflicts policy & register in place, with conflicts declarations issued annually	2	4	8	↔	**TREAT**		**Ongoing**
Benefit Administration									

North East Scotland Pension Fund nespf

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
NESPF012	**Risk:** Requirement to complete GMP reconciliation **Causes:** End of contracting out due to reforms of state pension **Potential Impact:** Failure to calculate future benefits correctly, audit criticism, financial loss	• Dedicated GMP project team reporting to Operations Manager • Regular updates to Committee and Board	2	2	4	↔	**TREAT**	IPE regulations with effect 1 March 2020. Final file received from HMRC in June 2020, further work is required to complete the project.	**Gary Gray, ongoing**
NESPF013	**Risk:** Fraud/Negligence **Causes:** Dishonesty or human error by staff, scheme members **Potential Impact:** Overpayment/unauthorised payments, system corruption, audit criticism, legal challenge, reputational risk	• Segregation of duties for benefits staff authorising/submitting lump sum payments • Pension payments signed off by benefits senior • Participation in National Fraud Initiative exercise • Overseas pensioner existence checking • Breaches Policy & register • Internal Audit control reviews	2	3	6	↔	**TREAT**	Enhanced Admin to Pay module to provide secondary calculation checks as system requirement implemented into Live system during October 2020. Procedure testing underway and full review to be completed in New Year.	**Ongoing**
Investments									
NESPF014	**Risk:** Insufficient assets to meet the Funds long term liabilities **Causes:** Failure of investment strategy or fund	• Quarterly assessment of investment performance and funding updates	4	3	12	↔	**TREAT**	Tri-ennial valuation in progress, investment strategy review outcome to follow.	**Ongoing**

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
	managers to produce expected returns **Potential Impact:** Increase in employer contribution rates, investment risk, audit criticism, financial loss	• Tri-ennial valuation and investment strategy review • Diversification of assets • Due diligence of fund managers • External advisor for specialist guidance on strategy						Tender underway for new investment management consultancy services.	
NESPF015	**Risk:** Failure to monitor investment managers and assets **Causes:** Lack of internal procedures **Potential Impact:** Audit criticism, legal challenge, reputational risk	• Quarterly assessment and reporting of asset performance • Regular meetings with investment managers	3	3	9	↔	**TREAT**		**Ongoing**
NESPF016	**Risk:** Failure of world stock markets **Causes:** Systemic **Potential Impact:** Increase in employer contribution rates, financial loss	• Diversification of Scheme assets • Tri-ennial valuation and investment strategy review	4	2	8	↔	**TOLERATE**		**Ongoing**
NESPF017	**Risk:** Negligence/Fraud/Default **Causes:** Dishonesty by fund managers, lack of care or human error **Potential Impact:** Financial loss, reputational damage	• Due diligence on appointment and appropriate clause in legal agreements • Fund management monitoring • SAS 70 reports	2	1	2	↔	**TOLERATE**		**Ongoing**
NESPF018	**Risk:** Failure of Global Custodian		4	1	4	↔	**TOLERATE**		**Ongoing**

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
	Causes: Financial market crisis, regulatory/political **Potential Impact:** Loss of assets or control of assets	• Regular meeting with custodian • Receipt of SAS 70 reports and monitoring							
NESPF019	**Risk:** Failure to implement ESG policy **Causes:** Lack of skills/knowledge, lack of transparency on practices or clear policy **Potential Impact:** Reputational damage	• Member training on roles and fiduciary duties • Policy incorporated within SIP • PRI membership	2	3	6	↔	**TREAT**	Annual PRI signatory assessment completed	**Ongoing**
Accounting									
NESPF020	**Risk:** Poor financial reporting **Causes:** Lack of internal policies and procedures, failure to keep up to date with changes in the Code of Practice and other overriding changes, training issues **Potential Impact:** Qualified accounts	• Comprehensive policies and procedures in place and review of *the Code* • Attending CIPFA meeting and reviews • Regular reconciliations e.g. fund managers, custodian • Internal/External Audits	3	2	6	↔	**TREAT**	Work commenced in preparation for year end accounts.	**Ongoing**
Systems									
NESPF021	**Risk:** Failure to secure and manage personal data in line with data protection requirements **Causes:** Cyber-attack, human processing error	• Annual information governance training for staff • Policies and procedures in place and reviewed	4	2	8	↔	**TREAT**	No data breaches this quarter, however risk rating left at same level due to ongoing COVID-19 and	**Ongoing**

