North East Scotland
**PENSION FUND**

# UNAUDITED
# ANNUAL REPORT
# & ACCOUNTS

## FOR THE PERIOD
## 1 APRIL 2019 TO 31 MARCH 2020

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

ABERDEEN
CITY COUNCIL

# Contents

# Foreword

As Convener of the Pensions Committee, I am pleased to introduce the 2019/20 Annual Report and Accounts. 2019/20 was another year of significant activity and achievement with the Funds continuing to utilise technology and digital communications, participate and collaborate on national projects and develop our services to meet customer needs.

However, this work was partially overshadowed by the turbulence we saw in investment markets as a result of the COVID-19 outbreak. Despite a solid financial performance throughout the year, the economic uncertainty in the last quarter saw the North East Scotland Pension Fund's (NESPF) total asset value reduce from £4,469m as at 31 March 2019 to £4,383m as at 31 March 2020. An overall reduction of 1.9%.

The NESPF has a diversified portfolio of assets to help spread the risk of exposure to any one investment area or stock. This has ensured the financial impact on the Fund is minimal. In order to maintain the success of the Fund, it is our duty to continue to make investment decisions from a long-term perspective and we will continue to do so in 2020/21, in what we expect to be another challenging period.

Meanwhile the Aberdeen City Council Transport Fund (ACCTF) had a net increase in fund value of £203.5m, increasing the total net asset value to £308.8m. This increase is primarily a result of the merger of Strathclyde's No. 3 Fund (First Glasgow) to the ACCTF. The move, at the request of First Group, was a substantial project that involved close working partnerships to ensure a smooth transition of financial assets and data from Strathclyde to ourselves, whilst ensuring No. 3 Fund members were fully informed and engaged throughout the process.

Administratively, the Funds continued to make use of technological improvements and systems to push administration and communications online. For the first time, all annual benefit statements for active and deferred members were issued via our self-service portal, My Pension. A record number of retirement cases and system updates were processed this year, with the Funds' data quality improvement plan maintaining the high quality and accuracy of our data.

Looking ahead while challenges and uncertainties remain, the Funds will continue to deliver essential services in addition to a number of projects that are already planned. These projects include the triennial valuation, where the Funds will look to replicate the success of previous valuations; the launch of the Funds' new website and revised branding; the move to a new office; and the completion of a buy-in process for the ACCTF.

Finally, I would like to take this opportunity to thank my colleagues on the Committee and Board, Pension staff and our advisors for their dedication and hard work during the year. In particular for their remarkable response to the COVID-19 outbreak and their continued efforts to maintain and deliver services.

**Councillor M. Tauqeer Malik**
**Pensions Committee Convener**

# Management Commentary

## 1. About the North East Scotland Pension Funds

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

The LGPS is a public sector, multi-employer defined benefit Scheme that was established under the Superannuation Fund Act 1972.

The Funds are used to pay pensions, lump sum benefits and other entitlements to Scheme members and their dependents. The funds to pay these benefits are built up from contributions from both employees and employing bodies, together with interest, dividends and rent from investments.

The NESPF is open to all employees of the 11 scheduled bodies, except for those who are entitled to belong to another statutory pension Scheme (e.g. Police, Fire, Teachers). Employees of admitted bodies can join the Scheme in line with the body’s individual admission criteria for staff.

The ACCTF was created in October 1986 for employees of the former passenger Transport Undertaking who transferred to the limited company now known as First Aberdeen.

The rules by which the LGPS operates by are set out in the Local Government Pension Scheme (Scotland) Regulations which are Scottish Statutory Instruments (SSIs). Separate regulations set out Scheme benefits, investment and governance requirements.

As at 31 March 2020, the NESPF is the third largest LGPS Fund in Scotland in asset size, with over 69,000 members and 50 participating employers.

# 2. Administration 2019/20

| | |
|---|---|
| **Administering Authority** | Aberdeen City Council |
| **Committees** | Pensions Committee, Pension Board,<br>Urgent Business Committee* |
| **Chief Officer – Finance** | Jonathan Belford |
| **Actuary** | Mercer |
| **Global Custodian** | HSBC |
| **Performance Measurement** | HSBC |
| **Banks** | Clydesdale Bank & HSBC |
| **AVC Providers** | Prudential, Standard Life Assurance |
| **External Auditor** | Audit Scotland |
| **Internal Auditor** | Aberdeenshire Council |
| **Investment Consultant** | KPMG (until March 2020)<br>Isio (from March 2020) |
| **Legal Advisor** | Aberdeen City Council |
| **Employers** | For full details see Appendix 2 |

* Following the COVID-19 outbreak, all Council Committees were suspended. The purpose of the Urgent Business Committee (UBC) is to determine business of an urgent nature which might otherwise have been reported to Full Council or other Committees and Sub-Committees. As the Pensions Committee was unable to meet, the Unaudited Annual Report and Accounts 2019/20 were considered by the UBC at their meeting on 30 June 2020.

In reviewing the Unaudited Annual Report and Accounts 2019/20, some UBC members were substituted to ensure individuals with the appropriate knowledge and competence were present to recommend the submission of the Unaudited Accounts to Audit. The UBC consisted of the following individuals when considering the Unaudited Annual Report and Accounts; Councillor Malik, Councillor Bell, Councillor Cooke and Councillor Delaney (all current Pension Committee members); and Councillor Laing (a former Pensions Committee member).

# 3. Pensions Committee & Pension Board

**Pensions Committee**

While day to day administration of the Pension Funds is the duty of Pension Fund staff, decision making and overall responsibility has been delegated to the Pensions Committee by Aberdeen City Council.

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

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

The Committee meets on a quarterly basis to address matters such as risk management, administration, funding, investment strategy and performance.

The Committee is comprised of nine elected members of Aberdeen City Council each with equal voting rights.

**Membership 2019/20**

| | |
|---|---|
| Councillor M. Tauqeer Malik (Convener) | |
| Councillor John Reynolds (Vice Convener) | |
| Councillor Barney Crockett | |
| Councillor Neil MacGregor | |
| Councillor Philip Bell | |
| Councillor John Cooke | |
| Councillor Steve Delaney | |
| Councillor Christian Allard | (left May 2019) |
| Councillor Stephen Flynn | (joined May 2019, left January 2020) |
| Councillor Dell Henrickson | (joined January 2020) |
| Councillor Alan Donnelly | (left December 2019) |
| Councillor John Wheeler | (joined December 2019) |

**Meeting Attendance in 2019/20**

| | 14/06/19 | 13/09/19 | 29/11/19 | 20/03/20 | Overall Attendance 2019/20 |
|---|---|---|---|---|---|
| Cllr Malik | ✓ | X | ✓ | ✓ | 75% |
| Cllr Reynolds | ✓ | ✓ | X | ✓ | 75% |
| Cllr Crockett | ✓ | ✓ | ✓ | ✓ | 100% |
| Cllr MacGregor | ✓ | ✓ | X | ✓ | 75% |
| Cllr Bell | ✓ | ✓ | ✓ | ✓ | 100% |
| Cllr Cooke | ✓ | ✓ | ✓ | ✓ | 100% |
| Cllr Delaney | X | ✓ | ✓ | ✓ | 75% |
| Cllr Flynn | ✓ | ✓ | X | n/a | 67% |
| Cllr Henrickson | n/a | n/a | n/a | ✓ | 100% |
| Cllr Donnelly | ✓ | ✓ | X | n/a | 67% |
| Cllr Wheeler | n/a | n/a | n/a | ✓ | 100% |

**Pension Board**

In line with Scheme regulations, the Funds established a Pension Board in 2015/16 with the responsibility of assisting the Scheme Manager (Administering Authority) in relation to compliance with Scheme regulations and the requirements of the Pensions Regulator.

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

**Membership 2019/20**

Unison
Morag Lawrence (Substitute: Kenny Luke)

GMB
Kevin Masson (Left May 2019)
Neil Stirling (Joined May 2019) (Substitute: Brenda Murdoch)

Unite
Alan Walker (Substitute: Graham Gavin)

UCATT
Liam Knox (Chair)

Admitted/Scheduled Bodies
Mr Ian Black (Aberlour Child Care Trust)

The Moray Council
Councillor John Cowe

Aberdeenshire Council
Councillor Alistair McKelvie (Vice Chair) (Substitute: Councillor Alastair Bews)

Aberdeen City Council
Councillor Yvonne Allan (Substitute: Councillor Freddie John)

**Meeting Attendance in 2019/20**

| | 14/06/19 | 13/09/19 | 29/11/19 | 20/03/20 | Overall Attendance in 2019/20 |
|---|---|---|---|---|---|
| Cllr Yvonne Allan | ✓ | ✓ | ✓ | X | 75% |
| Cllr Alistair McKelvie | ✓ | ✓ | ✓ | X | 75% |
| Cllr John Cowe* | X | X | X | X | 0% |
| Ian Black | X | X | ✓ | X | 25% |
| Neil Stirling | ✓ | ✓ | ✓ | X | 75% |
| Morag Lawrence | ✓ | ✓ | ✓ | ✓ | 100% |
| Alan Walker | ✓ | ✓ | ✓ | X | 75% |
| Liam Knox | ✓ | ✓ | ✓ | ✓ | 100% |

**Notes:**

- Councillor Cowe was unable to attend meetings and training during 2019/20 due to personal mitigating circumstances.
- March 2020 – based on government guidance around non-essential travel and social distancing due to the COVID-19 pandemic, a number of members did not attend.

Apart from the Pension Board's Annual Meeting, the Board sits at the same time as the Pensions Committee. For each meeting, both the Board and the Committee receive the same reports. These reports include information on all areas of the Pension Funds; Investment, Accounting, Governance, Employer Relationship, Administration and Technical.

In assisting with compliance, the Board can report the Funds to the Pensions Regulator for non-compliance with guidance or regulations. In 2019/20 no issues were reported by the Board to the Pensions Regulator.

An Annual Report which reviews the activity of the Pension Board can be viewed on our website at www.nespf.org.uk

## Conflicts of Interest

The Funds maintain a 'Conflicts Register' on an ongoing basis to record and monitor all potential or actual conflicts noted prior to or during Pension Board meetings.

Every 12 months all individuals complete a new 'Declaration of Interest' form to either confirm that the information held on the Register is correct or to update their declaration as necessary.

In terms of management, where an actual conflict of interest arises the following option(s) exist:

- a member can withdraw from the discussion and decision making process;
- the Pension Board can establish a sub-board to review the issue (where the terms of reference give the power to do so); or
- a member can resign from the Pension Board if the conflict is so fundamental that it cannot be managed in any other way.

Pensions Committee members are managed by the national Councillors' Code of Conduct. Training was delivered on audit, risk and scrutiny by Aberdeen City Council in February 2020.

## Committee and Board Training 2019/20

While Pensions Committee members are not legally obliged to undertake training, the Funds feel strongly that Committee members should receive training to ensure that they have the necessary levels of knowledge and understanding to exercise their functions. In addition, training is a requirement of the Council's Standing Orders. As per the Training Plan agreed by Committee, Committee members are expected to undertake 2 days of training per year. Recording and monitoring of attendance at meetings or training events allows any issues to be addressed promptly.

In line with the Training Policy, Board members undertook 6 training sessions during 2019/20. Board members were asked to carry out a personal training needs analysis in 2019 to assess their overall level of knowledge and understanding. The results have been evaluated and will be used to direct training in 2020/21.

In 2019/20, attendance for both Pensions Committee and Pension Board members' training is outlined below.

| | 24/04/19 | 03/09/19 | 13/09/19 | 08/10/19 | 24-25 /10/19 | 7-10 /01/20 | Overall Attendance |
|---|---|---|---|---|---|---|---|
| **Pensions Committee** | | | | | | | |
| Cllr Malik | ✓ | X | X | ✓ | ✓ | ✓ | 67% |
| Cllr Reynolds | ✓ | X | ✓ | ✓ | X | ✓ | 67% |
| Cllr Crockett | X | X | ✓ | X | X | ✓ | 33% |
| Cllr MacGregor | X | ✓ | ✓ | ✓ | ✓ | ✓ | 83% |
| Cllr Bell | X | X | ✓ | X | X | ✓ | 33% |
| Cllr Cooke | X | ✓ | ✓ | X | ✓ | X | 50% |
| Cllr Delaney | ✓ | X | ✓ | X | X | ✓ | 50% |
| Cllr Allard | X | n/a | n/a | n/a | n/a | n/a | 0% |
| Cllr Flynn | n/a | X | ✓ | X | ✓ | n/a | 50% |
| Cllr Henrickson | n/a | n/a | n/a | n/a | n/a | n/a | n/a |
| Cllr Donnelly | X | ✓ | ✓ | X | ✓ | n/a | 60% |
| Cllr Wheeler | n/a | n/a | n/a | n/a | n/a | X | 0% |
| **Pension Board** | | | | | | | |
| Cllr Allan | X | X | ✓ | X | X | X | 17% |
| Cllr McKelvie | X | X | ✓ | X | ✓ | X | 33% |
| Cllr Cowe | X | X | X | X | X | X | 0% |
| Ian Black | ✓ | ✓ | ✓ | X | ✓ | ✓ | 83% |
| Kevin Masson | X | n/a | n/a | n/a | n/a | n/a | 0% |
| Neil Stirling | n/a | ✓ | ✓ | X | ✓ | ✓ | 80% |
| Morag Lawrence | ✓ | X | ✓ | X | ✓ | X | 50% |
| Alan Walker | ✓ | ✓ | ✓ | X | ✓ | X | 67% |
| Liam Knox | X | ✓ | X | X | X | ✓ | 33% |

**Notes:**

- Councillor Cowe was unable to attend any meetings or training sessions during 2019/20 due to personal mitigating circumstances.
- Councillor Henrickson joined the Committee in January 2020, after the January training session took place.

**Training Topics**

**24 April 2019**

The first event of the year was the Funds' Finance Forum. There were a number of presentations and panels on the day covering:

- Investment Overview
- Introduction to Environmental, Social and Governance (ESG): Strategy & Implementation in Real Estate
- Fund Review
- Brexit and Regulatory Insights
- Actuarial Considerations for 2020

**3 September 2019**

Training from the Investment Governance Group (IGG) and Scottish Pension Liaisons Group (SPLG) covered the following:

- Valuations/Cost Cap/Section 13
- ESG
- Structure Review
- Annual Report and Accounts
- Pensions Administration
- Cost Transparency
- Investments

**13 September 2019**

The training on 13 September took place in Aberdeen following the Pensions Committee/Board meeting on the same day and covered actuarial valuation calculations and liability assessment.

