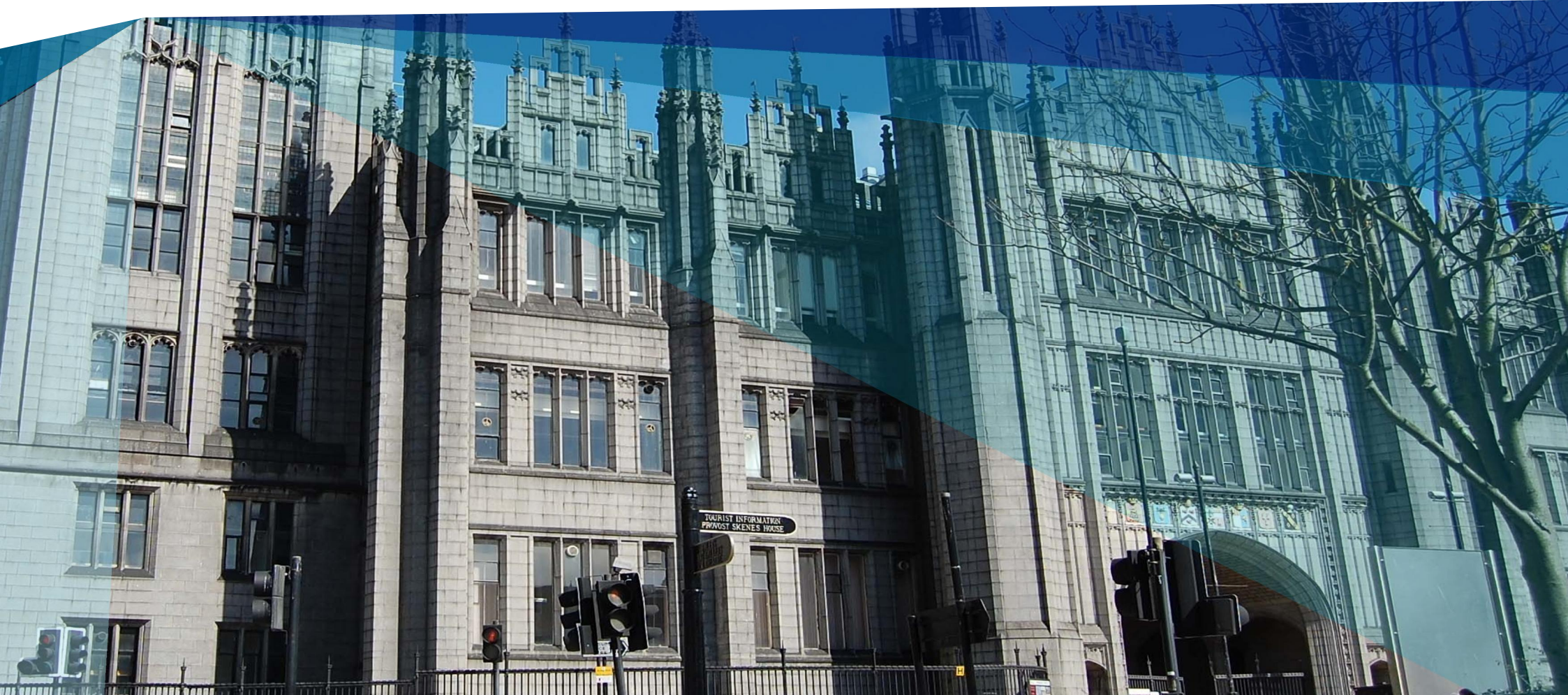


FUNDING REPORT OF THE ACTUARIAL VALUATION AS AT 31 MARCH 2014 NORTH EAST SCOTLAND PENSION FUND

MARCH 2015



CONTENTS

| | |
|--|----|
| 1. Introduction | 1 |
| 2. Key results of the funding assessment | 3 |
| 3. Experience since last valuation | 6 |
| 4. Variability and risk | 9 |
| Appendix A: Assumptions | 13 |
| Appendix B: Summary membership data | 25 |
| Appendix C: Assets | 26 |
| Appendix D: Scheme Benefits | 27 |
| Appendix E: Summary of Income and Expenditure | 29 |
| Appendix F: Analysis of experience of the membership of the Fund for the period 1 April 2011 to 31 March 2014 | 30 |
| Appendix G: Rates and Adjustments Certificate issued in accordance with Regulation 32 of the Administration Regulations..... | 31 |
| Appendix H: Schedule to the Rates and Adjustment Certificate dated 31 March 2015 | 33 |

1

Introduction

This report is addressed to Aberdeen City Council as the Administering Authority of the North East Scotland Pension Fund (“the Administering Authority”) and is provided to meet the requirements of Regulation 32 of the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008 (as amended). It describes the factors considered when carrying out the actuarial valuation as at 31 March 2014 and the decisions reached as a result.

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

- 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”).
- An appropriate plan for making up the shortfall if there are less assets than liabilities.
- 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.