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
	Potential Impact: Audit criticism, legal challenge, reputational risk, financial penalties	regularly (Breaches, Data Protection, Systems Access and Retention Schedule) • Secure physical storage measures • Admin system providers implement range of protections against cyber threats including encryption, firewalls, annual 3rd party penetration testing etc						homeworking situation.	
NESPF022	**Risk:** Failure of the Fund's administration system **Causes:** Outages, hardware and software failures and cyber attacks **Potential Impact:** Staff downtime, loss of service delivery	• Administration system is hosted externally with back up in separate location • Regular software updates • Business continuity and disaster recovery plans in place	3	2	6	↔	**TOLERATE**		**Ongoing**
NESPF023	**Risk** Failure to track member status and trace information **Causes:** Poor record keeping **Potential Impact:** Incorrect pension payments, incorrect assessment of actuarial liabilities, tPR action	• Tracing service in place (ATMOS) • Use of 'Tell Us Once' service • Data quality improvement plan including measures to trace • Existence checking	2	3	6	↔	**TREAT**		**Ongoing**
Employer Relationship									

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
NESPF024	**Risk:** Failure to monitor employer covenant **Causes:** Failure of internal procedures **Potential Impact:** Orphaned liabilities could fall on remaining employers	• Continued implementation of Covenant Assessment and Monitoring Policy (within FSS)	3	4	12	↔	**TREAT**		**Ongoing**
NESPF025	**Risk:** Changes in early retirement strategies by employers **Causes:** Public service cuts to funding **Potential Impact:** Pressure on cash flows	• Management through Covenant Assessment and Monitoring Policy (within FSS)	3	3	9	↔	**TREAT**		**Ongoing**
NESPF026	**Risk:** Employers leaving Scheme or closing to new members **Causes:** Public service cuts to funding, increased pension contribution costs **Potential Impact:** Orphaned liabilities could fall to remaining employers	• Management through Covenant Assessment and Monitoring Policy (within FSS) • Cost Cap mechanism introduced in LGPS regulations	2	6	12	↔	**TREAT**		**Ongoing**
NESPF027	**Risk:** Longevity **Causes:** Increasing life expectancy rates **Potential Impact:** Increase in employer contribution rates and liabilities	• Tri-ennial valuation undertakes scheme specific analysis including review of life expectancy/mortality assumptions which are set with some allowance for increases	2	2	4	↔	**TOLERATE**	Tri-ennial valuation in progress	**Ongoing**

North East Scotland Pension Fund nespf

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
NESPF028	**Risk:** Employer contributions not received, collected or recorded accurately **Causes:** Lack of staff resources, training issues **Potential Impact:** Orphaned liabilities could fall to remaining employers	• Internal escalation procedures • Breaches policy and register Monthly data submission reconciled by ERT • Quarterly PAS reporting to Committee & Board • Ongoing training provided by dedicated ERT to Scheme employers • Employer Briefings	2	4	8	↔	**TREAT**		**Ongoing**
NESPF029	**Risk:** Failure to maintain member records; data incomplete or inaccurate **Causes:** Lack of staff resources, training issues **Potential Impact:** Incorrect pension payments, incorrect assessment of actuarial liabilities, reputational damage, tPR action	• Monthly data from employers which is reconciled by ERT • Quarterly PAS reporting to Committee & Board • Data quality improvement plan implemented	2	2	4	↔	**TREAT**		**Ongoing**
NESPF030	**Risk:** The Fund is unable to adequately comply with required administrative processes owing to McCloud Judgement **Causes:** Not having the required historic data, adequate resources, sufficient guidance	• SAB and other industry guidance • Early and ongoing communication with employers • McCloud project team created	2	3	6	**NEW**			**Ongoing**