**8 October 2019**

Training was held by Baillie Gifford in their Edinburgh offices. The Local Authority Investment and Training Seminar focused on LGPS specific issues including investments across the life cycle of an LGPS fund, responsible investment and changes within the LGPS.

**24 – 25 October 2019**

Local Government Chronicle (LGC) Seminar. Areas covered during the 2 days of training included:

- Update on the SPLGS structural review consultation
- The infrastructure and housing challenge
- ESG
- How aligned is your scheme's approach to climate change and to your council's policy?
- What is keeping the investment managers awake at night?
- Investment strategy and the challenge of being an overfunded fund
- Investing in renewable energy: the opportunities and pitfalls
- Early reflections on the LGPS and looking to the future

**7 – 10 January 2020**

The extended training from 7 to 10 January took place at the Aberdeen Standard offices in London covering various topics from fund managers.

# 4. Administration and Performance

This year's report focuses on digital communications, pension administration strategy performance, data quality and our commitment to collaboration with other administering authorities.

**Going Digital**

2019/20 was the first year that both active and deferred annual benefit statements (ABS) were issued through our online Member Self Service (MSS) portal – 'My Pension'. Providing statements online has provided several advantages including:

> **Segmentation:** by taking the ABS process in-house, it provides additional scope to produce multiple benefit statements. Statements are now tailored based on type of service, so members will only receive statements with information relevant to themselves.
>
> **Cost savings:** There are significant cost savings in terms of production and postage. These savings will continue to increase as more members register for the system.
>
> **Environmental Impact:** Issuing statements online saves over 120,000 sheets of A4 each year. This saving will increase as the Funds replace letters with email notifications to alert members of future statements.

The overall percentage achieved for providing benefit statements to more than 42,000 active and deferred members prior to the 31 August deadline was 99.86% (99.81% in 2018/19).

As at 31 March 2020, 44.6% of active members and 41.2% of deferred members were registered for MSS. The Funds will continue to promote and develop online services. This includes the development of a new website that will have increased functionality, enhanced usability and improved design, resulting in a better user experience.

**Pension Administration Strategy**

The Pension Administration Strategy (PAS) focuses on NESPF processing against key performance measurements and monthly data provision from employers.

NESPF processing performance

| Key performance measurement | Target | 2018/19 | Amount | Achieved | 2019/20 |
|---|---|---|---|---|---|
| Letter notifying death in service to dependent | 5 days | 84% | 43 | 38 | 88% |
| Letter notifying retirement estimate | 10 days | 99% | 1029 | 1009 | 98% |
| Letter notifying actual retirement benefit | 10 days | 96% | 2072 | 1984 | 96% |
| Letter notifying deferred benefit | 10 days | 97% | 1302 | 1185 | 91% |
| Letter notifying amount of refund | 10 days | 98% | 1473 | 1401 | 95% |
| Letter detailing transfer in quotes | 10 days | 88% | 77 | 65 | 84% |
| Letter detailing transfer out quotes | 10 days | 85% | 432 | 327 | 76% |

This year again saw an increase in actual retirements with 528 processed in the fourth quarter. This exceeds the previous best and contributed to the total retirements for the year exceeding 2000 cases for the first time. New regulations came into force on 28 June 2019 and were backdated to 1 June 2018 which allowed deferred members to take their benefits from age 55 rather than 60. This resulted in an additional 220 retirements. Despite this increase, the percentage achieved remained the same as the previous year at 96%. However prioritising retirements was the main reason for percentage reductions in other areas.

From August 2019 trivial commutation, a one-off pension payment that extinguishes all rights in the scheme, was automatically offered to members whose capital value of all benefits was below £30,000 which increased the time taken to process retirement options.

Prior to the 6 October 2019 deadline, statements were issued to all members who potentially could exceed their Annual Allowance threshold for tax free pension savings.

Employer data provision

Moving from annual returns to obtaining monthly data from employers through i-Connect has provided huge benefits for the Funds in terms of information accuracy and the ability to record, check and reconcile contributions paid to the Funds. As of March 2020, the Employer Relationship Team has met its objective to obtain monthly information from all participating employers within the NESPF.

As new records, member movements and leaver information for all active members is updated through this secure online portal, the administrative burden has eased considerably across all areas of the Fund. The change of methodology allows the Fund to comfortably meet the regulatory deadlines for providing accurate benefit statements to members by 31 August each year. Of noticeable significance is the reduction in time taken to process the year-end from 328 working days (2013/14) to 21 working days (2018/19).

| **Updates from I-Connect** | **2017/18** | **2018/19** | **2019/20** |
|---|---|---|---|
| Starters | 4,415 | 4,852 | 5,125 |
| Amendments | 30,314 | 31,543 | 59,305 |
| Leavers | 3,345 | 4,352 | 4,196 |
| Contributions (employee, employer and additional) | 261,380 | 310,983 | 309,519 |
| Salary | 259,913 | 308,978 | 309,637 |
| CARE pay | 251,773 | 299,746 | 297,847 |
| **Total Updates** | **811,140** | **960,454** | **985,629** |

Communication between the Funds and participating employers is key to ensuring compliance with administration requirements. Through the Funds' Employer Relationship Team regular updates are provided by email and quarterly employer newsletters. The team provide training and guidance using the employer pages of the Funds' website, annual administration and financial forums and one to one training where requested. In addition, a dedicated telephone helpline and clear points of contact help the Funds to maintain a good working relationship with employers which allows the Funds to meet the expectations of administering the scheme on their behalf.

**Data Quality**

Measuring and improving the quality of data held by pension scheme administrators is high on the agenda of the Pensions Regulator. Data quality held by Funds impacts directly on the calculation of member benefits and determines the level of comfort that both Funds and participating employers can have around the valuation of the liabilities calculated by the scheme actuary.

As data is collected and reconciled on a monthly basis the Funds hold consistently high quality data. Validation of the data processed by the transferring system and reconciliation of the data received ensures that inaccurate or missing data is caught at source or queried upon receipt.

As part of the annual scheme return all LGPS Schemes are required to score the quality of their data. For accurate scores that are comparable to other Funds the NESPF contracted with Aquila Heywood to use their Data Quality Analysis Tool. In November 2019 Heywood carried out the first of three annual evaluations against the data held by the Fund. The scores provided as part of the results were reported in the 2019 annual return. The scores of 98.3% for common data and 97.1% for scheme specific data fell well above the national average for the 50 plus LGPS funds that have used this analysis tool for the same purpose.

Although the Funds can take great pride in the quality of the data held, work continues to improve and maintain data quality through the implementation of the NESPF data quality improvement plan. The plan, used in conjunction with the in-depth reports provided as part of the data analysis service contract with Heywood work towards meeting the following objectives:

1. To maintain the accuracy of member records to ensure that benefits held and paid are correct
2. To meet the regulatory requirements of pension administration including the Pensions Regulator Code of Practice 14
3. To provide comfort to the Administering Authority and participating employers in the accuracy of the actuarial results based on the quality of the data provided
4. To ease the administrative burden of incomplete or inaccurate records.

In addition to maintaining the accuracy of the current data and improving the historical data the plan details projects regarding tracing members and reducing the number of unprocessed records. Work continues around the completion of the reconciliation of Guaranteed Minimum Pensions (GMP) with Her Majesty's Revenue and Customs (HMRC).

**Collaboration through CLASS**

The Funds recognise the importance of working with other authorities and the software provider, Aquila Heywood, through the CLASS (Computerised Local Authority Superannuation System) group. Currently the group consists of 81 administering authorities in England, Wales, Scotland and Northern Ireland (NILGOSC), with all 11 Scottish funds currently using the Altair pension administration system.

CLASS collaboration takes many forms including regional and national user groups, a national testing working party for every software release and regular webinars on system issues and development. These events provide an opportunity to collaborate with colleagues from other funds to discuss system issues, consider development ideas and share best practise.

The regional group attended by staff contains Scottish funds only and is one of six regional groups in Britain and is currently chaired by NESPF. Staff also attend national user groups for Altair Payroll, MSS and i-Connect.

In October 2019 at the i-Connect user group in Manchester NESPF staff were invited to do a presentation on data quality and reconciliation of monthly submissions and sit on an expert panel for a question and answer session.

Staff participated in two Testing Working Parties (TWP) during 2019/20. In August, the Funds chaired the TWP for the Altair 10 software release and helped test developments which included a change to additional pension benefit calculation methodology for Scotland, paperless pay advices and functionality for members to upload documentation through MSS. Other sites that made significant contributions to the successful testing and sign-off of the release included Greater Manchester, NILGOSC and Oxfordshire.

Although the TWP is a big commitment, taking part provides early access to the latest software which benefits staff, members and employers.

**Merge of the Aberdeen City Council Transport Fund and the Strathclyde (No. 3) Fund**

In September 2018 First Group approached both the ACCTF and Strathclyde Pension Fund to express their desire to reduce the risk associated with their liabilities held within the LGPS (Scotland). One way to achieve this was to secure the liabilities by way of a buy-in. A buy-in is an insurance policy, purchased by a pension fund, that is an exact match against some, or all of the liabilities held. A buy-in would allow the fund to transfer the longevity risk to the insurer and create certainty around the valuation of the liabilities insured. Unlike a buy-out, the administration of all benefits is maintained within the fund and, should final pricing allow the final purchase to go ahead, would be the first of its kind in LGPS (Scotland).

In order to secure the best price for any potential buy-in and make the proposal more attractive to insurers it was agreed that the liabilities for both the ACCTF and Strathclyde No. 3 Fund would need to be included. Administratively, the easiest way to achieve this would be through a merge of both Funds.

There were additional advantages to the merge which included; the levelling out of funding due to Strathclyde (No. 3) Fund being over funded and the ACCTF being underfunded; the ability to increase the strength of the employer covenant supporting the liabilities held; and simplification of the management of the administrative relationship for First Group.

Aberdeen City Council expressed an interest in acting as the receiving administering authority for the merged liabilities and this was agreed by both the Aberdeen City Council and Glasgow City Council at committee level.

Following application for approval to the Scottish Government and guidance by legal advisors, the scheme actuaries and system providers, the transfer of the liabilities and member records took place in 2019. Communication with members was an integral part of the project to ensure smooth transition, with the first pension payment of Strathclyde pensioners being made in Aberdeen on 15$^{th}$ September 2019. Further work was undertaken to ensure the transfer of assets held was finalised in January 2020 and all signed admission agreements and additional guarantee are now held by the ACCTF.

The successful merge allowed the ACCTF to begin the buy-in process with the approval of the Pensions Committee and an understanding of the clear benefits that this method of de-risking would provide. It was decided following project work carried out by the First Group that the buy-in of pensioner liabilities only would attract the most insurance company interest and would be most cost effective for the ACCTF.

Since completion of the merge, the ACCTF have been working with buy-in specialists at Mercer to secure initial bids through a transparent procurement process.

Unfortunately, having given the insurers the opportunity to bid in early 2020, the COVID crisis and the effect on the assets held have meant that the project has been paused due to the current uncertainty. However, the ACCTF remain committed to progressing the buy-in at the earliest opportunity due to the benefits it will provide for both the ACCTF and First Group and hope to enter into an agreement in advance of the 2020 valuation results.

# 5. Financial Performance

| 2019/20 at a Glance | | |
|---|---|---|
| North East Scotland Pension Fund | | Aberdeen City Council Transport Fund |
| £144m | Contributions Receivable | £2m |
| £155m | Benefits Payable | £9m |
| £20m | Management Expenses | £290k |
| £(56)m | Net Return on Investments | £(6)m |
| £4,383m | Net Assets of the Fund at the End of Year | £309m |

# Key Statistics

| North East Scotland Pension Fund | | Aberdeen City Council Transport Fund |
|---|---|---|
| 50 | Total Number of Employers | 2 |
| 69,417 | Total Membership | 1,630 |

**2,049**
Votes at AGMs

**35%**
Members Registered for MSS

**985,629**
Updates Processed

**33.5**
Staff Employed (FTE)

**North East Scotland Pension Fund Financial Summary**

| | 2015/16 £'000 | 2016/17 £'000 | 2017/18 £'000 | 2018/19 £'000 | 2019/20 £'000 |
|---|---|---|---|---|---|
| Contributions Less Benefits and Expenses paid **Net Additions/ (Deductions)*** | **(13,485)** | **(15,456)** | **(18,219)** | **(19,697)** | **(30,977)** |
| Net Investment Income Change in Market Value **Net Return on Investment** | **23,929** | **648,411** | **329,035** | **363,300** | **(55,506)** |
| **Net Increase/ (Decrease) in Fund** | **10,444** | **632,955** | **310,816** | **343,603** | **(86,483)** |
| **Fund Balance as at 31 March (Market Value)** | **3,181,793** | **3,814,748** | **4,125,564** | **4,469,167** | **4,382,684** |

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

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

After meeting the cost of current benefits, all surplus cash is invested and the value of investments is then available to meet future liabilities.

**Budget**

| | Note | Actual Spend 2019/20 £’000 | Budget or Forecast* 2019/20 £’000 | Over or (Under) Spend 2019/20 £’000 |
|---|---|---|---|---|
| Administration Expenses | 1 | 1,822 | 2,036 | (214) |
| Oversight and Governance Expenses | 2 | 422 | 601 | (179) |
| Investment Management Expenses* | 3 | 17,953 | 20,083 | (2,130) |
| **Management Expenses Total** | | **20,197** | **22,720** | **(2,523)** |

Where the variance is +/- 5%, an explanation is outlined below:

1. Under spend – New staff posts some of which were recently filled and some yet to be filled.

2. Under spend – Reduction in actuarial fees, as focus switched to the merger of the Transport Funds.

3. Under spend – This is a forecast* rather than a traditional budget. This is largely due to the level of estimation and the extent of the unknown, especially given that the expenses are based upon an unpredictable market activity/value. However, the under spend is largely associated with the reduction in market value arising from the COVID-19 outbreak.

**Membership Statistics**

| **NESPF** | **2015/16** | **2016/17** | **2017/18** | **2018/19** | **2019/20** |
|---|---|---|---|---|---|
| Active | 24,546 | 25,329 | 25,568 | 25,892 | 26,275 |
| Pensioners | 18,328 | 19,111 | 20,023 | 21,029 | 22,156 |
| Deferred | 16,590 | 16,888 | 17,218 | 17,846 | 17,965 |
| Frozen Leavers | 1,865 | 2,232 | 2,435 | 2,759 | 3,021 |
| **Total** | **61,329** | **63,560** | **65,244** | **67,526** | **69,417** |

Active membership has risen from 2018/19 to 2019/20 with all of the local authorities showing an increase in the number of records held. As 2019/20 was a re-enrolment year for the larger authorities, members that had previously opted out of the scheme were taken back in automatically. Changes to payroll systems and the way employment records are held may also have had an impact on the number of pension records held for active members. Pensioner numbers continue to increase as the use of voluntary severance schemes encourage more eligible employees to take early retirement.