Signature: 

Date of signing: 31 March 2015

Name: Paul Middleman
Fund Actuary

Qualification: Fellow of the Institute and Faculty of Actuaries

Signature: 

Date of signing: 31 March 2015

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Qualification: Fellow of the Institute and Faculty of Actuaries

This report has been prepared in accordance with the version of the *Pensions Technical Actuarial Standard* current at the date this report is signed. It also complies with the relevant requirements of *Technical Actuarial Standards R: Reporting Actuarial Information, D: Data* and *M: Modelling*, where they apply to this report. These Standards are all 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 contribution rates for the future for participating employers. 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.

2

Key results of the funding assessment

2.1. Past service funding position

The table on the right compares the assets and liabilities of the Fund at 31 March 2014. Figures are also shown for the last valuation as at 31 March 2011 for comparison.

The table shows that at 31 March 2014 there was a shortfall of £191m. An alternative way of expressing the position is that the Fund's assets were sufficient to cover 94% of its liabilities – this percentage is known as the funding level of the Fund.

At the previous valuation at 31 March 2011 the shortfall was £294m, equivalent to a funding level of 88%. The key reasons for the changes between the two valuations are considered in 3.2.

| | £m | |
|------------------------------------|---------------|---------------|
| | 31 March 2014 | 31 March 2011 |
| Total assets | 2,834 | 2,218 |
| Liabilities: | | |
| Active members | 1,282 | 1,183 |
| Deferred pensioners | 512 | 357 |
| Pensioners | 1,231 | 972 |
| Total liabilities | 3,025 | 2,512 |
| Past service surplus / (shortfall) | (191) | (294) |
| Funding level | 94% | 88% |

The liability value at 31 March 2014 shown in the table is known as the Fund's "funding target". The 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 Administering Authority's Funding Strategy Statement (FSS).

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

The above liabilities allow for the fact that pension increases will continue to be recharged £ for £ to the Fund in respect of pensionable service in the Aberdeen City Council Transport Fund accrued prior to 26 October 1986 in relation to First Aberdeen Limited.

2.2. Normal 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 “Common Contribution Rate”). A summary of the assumptions used is provided in Appendix A.

The table on the right gives a breakdown of the Common Contribution Rate at 31 March 2014 and also shows the corresponding rate at 31 March 2011 for comparison. In calculating the average Common Contribution rate we have made no allowance for existing and future members to opt for the 50:50 scheme.

| | % of Pensionable Pay | |
|--|----------------------|---------------|
| | 31 March 2014 | 31 March 2011 |
| Normal contribution rate for retirement and death benefits | 20.6 | 20.1 |
| Allowance for administrative expenses | 0.4 | 0.4 |
| Total normal contribution rate | 21.0 | 20.5 |
| Average member contribution rate | 6.1 | 6.3 |
| Common Contribution rate | 14.9 | 14.2 |

The benefits earned under the LGPS change with effect from 1 April 2015, and the Common Contribution Rate at 31 March 2014 allows for these changes. The impact of these benefit changes on the Common Contribution Rate is given in section 3.3.

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).

2.3. Allowance for post valuation market changes

Since 31 March 2014 there have been significant changes in the financial market position. In particular there has been a fall in gilt yields, which underpin the assessment of the past service liability values and therefore the long term funding target, which has led to a worsening of the funding position and an increase in the shortfall. As the new contribution rates are effective from 1 April 2015, the Administering Authority (following consultation with the Actuary and employers) has agreed that average contributions will be kept, as far as possible, at current levels.

In practice, each employer's position is assessed separately. The Schedule to the Rates and Adjustments Certificate (attached as Appendix H) sets out the contributions for each employer over the three year period to 31 March 2018. The individual rates take into account the differing circumstances of each employer or employer group and the funding plan, as laid down in the FSS. Contribution requirements for the period from 1 April 2018 onwards will be revised as part of the next actuarial valuation as at 31 March 2017 and will be confirmed in the Rates and Adjustments Certificate and Schedule accompanying that valuation report. As a general rule employers will not be allowed to reduce contributions from current levels.

2.4. Correcting the shortfall

The funding objective as set out in the FSS is to achieve and maintain a funding level of 100% of liabilities (the Funding Target). In line with the FSS, where a shortfall exists at the effective date of the valuation a deficit recovery plan will be put in place which requires additional contributions to correct the shortfall (or contribution reductions to refund any surplus). The maximum deficit recovery period for the Fund has been set as 19 years.

Given the deterioration in funding position noted above, if we maintained the average employer contribution payable at the previous valuation of 19.3% of Pensionable Pay, this would imply a deficit recovery contribution of 4.4% of projected Pensionable Pay at the valuation date. Under the same method and assumptions as used for calculating the funding target, the deficit of £191 million could be eliminated over a period of around 11 years. However, the deterioration in the funding position has increased the deficit and therefore the implied recovery period will also have increased.

3

Experience since last valuation

3.1. Summary of key inter-valuation experience

The last actuarial valuation was carried out with an effective date of 31 March 2011. Since the last valuation the Government announced that the benefit structure under the LGPS will change with effect from 1 April 2015. The changes do not affect benefits earned prior to 1 April 2015, and so do not directly affect the funding level or shortfall of the Fund as detailed in section 2.1, but do affect the Common Contribution Rate for the Fund as quoted in section 2.2 (the impact of the changes is given below). Details of the benefits are given in Appendix D.

The average salary increase (weighted by liability) for the Fund members who were in service for the whole of the inter-valuation period was 1.9% per annum.