Last Update: February 2021

Code	Risk Description	Mitigating Controls	Current Risk				Approach	Additional Actions/Latest Notes	Owner & Timescale
			Impact	Likelihood	Score	Movement			
	Potential Impact: Breaches and potential action by tPR, increase in liabilities, incorrect pension entitlements, damage to Fund reputation								

Rothesay

January 2021

Rothesay secures first LGPS policy with Aberdeen City Council's £230m buy-in

- Rothesay completes first deal with a Local Government Pension Scheme
- Buy-in policy is the Fund's first, covering £230m out of its c£300m liabilities
- Policy secures payments to 1,360 retired FirstGroup employees

Rothesay, the largest specialist annuity provider in the UK, is pleased to announce that it has completed a £230m pensioner buy-in transaction with the Aberdeen City Council Transport Fund ("The Fund").

The transaction insures the pension payments of 1,360 retired FirstGroup employees through a pensioner-only buy-in.

The buy-in is the Fund's first insurance transaction, securing £230m of its c£300m of pension liabilities. The Aberdeen City Council Transport Fund is only the second Local Government Pension Scheme to secure its pension obligations through an insurance policy.

The transaction was led by Mercer, acting for Aberdeen City Council, with Brodies providing legal advice to the Fund. Legal advice to Rothesay was provided by Linklaters.

Roisin O'Shea from Rothesay, said: "We are delighted that Aberdeen City Council chose Rothesay to protect their pensioners' payments and allowed the Fund to complete this significant de-risking step. Despite all the uncertainties last year, we saw a continued focus on de-risking from pension schemes with 2020 looking to be the second largest year for the market."

Laura Colliss from Aberdeen City Council, said: "We are very proud to be able to offer our members the protection to their pensions and peace of mind that this insurance policy provides. This transaction underscores the commitment to meeting the pension obligations and places the Fund and the tax-payer in a strong position for the future."

Adrian Marshall, LGPS Risk transfer specialist from Mercer, said: "We are delighted to have worked with the Council to achieve this significant milestone in its long term plan to secure members' benefits and ultimately protect the tax-payer. We worked with the Council to devise a clear, well-structured broking and procurement process to maximise insurer engagement to secure the best deal for all stakeholders. By entering into this buy-in with Rothesay, the Council has minimised its exposure to future volatility on around three-quarters of the Fund's liabilities."

Ian Hodgson, Group Pensions Manager of FirstGroup said: "This buy-in is the culmination of a project to sustainably de-risk our Scottish LGPS Funds. After the successful merger of our obligations from the Strathclyde Pension Fund, this buy-in has removed £230m of pensions risk from the Company, securing the pensions for some 1,360 members in the process. Transactions with the insurance market are not commonplace in the LGPS, and we are grateful to both Rothesay and the Fund for their work in making this an attractive de-risking option for employers and funds alike."

ENDS

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Notes to Editors

Rothesay

About Rothesay

Rothesay is the UK's largest pensions insurance specialist, purpose-built to protect pension schemes and their members' pensions. With £56 billion of assets under management, we secure the pensions of over 800,000 people and pay out, on average, more than £200 million in pension payments each month.

Rothesay is dedicated to providing excellence in customer service alongside prudent underwriting, a conservative investment strategy and the careful management of risk. We are trusted by some of the UK's best known companies to provide pension solutions, including the schemes of Allied Domecq, Asda, British Airways, Cadbury's, the Civil Aviation Authority, National Grid, the Post Office, Prudential and telent.

Rothesay has two substantial institutional shareholders, GIC and Massachusetts Mutual Life Insurance Company ("MassMutual"), who provide the company with long-term support for its growth and development. In September 2020, our shareholders increased their investment in Rothesay through a transaction which valued the business at £5.75bn.

Rothesay is the trading name for Rothesay Life Plc, a company authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. Firm Reference Number: 466067. Rothesay Life Plc is registered in England and Wales with company registration number: 06127279 and registered address: Rothesay Life Plc, The Post Building, 100 Museum Street, London WC1A 1PB. Further information is available at www.rothesay.com

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of the Local Government (Scotland) Act 1973.

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