### Management Expenses

| | 2015/16 £'000 | 2016/17 £'000 | 2017/18 £'000 | 2018/19 £'000 | 2019/20 £'000 |
|---|---|---|---|---|---|
| Administration | 1,542 | 1,563 | 1,638 | 1,634 | 1,822 |
| Oversight and Governance | 348 | 468 | 467 | 474 | 422 |
| Investment Management | 14,627 | 16,455 | 19,092 | 18,665 | 17,953 |
| **Total Management Expenses** | **16,517** | **18,486** | **21,197** | **20,773** | **20,197** |

### Unit Cost Per Member

| | 2015/16 £ | 2016/17 £ | 2017/18 £ | 2018/19 £ | 2019/20 £ |
|---|---|---|---|---|---|
| Administrative Unit Cost per Member | 25.14 | 24.59 | 25.11 | 24.20 | 26.25 |
| Oversight and Governance Unit Cost per Member | 5.68 | 7.36 | 7.16 | 7.02 | 6.08 |
| Investment Management Unit Cost per Member | 238.50 | 258.89 | 292.62 | 276.41 | 258.62 |
| **Total Cost per Member** | **269.32** | **290.84** | **324.89** | **307.63** | **290.95** |

### Aberdeen City Council Transport Fund Financial Summary

| | 2015/16 £'000 | 2016/17 £'000 | 2017/18 £'000 | 2018/19 £'000 | 2019/20 £'000 |
|---|---|---|---|---|---|
| Contributions Less Benefits and Expenses paid **Net Additions/ (Deductions)*** | **(1,347)** | **(1,731)** | **(2,669)** | **(1,900)** | **(7,024)** |
| Net Investment Income Change in Market Value **Net Return on Investment** | **(2,050)** | **15,454** | **2,774** | **7,129** | **(5,836)** |
| **Net Increase/ (Decrease) in Fund** | **(3,397)** | **13,723** | **105** | **5,229** | **(12,860)** |
| **Transfer of Cash/Stock** | **0** | **0** | **0** | **0** | **216,388** |
| **Fund Balance as at 31 March (Market Value)** | **86,243** | **99,966** | **100,071** | **105,300** | **308,828** |

Net Additions/(Deductions)* - 'Management Expenses' are included within this figure resulting in a negative position.

## Membership Statistics

| Transport Fund | 2015/16 | 2016/17 | 2017/18 | 2018/19 | 2019/20 |
|---|---|---|---|---|---|
| Active | 71 | 61 | 48 | 42 | 77 |
| Pensioners | 411 | 423 | 434 | 429 | 1,373 |
| Deferred | 133 | 121 | 114 | 110 | 171 |
| Frozen Leavers | 9 | 9 | 9 | 9 | 9 |
| **Total** | **624** | **614** | **605** | **590** | **1,630** |

Following an application to the Scottish Public Pensions Agency (SPPA), Strathclyde No. 3 Fund merged with the Aberdeen City Council Transport Fund in the financial year 2019/20. All membership data held by Strathclyde Pension Fund was transferred electronically to the ACCTF in advance of the official merge with the first pension payment being made by the ACCTF on 15 September 2019. The transfer included 52 active members, 83 deferred members, 945 pensioners and 1 frozen leaver.

Both admission agreements for First Glasgow and First Aberdeen are closed to new entrants and are very mature in nature therefore the combined membership totals will continue to reduce on an annual basis.

## Management Expenses

| | 2015/16 £'000 | 2016/17 £'000 | 2017/18 £'000 | 2018/19 £'000 | 2019/20 £'000 |
|---|---|---|---|---|---|
| Administration | 46 | 50 | 51 | 50 | 60 |
| Oversight and Governance | 16 | 38 | 72 | 31 | 49 |
| Investment Management | 166 | 157 | 868 | 231 | 181 |
| **Total Management Expenses** | **228** | **245** | **991** | **312** | **290** |

## Unit Cost Per Member

| | 2015/16 £ | 2016/17 £ | 2017/18 £ | 2018/19 £ | 2019/20 £ |
|---|---|---|---|---|---|
| Administrative Unit Cost per Member | 73.72 | 81.43 | 84.30 | 84.75 | 36.81 |
| Oversight and Governance Unit Cost per Member | 25.64 | 61.89 | 119.01 | 52.54 | 30.06 |
| Investment Management Unit Cost per Member | 266.02 | 255.70 | 1,434.71 | 391.52 | 111.04 |
| **Total Cost per Member** | **365.38** | **399.02** | **1,638.02** | **528.81** | **177.91** |

## Remuneration Report

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

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

# 6. Economic and Market Background

It may seem a distant memory, however 2019 was a strong year for financial markets, with most asset classes delivering positive returns. We saw a stabilisation in global growth, helped by the US-China trade truce; plus, supportive economic monetary policies of central banks including the US Federal Reserve. Towards the end of January 2020, the World Health Organisation declared that Coronavirus (COVID-19) was a global pandemic as the virus spread across the world. This unprecedented event caused a major shock to global stock markets and our way of life. We have seen headline grabbing moves across most asset classes despite the unprecedented actions taken by governments and central banks to provide financial support to the world economy. Volatility was unprecedented with stocks having the best and worst sessions in a decade on consecutive days, moving around amid widespread investor concern.

**US**

Despite the significant political risks and fears of global economic slowdown, 2019 was great for US equities. The S&P 500 saw its best year since 2013 and Nasdaq had its loftiest annual performance in six years. The rally was driven by increasingly conciliatory negotiations between the U.S. and China and dovish policy from the Federal Reserve Bank. A sense of optimism spilled over into 2020, when US markets made fresh highs. However, news of the deadly COVID-19 spreading from China caused havoc, wiping out gains, leaving the US down just under 3%.

**UK**

UK markets had a slow start to 2019 with political uncertainty and Brexit worries subduing UK stocks. However, the passing of a withdrawal agreement by a newly elected UK parliament lifted sentiment and markets responded positively. As we came into 2020, and investors feared that the spread of COVID-19 would destroy economic growth, gains vanished, and the index closed down over 18%.

**Europe**

2019 was one of the best years for European equities in two decades after strong runs in 1999 and 2009. The market was driven by ample M&A activity and share buy backs as well as easing measures from the European Central Bank. However, Europe was not immune to steep sell offs and market volatility as the global pandemic took hold with the market closing down 8% for the 12 months to 31 March.

**Japan**

In 2019, Japan was the second-best performer among major indexes in Asia behind China. The market was buoyed by the Bank of Japan announcing a massive stimulus package to help its economy. However, after a promising start to 2020, stocks fell, as concerns about a Coronavirus-induced recession grew.

## Emerging Markets

Despite the volatility that afflicted the Emerging Markets for much of the year, the asset class produced positive returns in 2019. This in part driven by the rise of optimism that a trade deal may be forthcoming between the US and China. With the global outbreak front and centre, in the first quarter of 2020 the Emerging Markets were sharply down, finishing the 12 months to 31 March, down 13%.

## Bonds

Bond market returns were better than anticipated in 2019, as concerns about economic growth, inflation outlook and the likelihood of central banks raising interest rates all acted as positive catalysts for the asset class. This was largely validated by disappointing economic data in China, Europe and the US, and by a marked shift in the tone of the European Central Bank and Federal Reserve. This environment was supportive for developed and emerging government bonds, as well as high yield and investment grade debt issuances. However, Bond markets have not been immune to the COVID-19 crisis. Having initially rallied as equities fell, developed market government bond yields moved higher (i.e. prices fell) in mid-March. This is highly unusual in times of market stress and one explanation is that this was driven by market participants selling their most liquid assets to meet collateral requirements, or to raise cash. However, the announcement of trillions of dollars of stimulus from central banks around the world has reversed this sell-off. Elsewhere, Emerging Market government bonds have been materially affected by the current crisis with the main impact seen in their currencies. Credit spreads (the difference between the yield on a corporate bond and a sovereign bond of the same maturity) have also moved sharply wider indicating that corporate credit is seen as riskier than it was.

## Property

Over the 12 months to March 2020, according to the Morgan Stanley Capital International (MSCI) Monthly Index, property recorded a total return of 0.1%. This was markedly down on the 5.6% recorded over the previous 12-month period and the weakest since 2009. Capital values fell by 5.0% in the year to March 2020, with rental value growth negative at -0.2% and equivalent yield impact at -4.5%.

The retail sector continued to underperform over the 12-month period, posting a negative total return of -9.7% with COVID-19 adding to the headwinds impacting on investment sentiment and rental levels at the very end of the period. Indeed, monthly returns lower than the -4.2% recorded in March have only been seen twice in the 33 years of data. All other sectors delivered positive returns, with the small residential sample posting the highest total return of 6.3%, closely followed by industrials at 5.8% and offices at 3.9%.

Capital value growth was dispersed across sectors over the year to March, with the retail sector recording a large decrease of 15.3%, although its income return, at 6.6%, remained higher than all other sectors. Hotel capital values decreased by 3.8%, whilst industrials and residential delivered small but positive capital returns of 1.0% and 1.3% respectively over the 12-month period. Office values had been growing modestly but ended the period 0.9% lower after values fell 1.4% in the month of March.

Market rental values delivered positive, yet modest, growth for most sectors, with industrial, office and residential rents growing 3.1%, 1.9% and 1.1% respectively. Retail growth was negative at -5.2% for the year, highlighting challenging occupational market conditions for the sector.

| **Market Returns** | **1 Year (%)** | **3 Years (% p.a.)** | **5 Years (% p.a.)** |
|---|---|---|---|
| **Equities:** | | | |
| FTSE All Share Index | -18.5 | -4.2 | 0.6 |
| FTSE All World Index | -6.2 | 2.2 | 7.2 |
| FTSE All World ex UK | -5.5 | 2.6 | 7.6 |
| FTSE North American Index | -2.8 | 5.0 | 10.1 |
| FTSE European (ex UK) Index | -8.0 | -0.5 | 3.8 |
| FTSE Japan Index | -2.1 | 1.4 | 6.0 |
| FTSE Developed Asia (ex Japan) Index | -17.6 | -4.2 | 2.7 |
| FTSE Emerging Markets Index | -13.0 | -1.2 | 3.6 |
| **Bonds:** | | | |
| FTA Government Securities All Stocks | 9.9 | 4.6 | 4.7 |
| ML UK Corporate Bonds | 1.7 | 2.2 | 3.2 |
| FTA Index Linked All Stocks | 2.2 | 2.7 | 5.7 |
| Above are total returns in Sterling. Source: Datastream content from Refinitiv | | | |

# 7. NESPF Investment Strategy

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

There are a range of fund managers employed to again spread risk, with different style biases, each with clear and documented agreements in place detailing their investment mandates. The Funds also employ an independent Global Custodian to custody assets securely.

The objective of the investment strategy is to deliver long term returns which are greater than the growth in expenditure to be paid out in pensions. The investment strategy is monitored on an ongoing basis by the Pensions Committee and Pension Board, focusing on long term investment with consideration given to short term tactical considerations if appropriate.

The suitability of particular investments and types of investments are detailed in the Statement of Investment Principles. The Funds take proper advice at reasonable intervals regarding their investments, through their appointed advisors.

**Asset Structure 2019/20**

| **Asset Class** | **Distribution as at 31 March 2019** | | **Distribution as at 31 March 2020** | |
|---|---|---|---|---|
| | Fund Actual % | Fund Benchmark % | Fund Actual % | Fund Benchmark % |
| Equities (including Alternative Assets) | 76.0 | 57.5 | 65.5 | 57.5 |
| Bonds / Credit | 10.0 | 20.0 | 20.0 | 20.0 |
| Property / Infrastructure | 11.2 | 20.0 | 12.6 | 20.0 |
| Cash / Other | 2.8 | 2.5 | 1.9 | 2.5 |
| **Total** | **100.0** | **100.0** | **100.0** | **100.0** |

The NESPF continues to re-balance assets in line with its revised investment strategy, aiming to de-risk by reducing exposure to equities and increasing real assets and alternatives.

The current Investment Strategy for the North East Scotland Pension Fund is set out in the Statement of Investment Principles as follows:

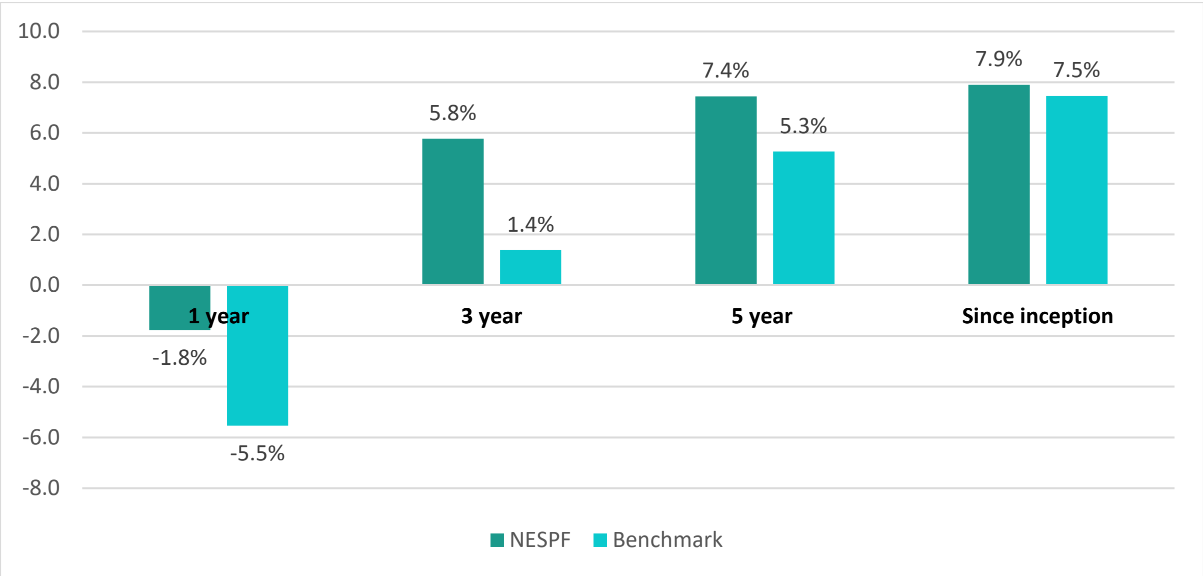
| | |
|---|---|
| Equities | 45.0% (range +/- 5%) |
| Alternative Assets (including private equity) | 12.5% (range +/- 5%) |
| Bonds / Credit | 20.0% (range +/- 5%) |
| Property / Infrastructure | 20.0% (range +/- 5%) |
| Cash / Other | 2.5% (range +/- 5%) |

**North East Scotland Pension Fund Performance**

For the best part of year 2019/20 investment returns were actually very strong and the Fund continued to re-balance and fold in investment gains made. However, towards the end of the period the unforeseeable impact of the COVID-19 pandemic struck and investment performance turned significantly, ending negatively across most asset classes. Risk assets, in particular equities have been more severely impacted, but this is why the Fund is well diversified and has other assets in the portfolio to provide defensive support.