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

- April 2012 5.2%
- April 2013 2.2%
- April 2014 2.7%

During the inter-valuation period, the gross investment return on the Fund's assets has averaged 7.9% per annum.

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

As noted in 2.1, the shortfall at 31 March 2011 was £294m. The table below sets out the main reasons for the change in the shortfall between 31 March 2011 and 31 March 2014.

| Analysis of changes in funding position | £m |
|--|-----------|
| Shortfall at 31 March 2011 | (294) |
| <i>Unwinding of interest on 2011 shortfall</i> | (55) |
| <i>Investment returns versus expectations</i> | 156 |
| <i>Deficit contributions paid</i> | 76 |
| <i>Salary increases versus expectations</i> | 108 |
| <i>Change in demographic assumptions</i> | 46 |
| <i>Change in financial assumptions</i> | (200) |
| <i>Member movements and other factors</i> | (28) |
| Shortfall at 31 March 2014 | (191) |

The above analysis highlights the key factors affecting the Fund since the previous valuation:

- Experience over the inter-valuation period has been largely positive, with improvements in the position due to positive investment performance, the impact of contributions paid by employers and lower than expected pay increases for active members.
- The shortfall increased significantly due to changes in underlying financial conditions, principally reductions in real gilt yields.
- Certain changes made to the underlying assumptions to reflect the current economic climate and the current state of public sector finances have also had a positive impact on the shortfall. These changes are discussed in detail in Appendix A.
- As discussed in section 2.3, the financial conditions have worsened since 31 March 2014 increasing the value of the Fund's past service liabilities and shortfall and this has been taken into account when determining the recovery plan.

3.3. Reasons for the change in Common Contribution Rate since the last actuarial valuation

The table below sets out the main reasons for the change in the Common Contribution Rate between 31 March 2011 and 31 March 2014.

| Analysis of changes in Common Contribution Rate | % |
|--|--------------|
| Common Contribution Rate at 31 March 2011 | 14.2 |
| <i>Change in membership profile</i> | <i>0.2</i> |
| <i>Change in demographic assumptions</i> | <i>0.3</i> |
| <i>Change in financial assumptions</i> | <i>2.6</i> |
| <i>Impact of LGPS changes from 1 April 2015</i> | <i>(2.4)</i> |
| Common Contribution Rate at 31 March 2014 | 14.9 |

- The change in the long-term assumptions adopted has caused a significant increase in the employer contribution requirement. This has been driven in large part by the significant fall in gilt yields over the inter-valuation period (the assumptions used to calculate the contribution rate, and their derivation, are discussed in Appendix A).
- This effect has been offset to some degree by the upcoming changes to the LGPS, which produce a significant reduction in employer costs at a Whole Fund level. At an individual employer level, the impact varies depending on profile and in some cases can result in an increased cost. Employers have been notified separately of the impact.

4

Variability and risk

The contributions for participating employers set out in the Schedule to the Rates and Adjustments Certificate (Appendix H) have been determined as described in Appendix A of this report and in line with the parameters as set out in the Funding Strategy Statement.

The funding of defined benefits is by its nature uncertain. 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.

It is likely, especially in the short-term, that the assumptions will not be borne out in practice. It is therefore important to consider the potential impact on the employer contribution rates of actual experience differing from what has been assumed. The details in this section do this, based on the valuation results for the Fund as a whole as at 31 March 2014. As noted in section 2.4 the funding position has deteriorated since the valuation date.

It should be borne in mind that the valuation results set out in Section 2 of this report, and the assumptions on which they are based, represent only one outcome, and measures which are set for funding purposes might well not be appropriate in other circumstances.

4.1. Projected funding position at next actuarial valuation

As part of this valuation, the Fund has agreed with the Employers to put in place a recovery plan to pay off the shortfall. The next actuarial valuation will take place with an effective date of 31 March 2017. If, on average, experience up to that date from 31 March 2014 is in line with the assumptions made for this current actuarial valuation and the illustrative average contributions are paid, the expected funding level would be 96% at 31 March 2017.

4.2. Least risk basis

In assessing the value of the Fund's liabilities (the funding target), allowance has been made for asset out-performance and an Inflation Risk Premium 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 closely matches the liabilities and represents the least 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 least 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 an Inflation Risk Premium. On this basis of assessment, the assessed value of the Fund's liabilities at the 2014 valuation would have been significantly higher, by 37% and the declared funding level would be correspondingly reduced to 69% and an equivalent deficit of approximately £1,296 million at 31 March 2014.

4.3. Material risks faced by the Fund

This section provides a broad overview of the risks faced by the Fund and their potential mitigation. However, this issue is covered in greater detail in the Funding Strategy Statement.

