

Aberdeen City Council Transport Fund

Funding Strategy Statement

March 2021

Aberdeen City Council

DRAFT

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)

Contents

Executive Summary	2
1. Introduction	7
2. Purpose of FSS in Policy Terms	9
3. Aims and Purpose of the Fund	10
4. Responsibilities of the Key Parties	11
5. Solvency Funding Target	13
6. Link to Investment Policy and the Statement of Investment Principles (SIP)	17
7. Identification of Risks and Counter-Measures	18
8. Monitoring and Review	21

Appendices

Appendix A – Actuarial Method and Assumptions

Appendix B – Employer recovery plan/surplus spreading plan

Appendix C – Termination policy for employers exiting the Fund

Appendix D – Glossary

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-III 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 exposed 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.

Allowing for the McCloud Judgment 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.

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.

Mercer Limited
No 4 St Paul's Square, Old Hall Street
Liverpool L3 9SJ
www.mercer.com

Mercer Limited is authorised and regulated by the Financial Conduct Authority. Registered in England and Wales No. 984275. Registered Office: 1 Tower Place West, Tower Place, London EC3R 5BU