It is notable that despite a difficult year, the Fund has outperformed the benchmark returns over all periods and comparators such as CPI and Average Earnings over the longer term. This provides assurance that the Fund's Investment Strategy will continue to deliver the required returns over the longer term.

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




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

| Year Ending | 2017/18<br><br><br>% | 2018/19<br><br><br>% | 2019/20<br><br><br>% | Since Inception Annualised<br>% |
|---|---|---|---|---|
| **CPI*** | 2.5 | 1.9 | 1.5 | 2.5 |
| **Average Earning*** | 2.6 | 3.2 | 2.4 | 2.9 |
| **NESPF Return** | 11.1 | 8.5 | -1.8 | 7.9 |

*Source: Office of National Statistics

**Investment Management Structure**

The Investment Management Structure is contained within Note 11: "Investments Analysed by Fund Manager" within the NESPF Accounts and within Note 9 of the ACC Transport Fund Accounts.

# 8. ACCTF De-Risking Strategy and Performance

The Aberdeen City Council Transport Fund has until recently been on a de-risking or "flightpath" strategy, therefore measuring performance versus Funding Level with the aim to being 100% funded and thus covering all liabilities.

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

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

Over the course of last year, the flightpath strategy returned 1.31% and is now in the process of being merged with the Strathclyde Transport Fund. This process will involve combining both sets of liabilities, effectively insuring out some of those liabilities known as a 'Buy In' and then re-assessing the investment strategy to align to the new target. All investment assets have now been received and at present there is an interim investment strategy in place to manage volatility, whilst the exercise is being conducted.

# 9. Risk

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

**Investment Risk** is recognised as falling into two distinct areas: Manager Skill (alpha) and Market Risk (beta). The structure of the Investment Strategy reflects this and is designed with the support of external expert advice. Details are contained in the Statement of Investment Principles and the Funding Strategy Statement.

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

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

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

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

### Risk Management

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

# 10. Funding Strategy Statement

The long term objective of the Funds' is to achieve and maintain sufficient assets in order to pay all pension benefits as they fall due. The Funding Strategy Statement (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 purpose of the FSS is therefore:

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

The FSS is required as part of Regulation 56 of the Local Government Pension Scheme (Scotland) Regulations 2018. As part of the 2017 actuarial valuation, the FSS for both the North East Scotland Pension Fund and the Aberdeen City Council Transport Fund were reviewed, with employers consulted on the revised version.

Copies of the full statement are available at www.nespf.org.uk

# 11. Statement of Investment Principles

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

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

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

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

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

The full statement is available at www.nespf.org.uk

# 12. Environmental, Social and Governance

As a long-term investor, the Funds have a duty to engage with the companies we invest in on Environmental, Social and Governance (ESG) issues.

**What makes engagement necessary?**

Put simply the interests of those who have control over a firm can differ from the interest of those who supply the firm with external finance i.e. the shareholders. With positive engagement you can help achieve better outcomes and awareness on topics such as executive compensation, environmental issues, corporate governance, and other topics falling outside of the usual financial and strategic conversations. The Funds believe engagement is the best approach to achieving better outcomes.

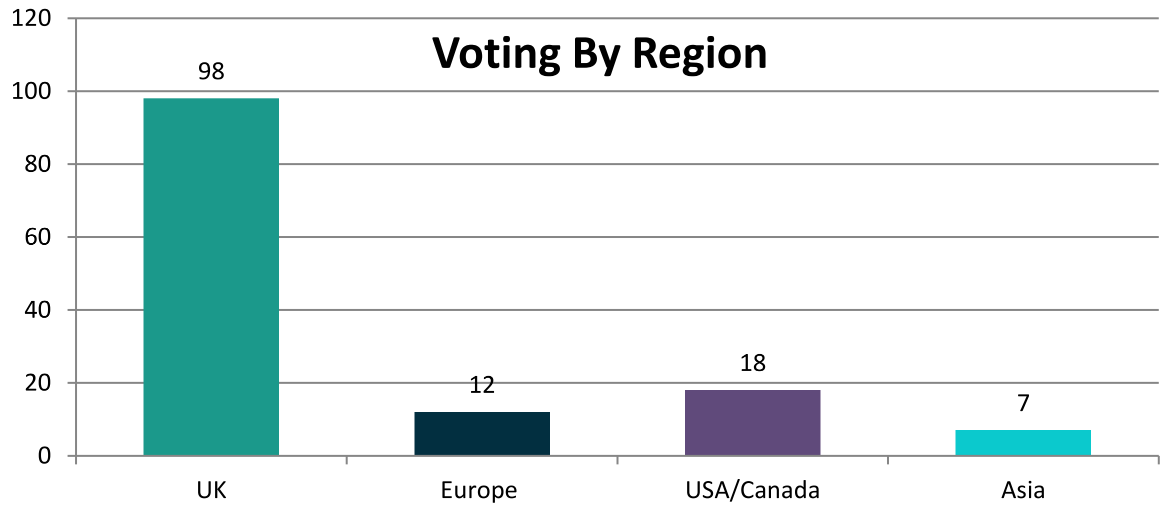
The below gives a snapshot of the activities that the Funds have undertaken on governance and engagement over the past year.

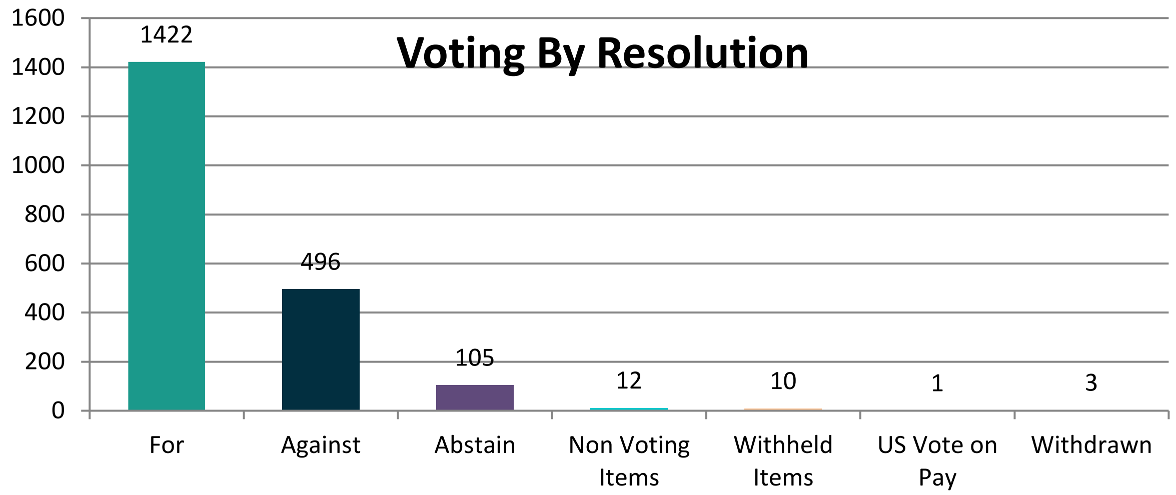
**Voting**

As an institutional shareholder we have a responsibility to make full use of our voting rights which enables the Funds to promote good governance practices in the companies in which we invest.

The Funds vote in-house on all our active Managers holdings and over the last year have voted at 135 Annual General Meetings/Special meetings on 2,049 resolutions. The Funds' voting advice is provided by P.I.R.C (Pensions & Investments Research Consultants Ltd). Additional advice is also received from the Local Authority Pension Fund Forum.

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




During the year to 31 March 2020, the main reasons for casting a vote against a resolution are listed below:

Annual Reports

- Vote on dividend or dividend policy not put to shareholders which is contrary to best practice.

Share Issues/Re-purchase

- No clear justification for the re-purchase put forward by the board.

Election of Directors

- Insufficient Independent representation on the board.
- Lack of board diversity.
- Concerns over aggregated time commitments.

## Engagement

### Local Authority Pension Fund Forum (LAPFF)

LAPFF is the UK's leading collaborative shareholder engagement group with combined assets of over £230 billion and brings together over 80 local authority pension funds and six pools. The Forum provides a unique opportunity for Britain's local authority pension funds to discuss shareholder engagement and investment issues. Councillor M. Tauqeer Malik, our Pensions Committee convenor, is a member of the LAPFF executive committee.

Some examples of the engagement work undertaken by LAPFF are noted below:

**Climate Change**

LAPFF's two main areas of work on this issue are:

1. Engagement - this work included raising climate risk and carbon management in nearly every direct company engagement. It has also involved being increasingly active in the Climate Action 100+ campaign and other international collaborative investor initiatives.
2. Social Impact – A Just Transition on Climate Change
   The social dimension of the transition to a resilient and zero-carbon economy has been given insufficient attention, notability in terms of the implications in the workforce and wider community. The entire Just Transition initiative is premised on the need to achieve a net zero economy for both social and environmental reasons.

Achievements

- Given that construction and building work contributes around 40% of the UK's total carbon footprint, addressing new build as well as retrofitting is a core component of the zero-carbon drive. A positive outcome here is Taylor Wimpey's commitment to set science-based targets.
- LAPFF was also able to leverage collaboration through its partnership with the US-based Climate Majority Project. Joining a call to the 20 largest carbon emitting US utility companies to commit to achieving net-zero carbon emissions by 2050. By the end of September, Entergy, NextEra, WEC Energy Group and NRG Energy indicated 2030 targets in line or ahead of science-based parameters.
- After consistent engagement with LAPFF and other investors ArcelorMittal announced an aim to be carbon neutral in European operations by 2050.

**Plastics**

During the last year the Forum has progressed work on the issue of plastics, joining a coalition of investors engaging with companies on the overall threats posed by plastic waste and pollution.

The Forum met with two companies on this issue, Nestle & PepsiCo, as well as discussing single use plastic specifically. Additionally, the Forum co-signed a letter to a range of companies on reducing plastic pellet loss. Pellet loss is incurred during both the manufacturing and transport stages, these pellets create pollution in the oceans and on the beaches.

Achievements

- Following on from engagement PepsiCo has committed to reducing use of virgin plastic across its portfolio by 35% by 2025. This is additional to the company's commitment to increase its use of recycled commitment in plastics packing by 30%.

The above are just a few examples of engagement carried out by LAPFF, more in-depth information can be found at http://www.lapfforum.org

## Climate Action 100+

Climate Action 100+ is an investor initiative launched in 2017.There are two categories of participation, Participant or Supporter. The Funds are a Supporter in this initiative.

Its aim is to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. More than 450 investors with over $40 trillion in assets collectively under management are engaging companies to:

- Curb emissions
- Improve governance
- Strengthen climate related financial disclosures

The companies include 100 'systemically important emitters', accounting for two-thirds of annual global industrial emissions, alongside more than 60 others with significant opportunity to drive the clean energy transition.

Achievements

- Rio Tinto has exited from mining coal, published a Task Force Climate-related Financial Disclosure (TCFD) report, and committed to an asset by asset review to set emissions reduction targets.
- Royal Dutch Shell released a statement committing to a range of industry leading climate commitments, including emissions reduction targets that include Scope 3 emissions.
- Maersk the world's biggest shipping company committed to net zero emissions by 2050.

The first progress report has now been produced and the full report can be found on our website-
http://www.nespf.org.uk/TheFund/Investment/ResponsibleInvestment/ResponsibleInvesting.aspx

## Principles for Responsible Investment (PRI)

PRI is the world's leading proponent of responsible investment.

It works to understand the investment implications of environmental, social and governance (ESG) factors and to support its international network of investor signatories in incorporating these factors into their investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

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

Through the year the Funds have added their name to:

| | |
|---|---|
| Feb 2020 | Legislation - Letter sent to the Securities and Exchange Commission in the USA on its proposed changes to shareholder proposals and proxy firms. |
| Aug 2019 | Deforestation – Statement to companies asking them to demonstrate clear commitment to eliminate deforestation within their operations and supply chains. |
| Jun 2019 | Climate Change – Global investor statement to governments in advance of G20 Summit in Osaka |
| Aug 2019 | Palm Oil - Statement of Investor expectations in the Palm Oil Industry |

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

# 13. Acknowledgement

The production of the Unaudited Annual Report and Accounts is very much a team effort involving many staff as well as information supplied by our advisors. We would like to take this opportunity to acknowledge the considerable efforts of staff in the production of the 2019/20 Unaudited Annual Report and Accounts.

**Angela Scott**
**Chief Executive**

**Jonathan Belford, CPFA**
**Chief Officer – Finance**

**Councillor M. Tauqeer Malik**
**Pensions Committee Convener**

**On behalf of Aberdeen City Council**

**30 June 2020**

# Statement of Responsibilities

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

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

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

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

- Approve the Annual Accounts for signature.

I confirm that these Unaudited Annual Accounts were approved for signature by the Urgent Business Committee, on behalf of the Pensions Committee, at its meeting on 30 June 2020.

Signed on behalf of Aberdeen City Council

**Councillor M. Tauqeer Malik**
**Pensions Committee Convener**

**The Chief Officer - Finance responsibilities:**

The Chief Officer - Finance is responsible for the preparation of the Pension Funds' Annual Accounts in accordance with proper practices as required by legislation and as set out in the CIPFA/LASAAC *Code of Practice on Local Authority Accounting in the United Kingdom* (the Accounting Code).