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. 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:

- If any 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. If the reason for the employer not paying the agreed contributions is one of financial difficulties, then the Administering Authority's focus would switch to the need to secure as far as possible that any debt from the employer on it exiting the Fund can be recovered. This risk can be mitigated by regular employer covenant reviews, strengthening of covenant as appropriate, and monitoring of changes in employer covenant. In the ultimate default of an employer any shortfall would then become the responsibility of any guarantor or all other employers in the Fund. If an employer terminates participation and becomes an Exiting Employer under the Regulations then the shortfall will be determined in line with the termination policy set out in the FSS.
- If market levels and / or gilt yields change such that the liability values increase by more (or decrease by less) than the assets, the funding position would be worse than expected. An increase in employer contributions would be expected as a result. The same comments would apply if general population mortality studies and analysis of the Fund show that pensioners are living longer, or if improvements in mortality are found to be at a faster rate than allowed for. The analysis shown below illustrates the quantitative impact of such changes.
- 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, and they review the Fund's investment strategy alongside each actuarial valuation to ensure it is consistent with the funding strategy adopted.
- If members make decisions around their options such that those decisions increase the Fund's liabilities (e.g. by not commuting pensions for cash to the extent assumed), the funding position would be worse than expected. As a result, future employer contributions might then need to be increased.

4.4. 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 used, then the projected future funding level will be different from the level described above in 4.1.

To illustrate how sensitive the funding level is to experience being different from the assumptions, the table below shows how the valuation results at 31 March 2014 would have differed given small changes in the key assumptions.

| | Increase in shortfall at 31 March 2014 (£m) | Increase in the average future service contribution rate at 31 March 2014 (% of Pensionable Pay) |
|---|---|--|
| Discount rate reduces by 0.25% | +133 | +1.2 |
| Long-term inflation is 0.25% higher than assumed | +127 | +1.2 |
| Pensionable Salary growth is 0.5% higher than assumed | +65 | Nil |
| Members live one year longer than assumed | +69 | +0.3 |
| Growth assets fall by 25% | +652 | Nil |

The same changes in the opposite direction would reduce the shortfall and the average future service contribution rate.

APPENDIX A

Assumptions

A.1. 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 | <p>The majority of benefits in a pension scheme are paid many years in the future. In the period before the benefits are paid, the Administering Authority invests the funds held by the scheme 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”.</p> <p>The higher the investment return achieved, the less money needs to be set aside now to pay for benefits. The calculation reflects this by placing a lower value on the liabilities if the discount rate is higher.</p> <p>The discount rate adopted so set the Funding Target is derived by mapping projected cashflows arising from accrued benefits to a yield curve (which is based on market returns on UK Government gilt stocks and other instruments of varying durations), in order to derive a market consistent gilt yield for the profile and duration of the Scheme’s accrued liabilities. To this an Asset Out-performance Assumption (“AOA”) of 1.4% per annum is added to reflect the Fund’s actual investment strategy.</p> <p>Details of the discount rate used to calculate the cost of future service are detailed in section A.3.</p> |

| Assumption | Why it is important and how it impacts on the liabilities |
|---------------------------|--|
| Inflation | <p>Pensions in payment increase in line with price inflation. 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.</p> <p>The inflation assumption will be taken to be the investment market's expectation for RPI inflation based on the difference between yields derived from conventional and index-linked UK Government gilts as at 31 March 2014, reflecting the profile and duration of the Scheme's accrued liabilities but subject to the following two adjustments.</p> <ul style="list-style-type: none"> • An allowance for supply/demand distortions in the bond market and • An adjustment due to retirement pensions being increased annually by the change in the Consumer Price Index rather than the Retail Price Index. <p>The overall reduction to market implied RPI inflation at the valuation date is 1.0% per annum, compared to 0.8% per annum in 2011. The increase in this assumption reflects a general increase in expectations of the long term difference between RPI and CPI, of this 1% per annum reduction, 0.3% per annum relates to the "Inflation Risk Premium" i.e. representing the allowance for supply/demand distortions in the bond market.</p> |
| Pensionable Salary growth | <p>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.</p> <p>The assumption for real salary increases in the long term is 1.5% p.a. over the CPI inflation assumption described above. This includes allowance for promotional increases. This has been modified from the assumption at the previous valuation (of 1.75% p.a. above CPI) to reflect reduced future expectations, averaged over the long-term, for real salary increases in the public sector.</p> <p>However, in the short term, salary increases are assumed to be lower to reflect expectations of further restraint on public sector pay. For the purpose of the whole Fund results shown in this report, we have assumed that salary increases for the first three years following the actuarial valuation will be 1.0% over 3 years for the Councils group. The allowance for other individual employers / employer groups depends on information provided and this is set out in the FSS.</p> |

| Assumption | Why it is important and how it impacts on the liabilities |
|-------------------|---|
| Pension increases | Increases to pensions are assumed to be in line with the inflation (CPI) assumption described above. The pension increase assumption is modified appropriately to reflect any benefits which are not fully indexed in line with inflation. |
| Life expectancy | <p data-bbox="651 477 1991 541">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.</p> <p data-bbox="651 588 1991 719">The mortality assumptions will be based on 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 scheme. The mortality tables used are adjusted to reflect the Fund's membership profile and recent mortality experience, and are set out in the summary section below.</p> <p data-bbox="651 767 1991 863">For all members, it is assumed that the accelerated trend in longevity seen in recent years will continue in the longer term and as such, the assumptions build in an allowance for longevity 'improvement' year on year in the future in line with the 2013 CMI projections subject to a long-term improvement trend of 1.5% per annum.</p> <p data-bbox="651 911 1991 975">Members who retire on the grounds of ill health are assumed to exhibit average mortality equivalent to that for a good health retiree at an age 3 years older for current pensioners, and 4 years older for future pensioners.</p> |
| 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 2009 service). The 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. |