In preparing the Annual Accounts, the Chief Officer - Finance has:

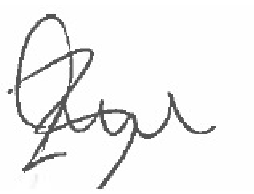
- selected suitable accounting policies and then applied them consistently;
- made judgements and estimates that were reasonable and prudent;
- complied with legislation;
- complied with the Local Authority Accounting Code (in so far as it is compatible with legislation).

The Chief Officer - Finance has also:

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

**Financial Position:**

I certify that the Unaudited Annual Accounts give a true and fair view of the financial position of the North East Scotland Pension Funds at the reporting date and the transactions of the Funds for the year ended 31 March 2020.



**Jonathan Belford, CPFA**
**Aberdeen City Council, Chief Officer – Finance**
**Date: 30 June 2020**

# Annual Governance Statement

### Scope of Responsibility

Aberdeen City Council has statutory responsibility for the administration of the Local Government Pension Scheme (LGPS) in the North East of Scotland.

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

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

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

### Purpose of the Governance Framework for North East Scotland Pension Funds

The governance framework comprises the systems, processes, culture and values by which the Administering Authority (including the Pension Funds) is directed and controlled. The Pension Funds comply with this framework ensuring that strategic objectives are monitored and to assess the effectiveness of services.

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

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

A governance framework has been in place at Aberdeen City Council and North East Scotland Pension Funds during 2019/20 and up to the date of approval of the Annual Report and Accounts.

**The Governance Framework**

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

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

The systems include:

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

These arrangements also include:

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

- Appropriate investment custody arrangements with a global custodian and access to the custodian's extensive internal control framework;
- Monitoring of appointed fund managers and third-party providers ensuring compliance within their management agreements and receipt of assurances from them on the adequacy of the internal financial control systems operated by them.

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

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

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

**Review of Effectiveness**

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

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

*Management Assurance*

As the administration of the Pension Funds was directly within the remit of the Chief Officer - Finance, assurance was sought from him in relation to the effectiveness of internal financial controls. These assurances include internal financial controls and provide the opportunity to highlight any weaknesses or areas of concern that should be taken account of. For 2019/20, no significant areas of weakness were highlighted.

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

Scrutiny Committee, City Growth and Resources Committee and the Pensions Committee.

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

*Assurance from Internal Audit*

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

During 2019/20, internal audit focused on the Pension Funds' Investment Strategy and Investment Performance Management with the outcome to be reported to the September 2020 Committee.

At the Pensions Committee meeting on the 20 March 2020, the 2020/21 internal audit plan was approved to review payroll. The audit will focus on the calculation and payment of new and ongoing pensions, and transfer and termination of pension payments.

*External Audit and Other External Scrutiny*

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

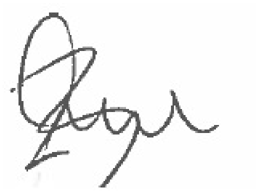
**Governance Compliance Statement**

The LGPS regulations require administering authorities to measure their governance arrangements against the standards set out in the guidance. Where compliance does not meet the published standard, there is a requirement for administering authorities to set out any reasons for non-compliance in their Governance Compliance Statement. In 2019/20, there were no significant issues to highlight on the Governance Compliance Statement.

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

**Certification**

It is our opinion that reasonable assurance can be placed upon the adequacy and effectiveness of systems of governance operated by Aberdeen City Council and the North East Scotland Pension Funds. The annual review demonstrates that the governance and internal control environment operated effectively during the 2019/20 financial year. On a quarterly basis, written updates regarding the Pension Funds' adherence to Investment Strategies and Performance are provided to the Pensions Committee.



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

**On behalf of Aberdeen City Council**

**30 June 2020**

# Governance Compliance Statement

| **Principle** | **Compliance** |
|---|---|
| **1. Structure** | |
| a) That representatives of participating LGPS employers, admitted bodies and Scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee. | Partially compliant as per the Scheme Governance Compliance Statement |
| b) The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing Council. | Fully compliant as per the Scheme Governance Compliance Statement |
| c) That where a secondary committee or panel has been established, the structure ensures effective communication across both levels. | |
| d) That where a secondary committee or panel has been established, at least one seat on the main committee is allocated for a member from the secondary committee or panel. | |
| **2. Committee Membership and Representation** | |
| a) That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include:-<br><br>i) employing authorities (including non-Scheme employers, e.g. admitted bodies),<br>ii) Scheme members (including deferred and pensioner Scheme members),<br>iii) where appropriate, independent professional observers, and<br>iv) expert advisors (on an ad-hoc basis). | Partially compliant as per the Scheme Governance Compliance Statement |
| b) That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers, meetings and training and are given full opportunity to contribute to the decision making process, with or without voting rights. | Fully compliant as per the Scheme Governance Compliance Statement |
| **3. Voting** | |
| a) The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees. | Fully compliant as per the Scheme Governance Compliance Statement |

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

# Accounting Policies

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

The Annual Accounts summarise the Funds' transactions for the 2019/20 financial year and its position at year end as at 31 March 2020.

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

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

**Contribution Income**

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

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

**Transfers to and from other Schemes**

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

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

**Investment Income**

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

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

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

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

The property portfolio accounts are prepared on an accruals basis.

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

**Fund Account - Expenses**

**Benefits Payable**

Pensions and lump sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the Net Assets Statement as current liabilities.

**Taxation**

The Funds are a registered public service Scheme under section 1 (1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax is accounted for as a Fund expense as it arises.

**Management Expenses**

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

**a.) Administrative Expenses and Oversight and Governance Costs**

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

**b.) Investment Management Expenses**

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

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

In addition, the Fund has negotiated performance related fees with several of its investment managers. Performance related fees were £6,047,983 in 2019/20 (2018/19 £6,146,372).

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

**Financial Assets**

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

**Valuation of Investments**

All investments are valued at their market value at 31 March 2020 and are determined as follows:

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

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

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

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

Unlisted investments are valued using one of the following methodologies:

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

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

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

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

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

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

**Derivatives**

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

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

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

**Cash**

Cash comprises of cash in hand and demand deposits.

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

**Financial Liabilities**

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

## Actuarial Present Value of Promised Retirement Benefits

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

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

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

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

## Additional Voluntary Contributions

North East Scotland Pension Funds provides an additional voluntary contributions (AVC) Scheme for its members, the assets of which are invested separately from those of the Pension Fund. The Fund has appointed Prudential as its AVC provider together with Standard Life. AVCs are paid to the AVC provider by the employers and are specifically for providing additional benefits for the individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and the movements in the year, from each service provider. AVCs are not included within the Annual Accounts however they are detailed in a Note to the Accounts.

## Critical Judgments in applying Accounting Policies

## Unquoted Private Equity/Debt and Infrastructure Investments

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

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

The value of unquoted investments at 31 March 2020 was £501,227,186 (31 March 2019 £323,345,002).

## Actuarial Present Value of Promised Retirement Benefits

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

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

## Events after the Reporting Period

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

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

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

## Changes in Accounting Policies

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

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

When a new or amended accounting standard has been issued but not yet adopted, the Code requires the disclosure of information relating to its impact. The following new or amended standards have been published but not yet adopted:

- **IFRS 16 Leases –** will affect new lease classifications for directly held investment properties. Implementation of this standard has been deferred to 1 April 2021. Therefore, the impact of this standard is not considered for 2019/20.

- **Amendments to IAS 28 Investments in Associates and Joint Ventures: Long Term Interests in Associates and Joint Ventures.** This amendment clarifies that a company applies IFRS9 Financial Instruments to long term interests in an associate or joint venture that form part of the net investment in the associate or joint venture.  This will have no impact as the Fund already complies.
- **Amendments to IAS 28 Employee Benefits:** Plan Amendment, Curtailment or Settlement. This amendment specifies how organisations determine pension expenses when changes to a defined benefit pension plan occur.

## NORTH EAST SCOTLAND PENSION FUND ACCOUNTS

### Fund Account for the year ended 31 March 2020

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

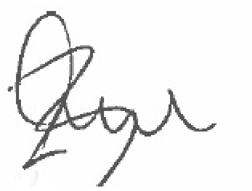
| | Notes | 2018/19 | 2019/20 |
|---|---|---|---|
| | | £'000 | £'000 |
| | | | |
| **Contributions Receivable** | | | |
| Employees' Contributions | 2 | 30,242 | 30,857 |
| Employers' Contributions | 2 | 108,618 | 110,335 |
| Transfer Values | 3 | 2,905 | 2,811 |
| Other Income | | 6 | 4 |
| | | | |
| | | **141,771** | **144,007** |
| | | | |
| **Benefits Payable** | | | |
| Retirement Pensions | 4 | 106,572 | 114,657 |
| Retirement Allowances | 4 | 25,574 | 30,298 |
| Death Gratuities | 4 | 4,061 | 4,189 |
| Contributions Refunded | 5 | 598 | 571 |
| Transfer Values | 5 | 3,890 | 5,072 |
| | | | |
| | | **140,695** | **154,787** |
| | | | |
| **Management Expenses** | 6 | **20,773** | **20,197** |
| | | | |
| **Return on Investment** | | | |
| Investment Income | 7 | 54,805 | 56,316 |
| Profits and (Losses) on Disposal of Investments and Changes in Market Value of Investments | 8 | 308,495 | (111,822) |
| | | | |
| **Net Return on Investments** | | **363,300** | **(55,506)** |
| | | | |
| **Net Increase/(Decrease) in the Net Assets available for Benefits during the year** | | **343,603** | **(86,483)** |
| | | | |
| **Opening Net Assets of the Fund** | | **4,125,564** | **4,469,167** |
| | | | |
| **Net Assets of the Fund at the end of the year** | | **4,469,167** | **4,382,684** |

## NORTH EAST SCOTLAND PENSION FUND ACCOUNTS

### Net Assets Statement as at 31 March 2020

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

| | **Notes** | **2018/19** | **2019/20** |
|---|---|---|---|
| | | **£'000** | **£'000** |
| | | | |
| **Investment Assets** | | | |
| UK Equities | | 766,975 | 561,127 |
| Overseas Equities | | 921,354 | 811,137 |
| Pooled Vehicles - Other | | 1,849,246 | 1,947,975 |
| Pooled Infrastructure | | 130,600 | 174,427 |
| Direct Property | 13 | 328,025 | 348,750 |
| Private Equity – Other | | 280,903 | 339,784 |
| Private Debt | | 18,428 | 85,111 |
| Funds held by Investment Managers | | 71,971 | 60,266 |
| ACC Loans Fund Deposit | 19 | 106,700 | 67,480 |
| Investment Income Due | | 5,799 | 3,685 |
| Investment Sales Amount Receivable | | 664 | 0 |
| | | | |
| **Total Investment Assets** | | **4,480,665** | **4,399,742** |
| | | | |
| **Investment Liabilities** | | | |
| Investment Purchases Amount Payable | | (890) | (1,711) |
| | | | |
| **Net Investment Assets** | | **4,479,775** | **4,398,031** |
| | | | |
| **Long Term Assets** | 18a | **0** | **81** |
| | | | |
| Current Assets | 18b | 16,026 | 15,106 |
| Current Liabilities | 18c | (26,634) | (30,534) |
| **Net Current Assets/(Liabilities)** | | **(10,608)** | **(15,428)** |
| | | | |
| **Net Assets of the Fund at the end of the year** | | **4,469,167** | **4,382,684** |



**Jonathan Belford, CPFA**
**Aberdeen City Council, Chief Officer – Finance**
**Date: 30 June 2020**

## ABERDEEN CITY COUNCIL TRANSPORT FUND ACCOUNTS

### Fund Account for the year ended 31 March 2020

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

| | Notes | 2018/19 | 2019/20 |
|---|---|---|---|
| | | **£'000** | **£'000** |
| | | | |
| **Contributions Receivable** | | | |
| Employees' Contributions | 2 | 72 | 129 |
| Employers' Contributions | 2 | 1,943 | 1,908 |
| Other Income | | 305 | 348 |
| | | | |
| | | **2,320** | **2,385** |
| | | | |
| **Benefits Payable** | | | |
| Retirement Pensions | 3 | 3,243 | 7,061 |
| Retirement Allowances | 3 | 337 | 1,734 |
| Death Gratuities | 3 | 328 | 324 |
| | | | |
| | | **3,908** | **9,119** |
| | | | |
| **Management Expenses** | 5 | **312** | **290** |
| | | | |
| **Return on Investment** | | | |
| Investment Income | 6 | 104 | 224 |
| Profits and (Losses) on Disposal of Investments and Changes in Market Value of Investments | 7a | 7,025 | (6,060) |
| | | | |
| **Net Return on Investments** | | **7,129** | **(5,836)** |
| | | | |
| **Net Increase/ (Decrease) in the Net Assets available for Benefits during the year** | | **5,229** | **(12,860)** |
| | | | |
| **Transfer of Strathclyde Transport Fund Assets (Cash & Stock)** | 7b | **0** | **216,388** |
| | | | |
| **Opening Net Assets of the Fund** | | **100,071** | **105,300** |
| | | | |
| **Net Assets of the Fund at the end of the year** | | **105,300** | **308,828** |

## ABERDEEN CITY COUNCIL TRANSPORT FUND ACCOUNTS

### Net Assets Statement as at 31 March 2020

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

| | Notes | 2018/19 | 2019/20 |
|---|---|---|---|
| | | **£'000** | **£'000** |
| | | | |
| **Investment Assets** | | | |
| Index Linked Securities | | 27,793 | 164,934 |
| Pooled Vehicle | | 76,192 | 135,282 |
| Funds held by Investment Managers | | 4,093 | 8,304 |
| ACC Loans Fund Deposit | 16 | 228 | 429 |
| Investment Income Due | | 3 | 148 |
| Investment Sales Amount Receivable | | 918 | 0 |
| | | | |
| **Total Investment Assets** | | **109,227** | **309,097** |
| | | | |
| **Investment Liabilities** | | | |
| Investment Purchases Amount Payable | | (3,999) | (675) |
| | | | |
| **Net Investment Assets** | | **105,228** | **308,422** |
| | | | |
| | | | |
| **Long Term Assets** | 15a | **296** | **269** |
| | | | |
| Current Assets | 15b | 192 | 909 |
| | | | |
| Current Liabilities | 15c | (416) | (772) |
| | | | |
| **Net Current Assets/ (Liabilities)** | | **(224)** | **137** |
| | | | |
| **Net Assets of the Fund at the end of the year** | | **105,300** | **308,828** |

**Jonathan Belford, CPFA**
**Aberdeen City Council, Chief Officer – Finance**
**Date: 30 June 2020**

# NOTES TO THE NORTH EAST SCOTLAND PENSION FUND ACCOUNTS

## Note 1: Actuarial Valuation Report

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

Information from the 2017 Actuarial Valuation is detailed below:

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

### Funding Level

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

### Achieving the Solvency Funding Target

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

The valuation determined that the average employer cost of providing members benefits across the Fund was 22.0% (the Primary contribution rate.) By spreading the surplus over 24 years the Secondary contribution rate for the whole Fund is -2.6% meaning that the average employer contribution rate is 19.4% of pensionable pay.

In practice, each employer’s position is assessed separately, details of which can be found in the 2017 Actuarial Valuation. This sets out the contributions for each employer over the 3 year period to 31 March 2021.

### Schedule to the Rates and Adjustments Certificate

The Schedule to the Rates and Adjustments Certificate for the Fund sets out the contributions for the employer over the 3 year period to 31 March 2021. The rates have been determined in accordance with the FSS. Any adjustments made to the rates proposed by the Scheme Actuary were made as a result of the consultation carried out by the Fund and were made in line with the approaches agreed with the Scheme Actuary. Contribution requirements for the period from 1 April 2021 onwards will be revised as part of the next actuarial valuation as at 31 March 2020 and will be confirmed in the Rates and Adjustments Certificate and Schedule accompanying that valuation report.

**Assumptions used to Calculate Funding Target**

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

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

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

**Actuarial Statement**

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

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standards 26 (IAS 26) assumptions, is estimated to be £5,252m (2019 £5,422m). Included within the calculation for 2020 is an amount of less than £100,000 by way of an estimate of the effect of the McCloud judgement. These figures are used for the statutory accounting purposes by North East Scotland Pension Fund and complies with the requirements of IAS 26.

These calculations are only prepared for the purposes of IAS 26 and have no validity in other circumstances. It is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

The full statement by the Scheme Actuary, including notes on the McCloud judgement, can be found in Appendix 1.

## Note 2: Contributions Receivable

| By Category | 2018/19 | 2019/20 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| **Employees' Normal Contributions** | **30,242** | **30,857** |
| | | |
| Employers' Normal Contributions | 106,088 | 107,777 |
| Employers' Deficit Recovery Contributions | 2,530 | 2,558 |
| **Total Employers' Contributions** | **108,618** | **110,335** |
| | | |
| **Total** | **138,860** | **141,192** |

| By Authority | 2018/19 | 2019/20 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| Administering Authority | 42,486 | 40,926 |
| Scheduled Bodies | 82,470 | 86,618 |
| Admitted Bodies | 9,087 | 8,727 |
| Transferee Admission Bodies | 4,817 | 4,921 |
| | | |
| **Total** | **138,860** | **141,192** |

## Note 3: Transfers in from other Pension Funds

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| Individual Transfers | 2,905 | 2,811 |
| | | |
| **Total** | **2,905** | **2,811** |

## Note 4: Benefits Payable

| By Category | 2018/19 | 2019/20 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| Pensions | 106,572 | 114,657 |
| Commutation and Lump Sum Retirement Benefits | 25,574 | 30,298 |
| Lump Sum Death Benefits | 4,061 | 4,189 |
| | | |
| **Total** | **136,207** | **149,144** |

| By Authority | 2018/19 | 2019/20 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Administering Authority | 36,309 | 41,103 |
| Scheduled Bodies | 88,538 | 94,819 |
| Admitted Bodies | 9,934 | 11,408 |
| Transferee Admission Bodies | 1,426 | 1,814 |
| | | |
| **Total** | **136,207** | **149,144** |

### Note 5: Payment to and on Account of Leavers

| | 2018/19 | 2019/20 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Refunds to Members Leaving Service | 599 | 565 |
| Payments for Members Joining State Scheme | (1) | 6 |
| Individual Transfers | 3,890 | 5,072 |
| | | |
| **Total** | **4,488** | **5,643** |

## Note 6: Management Expenses

| | 2018/19 | 2019/20 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Pension Fund Staffing Costs – Administration | 1,084 | 1,203 |
| Information Technology | 366 | 400 |
| Supplies & Services | 83 | 115 |
| Accommodation | 79 | 84 |
| Printing and Publications | 22 | 20 |
| **Administration Expenses Total** | **1,634** | **1,822** |
| | | |
| Pension Fund Staffing Costs – Investment | 159 | 168 |
| Pension Fund Committee | 12 | 16 |
| Pension Board | 1 | 8 |
| External Audit Fee | 39 | 40 |
| Internal Audit Fee | 8 | 7 |
| Actuarial Fees | 113 | 49 |
| General Expenses | 142 | 134 |
| **Oversight and Governance Expenses Total** | **474** | **422** |
| | | |
| Investment Management | 10,721 | 10,293 |
| Performance Fees | 6,146 | 6,048 |
| Direct Operating Property Expenses | 186 | 664 |
| Transaction Costs | 1,477 | 823 |
| Custody Fees | 135 | 125 |
| **Investment Management Expenses Total** | **18,665** | **17,953** |
| | | |
| **Management Expenses Grand Total** | **20,773** | **20,197** |

### Analysis of Transaction Costs:

| Commission £'000 | Fees/ Tax £'000 | 2018/19 Total £'000 | Asset Type | Commission £'000 | Fees/ Tax £'000 | 2019/20 Total £'000 |
|---|---|---|---|---|---|---|
| | | | | | | |
| 0 | 0 | **0** | Fixed Income | 0 | 0 | **0** |
| 319 | 747 | **1,066** | Equities | 192 | 397 | **589** |
| 0 | 267 | **267** | Pooled Infrastructure | 0 | 234 | **234** |
| 0 | 144 | **144** | Private Equity | 0 | 0 | **0** |
| | | | | | | |
| **319** | **1,158** | **1,477** | **Total** | **192** | **631** | **823** |

**Note 7: Investment Income**

| | 2018/19 | 2019/20 |
|---|---|---|
| | **£'000** | **£'000** |
| | | |
| Equity Dividends | 27,079 | 25,573 |
| | | |
| Property Rental Income | 15,690 | 17,442 |
| | | |
| Interest on Cash Deposit | 689 | 1,395 |
| | | |
| Pooled Infrastructure* | 6,734 | 7,506 |
| | | |
| Private Equity* | 485 | 670 |
| | | |
| Private Debt* | 0 | 1,946 |
| | | |
| Other (including P/L from Currency & Derivatives) | 4,897 | 1,962 |
| | | |
| **Total** | **55,574** | **56,494** |
| | | |
| **Tax** | | |
| Withholding Tax – Fixed Interest Securities | 0 | 0 |
| Withholding Tax – Equities | (769) | (178) |
| Withholding Tax – Pooled | 0 | 0 |
| | | |
| **Total Tax** | **(769)** | **(178)** |
| | | |
| **Net Total** | **54,805** | **56,316** |

***Note: Previously included within 'Other' Income**

**Note 8: Investment Assets**

Reconciliation of Movements in Investments and Derivatives

| | **Market Value 31 March 2019** | **Purchases** | **Sales** | **Change in Market Value** | **Market Value 31 March 2020** |
|---|---|---|---|---|---|
| | **£'000** | **£'000** | **£'000** | **£'000** | **£'000** |
| | | | | | |
| UK Equities | 766,975 | 83,732 | (182,766) | (106,814) | 561,127 |
| Overseas Equities | 921,354 | 62,690 | (291,957) | 119,050 | 811,137 |
| Pooled Other | 1,849,246 | 383,504 | (131,066) | (153,709) | 1,947,975 |
| Pooled Infrastructure | 130,600 | 58,489 | (4,109) | (10,553) | 174,427 |
| Property | 328,025 | 28,849 | 0 | (8,124) | 348,750 |
| Private Equity | 280,903 | 51,997 | (42,637) | 49,521 | 339,784 |
| Private Debt | 18,428 | 73,883 | (6,007) | (1,193) | 85,111 |
| | | | | | |
| | **4,295,531** | **743,144** | **(658,542)** | **(111,822)** | **4,268,311** |
| | | | | | |
| **Derivative Contracts** | | | | | |
| | | | | | |
| FX Contracts | 0 | 0 | 0 | 0 | 0 |
| | | | | | |
| | **4,295,531** | **743,144** | **(658,542)** | **(111,822)** | **4,268,311** |
| | | | | | |
| **Other** | | | | | |
| | | | | | |
| Cash | 178,671 | | | | 127,746 |
| Investment Income Due | 5,799 | | | | 3,685 |
| Investment Sales Amount Receivable | 664 | | | | 0 |
| Investment Purchases Amounts Payable | (890) | | | | (1,711) |
| | | | | | |
| **Net Investment Assets** | **4,479,775** | | | | **4,398,031** |

Reconciliation of Movements in Investment and Derivatives (continued)

| | **Market Value 31 March 2018** | **Purchases** | **Sales** | **Change in Market Value** | **Market Value 31 March 2019** |
|---|---|---|---|---|---|
| | **£'000** | **£'000** | **£'000** | **£'000** | **£'000** |
| | | | | | |
| UK Equities | 734,875 | 170,380 | (157,517) | 19,237 | 766,975 |
| Overseas Equities | 819,078 | 105,501 | (157,630) | 154,405 | 921,354 |
| Pooled Other | 1,855,823 | 9,918 | (96,768) | 80,273 | 1,849,246 |
| Pooled Infrastructure | 88,899 | 39,576 | (1,662) | 3,787 | 130,600 |
| Property | 293,045 | 35,652 | (4,323) | 3,651 | 328,025 |
| Private Equity | 232,461 | 59,967 | (58,780) | 47,255 | 280,903 |
| Private Debt | 0 | 17,549 | (94) | 973 | 18,428 |
| | | | | | |
| | **4,024,181** | **438,543** | **(476,774)** | **309,581** | **4,295,531** |
| | | | | | |
| **Derivative Contracts** | | | | | |
| | | | | | |
| FX Contracts | 0 | 33,374 | (32,288) | (1,086) | 0 |
| | | | | | |
| | **4,024,181** | **471,917** | **(509,062)** | **308,495** | **4,295,531** |
| | | | | | |
| **Other** | | | | | |
| | | | | | |
| Cash | 113,484 | | | | 178,671 |
| Investment Income Due | 0 | | | | 5,799 |
| Investment Sales Amount Receivable | 0 | | | | 664 |
| Investment Purchases Amounts Payable | 0 | | | | (890) |
| | | | | | |
| **Net Investment Assets** | **4,137,665** | | | | **4,479,775** |

## Note 9: Analysis of Investments

| | 2018/19 | 2019/20 |
|---|---|---|
| | **£'000** | **£'000** |
| | | |
| **Equities** | | |
| | | |
| **UK** | | |
| Quoted | 766,975 | 561,127 |
| | | |
| **Overseas** | | |
| Quoted | 921,354 | 811,137 |
| | | |
| **Subtotal Equities** | **1,688,329** | **1,372,264** |
| | | |
| **Pooled Funds (Other) – Additional Analysis** | | |
| | | |
| **UK** | | |
| Unit Trusts | 872,300 | 741,632 |
| Pooled Indexed Linked | 202,644 | 206,888 |
| | | |
| **Overseas** | | |
| Unit Trusts | 652,004 | 791,417 |
| Global Pooled Bonds | 122,298 | 208,038 |
| | | |
| **Subtotal Pooled Funds (Other)** | **1,849,246** | **1,947,975** |
| | | |
| Pooled Infrastructure - Quoted | 106,586 | 98,094 |
| Pooled Infrastructure - Unquoted | 24,014 | 76,333 |
| **Subtotal Pooled Infrastructure** | **130,600** | **174,427** |
| | | |
| Property, Direct | 328,025 | 348,750 |
| Private Equity | 280,903 | 339,784 |
| Private Debt | 18,428 | 85,111 |
| Funds held by Investment Managers | 71,971 | 60,266 |
| ACC Loans Fund Deposit | 106,700 | 67,480 |
| Investment Income Due | 5,799 | 3,685 |
| Investment Sales Amount Receivable | 664 | 0 |
| | | |
| **Investment Assets Total** | **4,480,665** | **4,399,742** |
| | | |
| **Investment Liabilities** | | |
| | | |
| Investment Purchases Amounts Payable | (890) | (1,711) |
| | | |
| **Investment Liabilities Total** | **(890)** | **(1,711)** |
| | | |
| **Net Investment Assets** | **4,479,775** | **4,398,031** |

## Note 10: Analysis of Derivatives

### Futures

There were no outstanding exchange traded future contracts as at 31 March 2020.

### Forward Foreign Currency

There were no outstanding forward foreign currency contracts as at 31 March 2020.