| Assumption | Why it is important and how it impacts on the liabilities |
|--------------------------------------|---|
| Early retirements (non-ill health) | <p>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.</p> <p>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.</p> <p>For the common contribution rate calculations, 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 reduced by the Government Actuary's Department.</p> <p>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.</p> |
| Early retirements (ill-health) | <p>Members can retire before their normal retirement age due to ill-health in certain circumstances. There are three levels of ill-health retirement, with each giving rise to different levels of benefit. Tier 3 retirements are funded separately outside the Scheme.</p> <p>A small proportion of the active membership is assumed to retire due to ill-health, as set out in the table in the next section. In addition the proportion assumed to fall into each ill health tier is also shown.</p> |
| Proportions with dependants on death | <p>The Fund pays benefits to qualifying dependants (spouse/civil partner/dependent child) on the death of a member. Therefore, the proportion of members with a qualifying dependant impacts on the total cost of benefit provision, with a higher proportion of dependants meaning a higher cost. The valuation calculations assume a proportion of the active membership to retire in normal health prior to age 65, as set out in the table in A.2.</p> |

| Assumption | Why it is important and how it impacts on the liabilities |
|------------------------|---|
| Expenses | Expenses are met out of the Fund, in accordance with the Regulations. Expenses of administration are 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. |
| 50:50 option | From 1 April 2015 there is a 50:50 option available to members, whereby they can opt to receive 50% of the standard Fund benefits in return for paying 50% of the standard employee contributions. When calculating the average Common Contribution Rate we have assumed no existing or future members will select this option. This assumption will be reviewed at the next valuation. |

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 be still be alive by the date of each payment, and then discounting each payment back to the effective date of the valuation; 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.

A.2. Assumptions used to calculate the funding target

The tables below summarise the key assumptions used in the calculation of the Funding Target and those used for the 31 March 2011 actuarial valuation.

| Financial assumptions | 31 March 2014 | 31 March 2011 |
|--|---|--|
| Discount rate: | 4.9 % p.a. | 5.9 % p.a. |
| Assumed long term CPI inflation | 2.6 % p.a. | 3.0 % p.a. |
| Salary increases – Long term | 4.1 % p.a. | 4.75% p.a. |
| – Short term (3 years) | 1.0 % p.a. | N/A |
| Pension increases in payment | 2.6 % p.a. | 3.0 % p.a. |
| Demographic assumptions | | |
| | 31 March 2014 | 31 March 2011 |
| Pre-retirement mortality – base table | AC00 tables with adjustments of 73% (male) and 60% (female) to reflect the Fund's membership profile | PA92 year of birth tables adjusted by 1 year (females only) to reflect the Fund's membership profile. Future improvements in line with medium cohort projections |
| Post retirement mortality – base table | CMI Self-Administered Pension Schemes (SAPS) tables with scheme and member category specific adjustments (see further detail below) | CMI Self-Administered Pension Schemes (SAPS) tables with scheme and member category specific adjustments (see further detail in 2011 valuation report) |
| Post retirement mortality – future improvements: | | |
| Males | CMI_2013_M [1.5%] | CMI_2009_M [1.5%] |
| Females | CMI_2013_F [1.5%] | CMI_2009_F [1.5%] |

| Demographic assumptions | 31 March 2014 | 31 March 2011 |
|-------------------------|----------------------------|-----------------------------|
| Ill health retirement | (see further detail below) | (see 2011 valuation report) |
| Withdrawal | (see further detail below) | (see 2011 valuation report) |
| Proportions married | (see further detail below) | (see 2011 valuation report) |

Post retirement mortality

| | | Base Table | Improvements | Adjustment (M / F) |
|---------------------------|----------------------|---------------|-----------------|-------------------------|
| Current pensioners | Normal health | S1PA | CMI_2013 [1.5%] | 106% / 103% |
| | Ill-health | S1PA | CMI_2013 [1.5%] | Normal health + 3 years |
| | Dependants | S1PMA / S1DFA | CMI_2013 [1.5%] | 175% / 121% |
| | Future dependants | S1PMA / S1DFA | CMI_2013 [1.5%] | 114% / 108% |
| Current active / deferred | Active normal health | S1PA | CMI_2013 [1.5%] | 107% / 97% |
| | Active ill-health | S1PA | CMI_2013 [1.5%] | Normal health + 4 years |
| | Deferred | S1PMA | CMI_2013 [1.5%] | 133% / 114% |
| | Future dependants | S1PMA / S1DFA | CMI_2013 [1.5%] | 114% / 108% |

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.

For example, a “+1 year” rating would mean beneficiaries are assumed to have the mortality of someone one year their senior which has the effect of reducing their life expectancy and hence reducing the assessed value of the corresponding liabilities.

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.

For example, a “106%” weighting would mean beneficiaries have mortality rates 6% higher than the unadjusted table which reduces the assessed value of the corresponding liabilities.

The mortality assumptions used for the 31 March 2014 valuation result in the following life expectancies.

| | Years |
|--|--------------|
| Life expectancy for a male aged 65 now | 22.1 |
| Life expectancy at 65 for a male aged 45 now | 24.2 |
| Life expectancy for a female aged 65 now | 24.6 |
| Life expectancy at 65 for a female aged 45 now | 27.4 |

III 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:

| Age | % retiring per annum | |
|-----|----------------------|---------|
| | Males | Females |
| 35 | 0.05 | 0.04 |
| 45 | 0.13 | 0.13 |
| 55 | 0.60 | 0.52 |

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 | Tier 3 |
|---------|--------|--------|--------|
| Males | 72% | 9% | 19% |
| Females | 73% | 14% | 13% |

| | Conditions | Benefits based on |
|--------|---|---|
| Tier 1 | No reasonable prospect of undertaking gainful employment before age 65. | Accrued membership plus prospective membership to age 65 |
| Tier 2 | Reasonable prospect of obtaining gainful employment before age 65. | Accrued membership plus 25% of prospective membership to age 65 |
| Tier 3 | Retirements are funded separately outside the Scheme. | |

Withdrawal

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

| Age | % leaving per annum | |
|-----|---------------------|---------|
| | Males | Females |
| 25 | 13.50 | 14.92 |
| 35 | 3.39 | 4.18 |
| 45 | 1.69 | 2.59 |

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), and that spouses/partners of female (male) members are three years older (younger), on average than the member.

| Age | % spouse/partner | |
|-----|------------------|---------|
| | Males | Females |
| 25 | 10 | 17 |
| 35 | 49 | 55 |
| 45 | 64 | 65 |
| 55 | 71 | 70 |
| 65 | 77 | 68 |

A.3. Assumptions used to calculate future service cost

The cost of future accrual (normal cost) has been calculated using the same actuarial assumptions as used to calculate the 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 following points:

- 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; and
- the future service liabilities for which these contributions will be paid have a longer average duration than the past service liabilities so the base yield is currently higher due to the shape of the yield curve.

The financial assumptions in relation to future service (i.e. the normal cost) 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 3.0% per annum. This represents a reduction of 0.50% per annum compared to the 2011 valuation, to reflect the reduction in gilt yields (and so the increase in the expected cost of providing LGPS benefits) over the period. With a long term average assumption for price inflation of 2.6% per annum, this gives rise to an overall discount rate of 5.6% p.a.

At each valuation the cost of the benefits accrued since the previous valuation will become a past service liability. At that time any mismatch against gilt yields and the asset out-performance assumptions used for the funding target is fully taken into account in assessing the funding position.

| | 31 March 2014 | 31 March 2011 |
|------------------------------|---------------|---------------|
| Discount rate | 5.6% p.a. | 6.5% p.a. |
| Salary increases | 4.1% p.a. | 4.75% p.a. |
| Pension increases in payment | 2.6% p.a. | 3.0% p.a. |

A.4. Assumptions used to calculate the contributions payable under the recovery plan

The contributions payable under the recovery plan are calculated using the same assumptions as those used to calculate the funding target.

The investment return assumed for the contributions under the recovery plan is taken to apply throughout the recovery period. As a result, any change in investment strategy which would act to reduce the expected future investment returns could invalidate these assumptions and therefore the funding strategy.

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 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.

In addition to the current pensioners and spouses in the table, there were 117 current dependant pensioners as at 31 March 2014 with pensions totalling £174,431 per annum.

| | 31 March 2014 | 31 March 2011 |
|---|---------------|---------------|
| Active members | | |
| Number | 22,805 | 21,519 |
| Total Pensionable Salaries (£000s p.a.) ¹ | 411,803 | 393,309 |
| Average Pensionable Salary (£ p.a.) | 18,058 | 18,277 |
| Average age ² | 51.0 | 50.1 |
| Average past service ³ | 11.2 | 11.4 |
| Deferred pensioners⁴ | | |
| Number | 17,390 | 16,011 |
| Total deferred pensions revalued to valuation date (£000s p.a.) | 29,415 | 22,817 |
| Average deferred pension (£ p.a.) | 1,691 | 1,425 |
| Average age ² | 48.4 | 47.6 |
| Current Pensioners and Spouses | | |
| Number | 16,826 | 14,811 |
| Total pensions payable (£000s p.a.) | 79,916 | 65,801 |
| Average Pension | 4,750 | 4,443 |
| Average Age ² | 69.8 | 69.0 |

¹ Including actual pay for part time members

² Weighted by accrued pension/deferred pension/pension

³ Weighted by salary

⁴ Including frozen refunds

APPENDIX C

Assets

The market value of the Fund's assets was £2,833,575,000 on the valuation date based on the audited accounts.

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.

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. Details of the investment strategy can be found in the Statement of Investment Principles.

| | Actual market value of assets at 31 March 2014 | |
|--|---|------|
| | £000s | % |
| Fixed Interest | 228,391 | 8.1 |
| Index Linked | 3,012 | 0.1 |
| Equities | 1,248,540 | 44.1 |
| Pooled Vehicle | 982,598 | 34.7 |
| Property | 159,247 | 5.6 |
| Unit Trust | 8,531 | 0.3 |
| Private Equity | 136,414 | 4.8 |
| Cash and current assets / (liabilities) | 66,842 | 2.3 |
| Total | 2,833,575 | 100 |

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 2008 (as amended). The principal regulations relating to benefits earned up to 31 March 2014 are:

[The Local Government Pension Scheme \(Benefits, Membership and Contributions\) \(Scotland\) Regulations 2008](#)

[The Local Government Pension Scheme \(Administration\) \(Scotland\) Regulations 2008](#)

[The Local Government Pension Scheme \(Transitional Provisions\) \(Scotland\) Regulations 2008](#)

The benefits offered under the LGPS will change with effect from 1 April 2015, and the regulations relating to benefits earned after that date are:

[The Local Government Pension Scheme Regulations \(Scotland\) 2014](#)

[The Local Government Pension Scheme \(Transitional Provisions, Savings and Amendment\) \(Scotland\) Regulations 2014](#)

We have made no allowance for other changes which may be introduced in the future.