## Note 11: Investments Analysed by Fund Manager

| | 31 March 2019 | | 31 March 2020 | |
|---|---|---|---|---|
| | £'000 | % | £'000 | % |
| | | | | |
| **Investment Assets** | | | | |
| State Street Global Advisors | 1,403,222 | 31.3 | 1,234,017 | 28.1 |
| Baillie Gifford | 1,237,351 | 27.7 | 1,022,435 | 23.3 |
| BlackRock Asset Management | 500,158 | 11.2 | 388,970 | 8.9 |
| BlackRock Diversified Growth Fund | 162,322 | 3.6 | 158,096 | 3.6 |
| Baring Asset Managers | (3) | 0.0 | (3) | 0.0 |
| AAM Property (API) | 364,367 | 8.1 | 370,869 | 8.5 |
| AAM Property Residential | 7,963 | 0.2 | 9,138 | 0.2 |
| HarbourVest | 113,833 | 2.5 | 139,992 | 3.2 |
| Standard Life | 29,677 | 0.7 | 26,333 | 0.6 |
| ACC Loans Fund Deposit | 106,700 | 2.4 | 67,480 | 1.5 |
| Global Custodian | 18,818 | 0.4 | 15,409 | 0.4 |
| Partners Group | 57,569 | 1.3 | 63,218 | 1.4 |
| Maven Capital | 2,043 | 0.1 | 1,474 | 0.0 |
| Capital Dynamics | 26,118 | 0.6 | 36,798 | 0.8 |
| RCP Advisors | 16,078 | 0.4 | 25,455 | 0.6 |
| Unigestion | 30,495 | 0.7 | 50,473 | 1.2 |
| Invesco Diversified Growth Fund | 150,707 | 3.4 | 152,724 | 3.5 |
| Russell Overlay | 0 | 0.0 | 0 | 0.0 |
| Russell Multi Asset Credit | 103,035 | 2.3 | 91,021 | 2.1 |
| Russell Transition | 294 | 0.0 | 312 | 0.0 |
| Aviva Infrastructure | 106,586 | 2.4 | 98,094 | 2.2 |
| Hermes Infrastructure | 24,014 | 0.5 | 76,440 | 1.7 |
| Alcentra | 18,428 | 0.4 | 54,126 | 1.2 |
| Hayfin Direct Lending | 0 | 0.0 | 30,985 | 0.7 |
| Insight Credit | 0 | 0.0 | 284,175 | 6.5 |
| | **4,479,775** | **100.2** | **4,398,031** | **100.2** |
| | | | | |
| **Net Long and Current Assets** | | | | |
| Bank Account | 19 | 0.0 | 27 | 0.0 |
| Long Term and Current Debtors Less Creditors | (10,627) | (0.2) | (15,374) | (0.2) |
| | | | | |
| **Net Assets** | **4,469,167** | **100.0** | **4,382,684** | **100.0** |

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

| Security | Market Value 31 March 2019 | % of Net Investment Assets | Market Value 31 March 2020 | % of Net Investment Assets |
|---|---|---|---|---|
| | **£'000** | | **£'000** | |
| | | | | |
| MPF International Equity Index Pooled Fund | 548,970 | 12.3 | 416,221 | 9.46 |
| MPF UK Equity Pooled Fund | 529,305 | 11.9 | 402,869 | 9.16 |
| Insight Investment Mgt Global Funds | 0 | 0.0 | 284,175 | 6.46 |

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

**Note 12: Stock Lending**

| | 31 March 2019 | Collateral Percentage | 31 March 2020 | Collateral Percentage |
|---|---|---|---|---|
| | **£'000** | | **£'000** | |
| | | | | |
| **Stock on Loan** | | | | |
| | | | | |
| Equities | 398,546 | | 305,518 | |
| Fixed Interest | 0 | | 0 | |
| **Total Exposure** | **398,546** | | **305,518** | |
| **Total Collateral** | **425,845** | **107%** | **329,942** | **108%** |

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

Collateral is held at 108% in respect of each borrower, consisting of Government Debt, UK and Overseas Equities.

## Note 13: Property Holdings

| | 2018/19 | 2019/20 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| **Opening Balance** | **293,045** | **328,025** |
| Purchases | 26,440 | 27,671 |
| Construction | 9,227 | 676 |
| Subsequent Expenditure | (15) | 502 |
| Disposals | (4,323) | 0 |
| Net Increase in Market Value | 3,651 | (8,124) |
| | | |
| **Closing Balance** | **328,025** | **348,750** |

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

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

| | 2018/19 | 2019/20 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Within One Year | 17,049 | 17,266 |
| Between One Year and Five Years | 59,748 | 62,912 |
| Later than Five Years | 100,571 | 98,659 |
| | | |
| **Total** | **177,368** | **178,837** |

In accordance with IAS17, the above table has been presented using the 'break date' of the lease agreements.

Based upon the Fund's own historic experience but also on similar properties received from the Fund's property letting agents, the above disclosure has been reduced by a credit loss allowance for one property, but not thought to be material.

During the year 2019/20, one tenant went into administration and a new turnover based lease was agreed with no base rent.

## Note 14: Financial and Non-Financial Instruments

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

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

| 31 March 2019 | | | | 31 March 2020 | | |
|---|---|---|---|---|---|---|
| **Designated as Fair Value through Profit & Loss** | **Assets at Amortised Cost** | **Financial Liabilities at Amortised Cost** | | **Designated as Fair Value through Profit & Loss** | **Assets at Amortised Cost** | **Financial Liabilities at Amortised Cost** |
| **£'000** | **£'000** | **£'000** | | **£'000** | **£'000** | **£'000** |
| | | | **Financial Assets** | | | |
| | | | | | | |
| 1,688,329 | | | Equities | 1,372,264 | | |
| 1,849,246 | | | Pooled Other | 1,947,975 | | |
| 130,600 | | | Pooled Infrastructure | 174,427 | | |
| 280,903 | | | Private Equity | 339,784 | | |
| 18,428 | | | Private Debt | 85,111 | | |
| | 178,671 | | Cash | | 127,746 | |
| | 6,463 | | Other Investment Balances | | 3,685 | |
| | 16,026 | | Debtors | | 15,187 | |
| | | | | | | |
| **3,967,506** | **201,160** | | **Subtotal** | **3,919,561** | **146,618** | |
| | | | | | | |
| | | | **Financial Liabilities** | | | |
| | | | | | | |
| | | (890) | Other Investment Balances | | | (1,711) |
| | | (26,634) | Creditors | | | (30,534) |
| | | | | | | |
| | | **(27,524)** | | | | **(32,245)** |
| | | | | | | |
| **3,967,506** | **201,160** | **(27,524)** | **Financial Instruments Total** | **3,919,561** | **146,618** | **(32,245)** |
| | | | | | | |
| | | | **Non-Financial Instruments** | | | |
| | | | | | | |
| 328,025 | | | Property | 348,750 | | |
| | | | | | | |
| **4,295,531** | **201,160** | **(27,524)** | | **4,268,311** | **146,618** | **(32,245)** |
| | | **4,469,167** | **Net Assets of the Fund** | **4,382,684** | | |

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

| 31 March 2019 | | 31 March 2020 |
|---:|---|---:|
| **£'000** | **Financial Assets** | **£'000** |
| | | |
| 304,844 | Fair Value through Profit and Loss | (103,698) |
| | | |
| | **Financial Liabilities** | |
| | | |
| 0 | Fair Value through Profit and Loss | 0 |
| | | |
| **304,844** | **Net Gains and Losses on Financial Instruments** | **(103,698)** |
| | | |
| | **Non-Financial Instruments** | |
| | | |
| 3,651 | Fair Value through Profit and Loss | (8,124) |
| | | |
| **308,495** | **Net Gains and Losses of the Fund** | **(111,822)** |

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

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

### Level 1

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

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

### Level 2

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

### Level 3

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

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

The values of the investments in unquoted private equity/debt and infrastructure are based on valuations provided by the general partners to the funds in which North East Scotland Pension Fund has invested.

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

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

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

**Note 16a: Fair Value – Basis of Valuation**

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

| Description of Asset | Valuation Hierarchy | Basis of Valuation | Observable and Unobservable Inputs | Key Sensitivities Affecting the Valuations Provided |
|---|---|---|---|---|
| Market Quoted Investments | Level 1 | Published bid market price ruling on the final day of the accounting period | Not required | Not required |
| Quoted Bonds | Level 1 | Fixed interest securities are valued at a market value based on current yields | Not required | Not required |
| Exchange Traded Pooled Investments | Level 1 | Closing bid value on published exchanges | Not required | Not required |
| Forward Foreign Exchange Derivatives | Level 2 | Market forward exchange rates at the year-end | Exchange rate risk | Not required |
| Pooled Investments – Overseas Unit Trusts and Property Funds | Level 2 | Closing bid price where bid and offer prices are published.<br>Closing single price where single price published | NAV-based pricing set on a forward pricing basis | Not required |
| Freehold and Leasehold Properties | Level 2 | Valued at fair value at the year -end using the investment method of valuation by Claire Magowan MRICS under the supervision of Tim Ainsley MRICS of Savills | Existing lease terms and rentals<br>Independent market research Nature of Tendencies Covenant Strength for | |

| | | | | |
|---|---|---|---|---|
| | | in accordance with the *RICS Valuation Professional Standard* | existing tenants<br>Assumed vacancy levels<br>Estimated rental growth<br>Discount rate | |
| Unquoted Equity/Debt & Infrastructure | Level 3 | Comparable valuation of similar companies in accordance with *International Private Equity and Venture Capital Valuation Guidelines* (2018) | EBITDA multiple<br>Revenue multiple<br>Discount for lack of marketability<br>Control premium | Valuations could be affected by material events occurring between the date of the financial statements provided and the Pension Fund's own reporting date, by changes to expected cashflows and by any differences between (un)audited accounts |

| | Quoted Market Price | Using Observable Inputs | With Significant Unobservable Inputs | |
|---|---|---|---|---|
| **Values at 31 March 2020** | **Level 1** | **Level 2** | **Level 3** | **Total** |
| | **£'000** | **£'000** | **£'000** | **£'000** |
| | | | | |
| Financial Assets at Fair Value through Profit and Loss | 3,418,333 | | 501,228 | **3,919,561** |
| Non-Financial Assets at Fair Value through Profit and Loss | | 348,750 | | **348,750** |
| Financial Liabilities at Fair Value through Profit and Loss | 0 | | | **0** |
| | | | | |
| **Net Investment Assets (Fair Value)** | **3,418,333** | **348,750** | **501,228** | **4,268,311** |

| | Quoted Market Price | Using Observable Inputs | With Significant Unobservable Inputs | |
|---|---|---|---|---|
| **Values at 31 March 2019** | **Level 1** | **Level 2** | **Level 3** | **Total** |
| | **£'000** | **£'000** | **£'000** | **£'000** |
| | | | | |
| Financial Assets at Fair Value through Profit and Loss | 3,644,161 | | 323,345 | **3,967,506** |
| Non-Financial Assets at Fair Value through Profit and Loss | | 328,025 | | **328,025** |
| Financial Liabilities at Fair Value through Profit and Loss | 0 | | | **0** |
| | | | | |
| **Net Investment Assets (Fair Value)** | **3,644,161** | **328,025** | **323,345** | **4,295,531** |

**Note 16b: Transfers between Levels 1 and 2**

There were no transfers between levels 1 and 2.

**Note 16c: Reconciliation of Fair Value Measurements within Level 3**

| | Market Value 1 April 2019 | Purchases during the year & Derivative Payments | Sales during the year & Derivative Receipts | Realised Gains & Losses | Unrealised Gains & Losses (a) | Market Value 31 March 2020 |
|---|---|---|---|---|---|---|
| | **£'000** | **£'000** | **£'000** | **£'000** | **£'000** | **£'000** |
| | | | | | | |
| Pooled Infrastructure | 24,014 | 50,205 | (3,096) | 518 | 4,692 | 76,333 |
| Private Equity | 280,903 | 51,997 | (42,637) | 25,332 | 24,189 | 339,784 |
| Private Debt | 18,428 | 73,883 | (6,007) | 976 | (2,169) | 85,111 |
| | | | | | | |
| **Total** | **323,345** | | | | | **501,228** |

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

**Note 16d: Sensitivity of Assets Valued at Level 3**

Having analysed historical data, current market trends and consulted with independent investment advisors, the Fund has determined that the valuation methods described above are likely to be accurate to within the following ranges and has set out below the consequent potential impact on the closing value of investments held at 31 March 2020**.**

| | Assessed Valuation Range (+/-) | Value at 31 March 2020 | Value on Increase | Value on Decrease |
|---|---|---|---|---|
| | | **£'000** | **£'000** | **£'000** |
| | | | | |
| Pooled Infrastructure | 13% | 76,333 | 86,256 | 66,410 |
| Private Equity | 30% | 339,784 | 441,719 | 237,849 |
| Private Debt | 30% | 85,111 | 110,644 | 59,578 |
| | | | | |
| **Total** | | **501,228** | **638,619** | **363,837** |

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

The Fund’s primary long term risk is that the Fund’s assets will fall short of its liabilities (i.e. promised benefits payable to members). Therefore, the aim of investment risk management is to minimise the risk of an overall reduction in the value of the Fund and to maximise the opportunity for gains across the whole Fund portfolio.

The Fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) and credit risk to an acceptable level. In addition, the Fund manages its liquidity risk, ensuring there is liquidity to meet the Fund’s forecast cash flows.

The Fund manages these investment risks as part of its overall Pension Fund Risk Management Strategy.

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

### Market Risk

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

The objective of the Fund’s Risk Management Strategy is to identify, manage and control market risk exposure within acceptable parameters, whilst optimising the return on risk.

In general, excessive volatility in market risk is managed through the diversification of the portfolio in terms of geographical location, industry sectors and individual securities.

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

**Other Price Risk – Sensitivity Analysis**

Following analysis of historical data and expected investment return movement during the financial year and in consultation with the Fund's Investment Advisor, the Fund has determined that the following movements in market price risk are reasonably possible for the 2019/20 reporting period.

| Asset Type | Potential Market Movements (+/-) |
|---|---|
| | |
| UK Bonds | 7.5% |
| Overseas Bonds | 7.5% |
| UK Equities | 16.5% |
| Overseas Equities | 20.5% |
| Pooled – Diversified Growth Fund | 12.5% |
| Pooled Infrastructure | 13.0% |
| Private Equity | 30.0% |
| Private Debt | 30.0% |
| Property | 13.0% |
| Cash | 1.0% |

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

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

| Asset Type | Value as at 31 March 2020 | % Change | Value on Increase | Value on Decrease |
|---|---|---|---|---|
| | £'000 | | £'000 | £'000 |
| | | | | |
| UK Bonds | 206,888 | 7.5 | 222,405 | 191,371 |
| Overseas Bonds | 583,234 | 7.5 | 626,977 | 539,491 |
| UK Equities | 991,938 | 16.5 | 1,155,608 | 828,268 |
| Overseas Equities | 1,227,358 | 20.5 | 1,478,966 | 975,750 |
| Pooled – Diversified Growth Funds | 310,821 | 12.5 | 349,674 | 271,968 |
| Pooled – Infrastructure | 174,427 | 13.0 | 197,103 | 151,751 |
| Private Equity | 339,784 | 30.0 | 441,719 | 237,849 |
| Private Debt | 85,111 | 30.0 | 110,644 | 59,578 |
| | | | | |
| **Total** | **3,919,561** | | **4,583,096** | **3,256,026** |

| Asset Type | Value as at 31 March 2019 | % Change | Value on Increase | Value on Decrease |
|---|---|---|---|---|
| | **£'000** | | **£'000** | **£'000** |
| | | | | |
| UK Bonds | 202,644 | 7.5 | 217,842 | 187,446 |
| Overseas Bonds | 225,333 | 7.5 | 242,233 | 208,433 |
| UK Equities | 1,326,246 | 16.0 | 1,538,445 | 1,114,047 |
| Overseas Equities | 1,470,324 | 20.5 | 1,771,740 | 1,168,908 |
| Pooled – Diversified Growth Funds | 313,028 | 12.5 | 352,157 | 273,899 |
| Pooled – Infrastructure | 130,600 | 13.0 | 147,578 | 113,622 |
| Private Equity | 280,903 | 30.0 | 365,174 | 196,632 |
| Private Debt | 18,428 | 30.0 | 23,956 | 12,900 |
| | | | | |
| **Total** | **3,967,506** | | **4,659,125** | **3,275,887** |

**Interest Rate Risk**

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

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

The Fund's direct exposure to interest rate movements as at 31 March 2019 and 31 March 2020 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value:

| Asset Type | As at 31 March 2019 | As at 31 March 2020 |
|---|---|---|
| | **£'000** | **£'000** |
| | | |
| Cash and Cash Equivalents | 178,671 | 127,746 |
| Cash Balances | 19 | 27 |
| Fixed Interest Securities | 427,977 | 790,122 |
| | | |
| **Total** | **606,667** | **917,895** |

**Interest Rate Risk Sensitivity Analysis**

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

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

| **Exposure to Interest Rate Risk** | **Asset Values as at 31 March 2020** | **Impact** | |
|---|---|---|---|
| | | **+ 1%** | **- 1%** |
| | **£'000** | **£'000** | **£'000** |
| | | | |
| Cash and Cash Equivalents | 127,746 | 129,023 | 126,469 |
| Cash Balances | 27 | 27 | 27 |
| Fixed Interest Securities | 790,122 | 798,023 | 782,221 |
| | | | |
| **Total** | **917,895** | **927,073** | **908,717** |

| **Exposure to Interest Rate Risk** | **Asset Values as at 31 March 2019** | **Impact** | |
|---|---|---|---|
| | | **+ 1%** | **- 1%** |
| | **£'000** | **£'000** | **£'000** |
| | | | |
| Cash and Cash Equivalents | 178,671 | 180,458 | 176,884 |
| Cash Balances | 19 | 19 | 19 |
| Fixed Interest Securities | 427,977 | 432,257 | 423,697 |
| | | | |
| **Total** | **606,667** | **612,734** | **600,600** |

**Currency Risk**

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Fund (£UK). The Fund holds both monetary and non-monetary assets denominated in currencies other than £UK.