The benefits arising from the award of compensatory added years (CAY) of service on premature retirement have been treated as follows:

The general position is that the CAY benefits (together with associated pension increases) are recharged to the relevant employer. These benefits are therefore excluded from the valuation. However, for any employers who have opted to discharge part or all of their liability in

respect of CAY, this has been allowed for when assessing the contribution requirements. Where appropriate, the contributions certified in the Rates and Adjustments Certificate allow for the additional costs.

The contributions certified in the Rates and Adjustments Certificate allow for the additional liabilities in relation to pension increases payable on benefits accrued before 26 October 1986 within the Aberdeen City Council Transport Fund for members of First Aberdeen Limited, which are recharged on a £ for £ basis to the Fund.

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” judgement) and this includes providing equal benefits accrued from that date to reflect the differences in GMPs. There is no consensus or legislative guidance as to what adjustments have to be made to scheme benefits to correct these inequalities for ongoing schemes (i.e. for schemes other than those which are in the Pension Protection Fund). 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 professional advice if it is concerned about this issue.

APPENDIX E

Summary of Income and Expenditure

| INCOME | Year ending 31 March | | | Total |
|--|----------------------|------------------|------------------|------------------|
| | 2012 | 2013 | 2014 | |
| | £000s | £000s | £000s | £000s |
| Fund at beginning of year | 2,218,008 | 2,269,116 | 2,570,020 | 2,218,008 |
| Contributions to Fund: | | | | |
| Employees | 25,263 | 24,918 | 26,007 | 76,188 |
| Employers | 111,513 | 77,585 | 81,679 | 270,777 |
| Transfer Values received | 4,170 | 2,962 | 2,939 | 10,071 |
| Investment income | 44,068 | 45,969 | 55,240 | 145,277 |
| Other income | 61 | 56 | 56 | 173 |
| Change in market value of investments | -22,509 | 260,044 | 217,074 | 454,609 |
| EXPENDITURE | | | | |
| | Year ending 31 March | | | Total |
| | 2012 | 2013 | 2014 | |
| | £000s | £000s | £000s | £000s |
| Retirement and Spouses' Benefits | 73,748 | 80,146 | 83,532 | 237,426 |
| Retiring allowances and death gratuities | 25,667 | 18,558 | 20,153 | 64,378 |
| Refund of conts | 1,205 | 398 | 618 | 2,221 |
| Transfer Values paid | 3,448 | 4,069 | 2,933 | 10,450 |
| Investment expenses | 5,680 | 5,470 | 10,592 | 21,742 |
| Administration expenses | 1,710 | 1,989 | 1,612 | 5,311 |
| Fund at end of year | 2,269,116 | 2,570,020 | 2,833,575 | 2,833,575 |

APPENDIX F

Analysis of experience of the membership of the Fund for the period 1 April 2011 to 31 March 2014

The analysis below compares the actual experience over the 3 year period with the assumptions used for the 2014 valuation.

| | Actual | Expected | % |
|------------------------|--------|----------|-----|
| Ill Health Retirements | 194 | 258 | 75 |
| Withdrawals | 7,617 | 1,915 | 398 |
| Pensioner Deaths | 1,421 | 1,227 | 116 |

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

APPENDIX G

Rates and Adjustments Certificate issued in accordance with Regulation 32 of the Administration Regulations

Name of Fund

North East Scotland Pension Fund

Primary Contribution Requirements

I hereby certify that, in my opinion, the common rate of employers' contributions payable in each year of the period of three years beginning 1 April 2014 should be at the rate of 14.9 per cent of Pensionable Pay (including those in respect of members of the LGPS under the 50:50 option).

I hereby certify that, in my opinion, the amount of the employers' contributions payable in each year of the period of three years beginning with 1 April 2015, as set out above, should be individually adjusted as set out 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) unless otherwise noted in Appendix H or in a separate agreement with an individual employer, and the contributions in the attached schedule take account of any such agreements.

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 zero.

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 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 deficit is transferred to a new employer on its inception, the Scheme employer's deficit recovery contributions, as shown on the schedule to this Certificate in Appendix H, may be reallocated between the Scheme employer and the new employer to reflect this, on advice of the Actuary and as agreed with the Administering Authority so that the total payments remain the same overall.

Regulation 32(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: |  | Date of signing: | 31 March 2015 |
| Name: | Paul Middleman Fund Actuary | Qualification: | Fellow of the Institute and Faculty of Actuaries |
| Signature: |  | Date of signing: | 31 March 2015 |
| Name: | Laura Evans | Qualification: | Fellow of the Institute and Faculty of Actuaries |

APPENDIX H

Schedule to the Rates and Adjustment Certificate dated 31 March 2015

| Employers | 2015/16 | | 2016/17 | | 2017/18 | |
|---|-------------------------|---------------------------|-------------------------|---------------------------|-------------------------|---------------------------|
| | Individual Adjustment % | Total Contribution Rate % | Individual Adjustment % | Total Contribution Rate % | Individual Adjustment % | Total Contribution Rate % |
| <i>Councils Group</i> | 4.4 | 19.3 | 4.4 | 19.3 | 4.4 | 19.3 |
| <i>Other employers group</i> | 5.1 | 20.0 | 5.9 | 20.8 | 6.6 | 21.5 |
| <i>Standalone employers:</i> | | | | | | |
| Aberlour Child Care Trust | 5.4 | 20.3 | 5.4 | 20.3 | 5.4 | 20.3 |
| The Robert Gordon University | 4.4 | 19.3 | 4.4 | 19.3 | 4.4 | 19.3 |
| Robert Gordon's College | 5.5 | 20.4 | 5.5 | 20.4 | 5.5 | 20.4 |
| Alcohol Support Ltd | 5.7 | 20.6 | 5.7 | 20.6 | 5.7 | 20.6 |
| Archway | 9.6 | 24.5 | 9.6 | 24.5 | 9.6 | 24.5 |
| Middlefield Community Project | 8.5 | 23.4 | 12.7 | 27.6 | 16.8 | 31.7 |
| Tenants First Housing Co-op | 11.4 | 26.3 | 11.4 | 26.3 | 11.4 | 26.3 |
| North East Scotland College (see note 3) | 0.8 | 15.7 | 0.8 | 15.7 | 0.8 | 15.7 |
| Moray College | 5.1 | 20.0 | 5.9 | 20.8 | 6.6 | 21.5 |
| Visit Scotland | 5.9 | 20.8 | 5.9 | 20.8 | 5.9 | 20.8 |
| Home Start Aberdeen | 7.8 | 22.7 | 11.3 | 26.2 | 14.7 | 29.6 |
| Scotland's Lighthouse Museum | 6.2 | 21.1 | 6.2 | 21.1 | 6.2 | 21.1 |
| Robertsons Shire | 7.6 | 22.5 | 7.6 | 22.5 | 7.6 | 22.5 |
| Station House Media Unit | -0.7 | 14.2 | -0.7 | 14.2 | -0.7 | 14.2 |
| Aberdeen Sports Village | -0.6 | 14.3 | -0.6 | 14.3 | -0.6 | 14.3 |

| | | | | | | |
|--------------------------------------|------|------|------|------|------|------|
| Sport Aberdeen | -2.0 | 12.9 | -2.0 | 12.9 | -2.0 | 12.9 |
| Robertsons City | 7.5 | 22.4 | 7.5 | 22.4 | 7.5 | 22.4 |
| Forth and Oban | 6.2 | 21.1 | 6.2 | 21.1 | 6.2 | 21.1 |
| Drugs Action | 2.9 | 17.8 | 2.9 | 17.8 | 2.9 | 17.8 |
| Bon Accord Care | 2.4 | 17.3 | 2.4 | 17.3 | 2.4 | 17.3 |
| Bon Accord Support | 0.3 | 15.2 | 0.3 | 15.2 | 0.3 | 15.2 |
| Sanctuary Housing | 14.8 | 29.7 | 14.8 | 29.7 | 14.8 | 29.7 |
| Scottish Water (see note 3) | 1.5 | 16.4 | 1.5 | 16.4 | 1.5 | 16.4 |
| Northern Community Justice Authority | 1.5 | 16.4 | 1.5 | 16.4 | 1.5 | 16.4 |
| Scottish Fire and Rescue Service | 5.8 | 20.7 | 5.8 | 20.7 | 5.8 | 20.7 |
| Scottish Police (Combined) | 4.4 | 19.3 | 4.4 | 19.3 | 4.4 | 19.3 |

| | |
|--|--------------------------------|
| Councils Group | |
| 100 | Aberdeen City Council |
| 101 | Aberdeenshire Council |
| 102 | The Moray Council |
| 104 | Grampian Valuation Joint Board |
| All other employers | |
| This group applies to all other employers that are not detailed in the above group or separated out as part of the Schedule to the Rates and Adjustment Certificate dated 31 March 2015. | |

Notes:

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 from 1 April 2015.
2. Unless noted separately (by note 3), employers can choose to pay in advance their expected deficit contributions for a given year by 30 April each year as a £ lump sum. Where an employer chooses to make such payments in advance, the Actuary will confirm the amount to be paid. The employer will also need to notify the Fund of its intentions before making any advance payment.
3. The contribution rate payable for these employers is based on the assumption that a lump sum in respect of deficit contributions will be paid in advance. Interest, as per the advice of the Actuary, will be applied for late payment.
4. Separate payments will be made from the North East Scotland Pension Fund to the Aberdeen City Council Transport Fund in respect of pension increases payable to retired members relating to benefits accrued prior to 26 October 1986. These recharge amounts will be calculated by the Fund separately.
5. The total annual contributions payable by each employer will be subject to a minimum of zero.



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