The Fund's currency rate risk is routinely monitored in accordance with the Fund's Risk Management Strategy, including monitoring the range of exposure to currency fluctuations.

The following table summarises the Fund's currency exposure as at 31 March 2020 and as at the previous year end:

| Assets Exposed to Currency Risk | Asset Value as at 31 March 2019 | Asset Value as at 31 March 2020 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Overseas Quoted Securities | 921,354 | 811,137 |
| Overseas Unquoted Securities | 263,207 | 377,484 |
| Overseas Unit Trusts | 652,004 | 791,417 |
| Overseas Global Pooled Bonds | 122,298 | 208,038 |
| | | |
| **Total Overseas Assets** | **1,958,863** | **2,188,076** |

**Currency Risk – Sensitivity Analysis**

Following analysis of historical data in consultation with the Fund's investment advisors, the Fund considers the likely volatility associated with foreign exchange rate movements to be 10.0%.

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

A 10.0% strengthening/weakening of the pound against the various currencies in which the Fund holds investments would increase/decrease the net assets to pay benefits as shown below:

| Assets Exposed to Currency Risk | Asset Value as at 31 March 2020 | Potential Market Movement | |
|---|---|---|---|
| | | +10.0% | -10.0% |
| | £'000 | £'000 | £'000 |
| | | | |
| Overseas Quoted Securities | 811,137 | 892,251 | 730,023 |
| Overseas Unquoted Securities | 377,484 | 415,232 | 339,736 |
| Overseas Unit Trust | 791,417 | 870,559 | 712,275 |
| Overseas Global Pooled Bonds | 208,038 | 228,842 | 187,234 |
| | | | |
| **Total** | **2,188,076** | **2,406,884** | **1,969,268** |

| Assets Exposed to Currency Risk | Asset Value as at 31 March 2019 | Potential Market Movement | |
|---|---|---|---|
| | | +10.2% | -10.2% |
| | £'000 | £'000 | £'000 |
| | | | |
| Overseas Quoted Securities | 921,354 | 1,015,332 | 827,376 |
| Overseas Unquoted Securities | 263,207 | 290,054 | 236,360 |
| Overseas Unit Trust | 652,004 | 718,508 | 585,500 |
| Overseas Global Pooled Bonds | 122,298 | 134,772 | 109,824 |
| | | | |
| **Total** | **1,958,863** | **2,158,666** | **1,759,060** |

**Credit Risk**

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

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

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

The Fund believes it has managed its exposure to credit risk and has had no experience of default or uncollectable deposits. The Fund's cash holding at 31 March 2020 was £127,773,000 (31 March 2019 £178,690,000). This was held with the following institutions as shown below:

| Summary | Rating | Balance as at 31 March 2019 | Balance as at 31 March 2020 |
|---|---|---|---|
| | | **£'000** | **£'000** |
| | | | |
| **Liquidity Funds** | | | |
| HSBC Liquidity Funds | A+ | 31,856 | 34,412 |
| | | | |
| **Bank Deposit Accounts** | | | |
| ACC Loans Fund Deposit | N/A | 106,700 | 67,480 |
| HSBC | A+ | 40,115 | 25,854 |
| | | | |
| **Subtotal** | | **178,671** | **127,746** |
| | | | |
| **Bank Current Accounts** | | | |
| | | | |
| Clydesdale Bank | A- | **19** | **27** |
| | | | |
| **Total** | | **178,690** | **127,773** |

**Liquidity Risk**

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

The Fund defines liquid assets as assets that can be converted to cash within three months. Illiquid assets are those assets which will take longer than three months to convert into cash. As at 31 March 2020 the value of illiquid assets was £849,977,186 which represented 19.3% of the total net assets of the Fund (31 March 2019 £651,370,002 which represented 14.5% of the total net assets).

**Note 18a: Long Term Assets**

| | 31 March 2019 | 31 March 2020 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| Merger – Transport Funds | 0 | 81 |
| | | |
| **Total Long Term Assets** | **0** | **81** |

**Note 18b: Current Assets**

| | 31 March 2019 | 31 March 2020 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| Employees' Contributions due | 3,259 | 2,498 |
| Employers' Contributions due | 9,674 | 7,513 |
| Sundry Debtors | 3,074 | 5,068 |
| **Subtotal** | **16,007** | **15,079** |
| Bank | 19 | 27 |
| | | |
| **Total Current Assets** | **16,026** | **15,106** |

**Note 18c: Current Liabilities**

| | 31 March 2019 | 31 March 2020 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| Sundry Creditors | 18,002 | 19,744 |
| Benefits Payable | 8,632 | 10,790 |
| | | |
| **Total Current Liabilities** | **26,634** | **30,534** |

**Note 19: Related Party Transactions**

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

The costs of these services for the North East Scotland Pension Fund amounted to £1,534,042 (2018/19 £1,354,549).

Prior to the remittance of excess cash to the investment fund managers, surplus cash is invested as a temporary loan with the Council. At the year end this amounted to £67,480,000 (2018/19 £106,700,000) for the North East Scotland Pension Fund.

Interest was received from the Council of £870,248 (2018/19 £345,451) for the North East Scotland Pension Fund.

**Note 20: Key Management Personnel**

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

| | | Accrued Pension 2018/19 | Accrued Pension 2019/20 |
|---|---|---|---|
| | | £'000 | £'000 |
| | | | |
| Steven Whyte | Director of Resources | 39 | 42 |
| Jonathan Belford | Chief Officer - Finance | 1 | 36 |

**Governance**

As at 31 March 2020, 9 members of the Pensions Committee and 7 members of the Pension Board were active members or pensioners of the North East Scotland Pension Fund.

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

In 2019/20, Elected Members' had interests in Sport Aberdeen and Aberdeen International Youth Festival.

**Note 21: Contractual Commitments as at 31 March 2020**

As at 31 March 2020 the NESPF had contractual commitment in respect of Private Equity/Debt and Global Real Estate portfolios:

| | Contractual Commitments | Undrawn Commitments |
|---|---|---|
| | £'000 | £'000 |
| | | |
| HarbourVest | 205,653 | 43,631 |
| Standard Life | 47,629 | 15,640 |
| Partners Group | 89,376 | 22,253 |
| Maven (SLF) | 6,308 | 44 |
| Capital Dynamics | 60,000 | 24,760 |
| RCP Advisors | 36,292 | 11,673 |
| Unigestion | 57,519 | 16,175 |
| AAM Residential Property | 30,000 | 21,232 |
| Hermes Infrastructure | 100,000 | 27,670 |
| Alcentra EDL | 88,492 | 55,492 |
| Hayfin DLF | 88,492 | 57,585 |
| | | |
| **Total** | **809,761** | **296,155** |

**Note 22: Additional Voluntary Contributions (AVC)**

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

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

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

| **2018/19** | | **Income (AVCs Paid by Members)** | | **2019/20** |
|---|---|---|---|---|
| **£'000** | | | | **£'000** |
| | | | | |
| 29 | | Standard Life | | 33 |
| 2,730 | | Prudential | | 2,428 |

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

| **Market Value** | | **Additional Voluntary Contributions** | | **Market Value** |
|---|---|---|---|---|
| **31 March 2019** | | | | **31 March 2020** |
| **£'000** | | | | **£'000** |
| | | | | |
| 1,473 | | Standard Life | | 1,135 |
| 24,313 | | Prudential | | 23,480 |

**Note 23: Contingent Assets/Liabilities**

Following a bond review in 2018 the North East Scotland Pension Fund hold two insurance bonds and one cash bond. These bonds guard against the possibility of being unable to recover pension liabilities from these Admission Bodies should they terminate their participation in the Scheme. These bonds are drawn up in favour of the Pension Fund and payment will only be triggered in the event of an employer default. The next bond review will be carried out by the Scheme Actuary following the completion of the 2020 valuation process.

The pension liabilities for all Transferee Admission Bodies are guaranteed by the originating employer as per Regulation 61(5)(a) of the Local Government Pension Scheme (Scotland) Regulations 2018. In total the Fund has secured guarantees for 24 Community Admission Bodies and Transferee Admission Bodies currently participating in the Scheme.

UK and European law require pension schemes to provide equal benefits to men and women in respect of service after 17 May 1990. This includes providing equal benefits accrued from that date to reflect the differences in Guaranteed Minimum Pensions (GMPs). To allow the government to continue to meet these requirements an interim solution was introduced which means that public sector pension schemes are required to provide full Consumer Price Index (CPI) pension increases on GMP benefits for members who reach State Pension Age between 6 April 2016 and 5 April 2021. The UK

Government may extend this for members reaching State Pension Age from 6 April 2021 onwards or will adopt a long-term methodology known as conversion. Currently, the additional cost of extending GMP cannot be quantified.

**Note 24: Impairment for Bad and Doubtful Debts**

The risk of employers being unable to meet their pensions obligations is managed through the NESPF Termination Policy and the NESPF Employer Covenant Assessment Policy which are imbedded within the Funding Strategy Statement. For 2019/20 one employer terminated from the Fund. The assets and liabilities held for this employer were subsumed by the scheme guarantor with a calculated termination fee of zero due upon exit from the Fund. As at 31 March 2020 there are no participating employers in the process of terminating from the Fund.

**Note 25: Investment Principles**

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

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

**Note 26: Critical Judgements in applying Accounting Policies**

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

The items in the Net Assets Statement as at 31 March 2020 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

| Item | Uncertainties | Effect if Actual Results Differ from Assumption |
|---|---|---|
| Actuarial present value of promised retirement benefits. | Estimation of the net liability to pay pensions depends on several complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on Pension Fund assets. | The methodology used by the Scheme Actuary is in line with accepted guidelines. Further to the Fund's liability being calculated every three years, an update of the funding position is calculated by the Scheme Actuary every 3 months. Further information can be found in Note 1. |
| Private Equity Private Debt & Pooled Infrastructure (Unquoted) | Private equity/debt and unquoted pooled infrastructure investments are valued at fair value in accordance with International Private Equity and Venture Capital Valuation guidelines. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation. | Private equity £340 million. Private Debt £85 million. Pooled Infrastructure (Unquoted) £76 million. There is a risk that these investments may be under or overstated in the accounts. |

**Note 27: Events after the Balance Sheet Date**

The draft Statement of Accounts was authorised for issue by the Chief Officer - Finance on 30 June 2020. Events taking place after this date are not reflected in the Annual Accounts or Notes. Where events taking place before this date provided information about conditions existing at 31 March 2020, the figures in the Annual Accounts and Notes have been adjusted in all material respects to reflect the impact of this information. No such adjustments have been required.

Along with the rest of the world, the Pension Fund has felt the force of the COVID-19 pandemic, not only in asset value and returns but also in the way we go about our daily business. While asset values and returns have retracted as a result of market volatility, the Fund remains above benchmark, however, there remains uncertainty and potential volatility yet to be experienced.

The Pension Fund has shown its resilience by adapting to alternative working environments to ensure service delivery and most importantly to continue the payment of pensions.

**Note 28: Agency Arrangement for Administering Compensatory ‘Added’ Years**

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

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

| | 2018/19 | 2019/20 |
|---|---|---|
| | **£’000** | **£’000** |
| | | |
| **Cost incurred/recovered on behalf of:** | | |
| | | |
| Aberdeen City Council | 2,360 | 2,386 |
| Aberdeenshire Council | 1,364 | 1,380 |
| Moray Council | 714 | 720 |
| Scottish Water | 1,276 | 1,286 |
| Other | 307 | 310 |
| | | |
| **Total** | **6,021** | **6,082** |
| | | |
| **Associated Payroll Cost** | **4** | **4** |

# NOTES TO THE ABERDEEN CITY COUNCIL TRANSPORT FUND ACCOUNTS

## Note 1: Actuarial Valuation Report

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

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

### Funding Level

| | |
|---|---|
| The Level of Funding in terms of the Percentage of Assets available to meet Liabilities | 94% |

In the year 2019/20 the assets and liabilities held with the LGPS (Scotland) for First Glasgow were transferred from the Strathclyde No. 3 Fund to the Aberdeen City Council Transport Fund for administrative purposes under a Scottish Government direction.

Following the completion of the transfer, the scheme actuary completed an evaluation of the total liabilities held for both First Aberdeen and First Glasgow based on the 2017 assumptions for the ACCTF

| | |
|---|---|
| Market Value of Assets at Valuation | £325,000,000 |
| Liabilities | £308,000,000 |
| Surplus | £ 17,000,000 |

### Funding Level

| | |
|---|---|
| The Level of Funding in terms of the Percentage of Assets available to meet Liabilities | 106% |

The figures above are an approximation based on a roll forward of the data held for First Aberdeen as at 31 March 2017 and based on an extract of data held for First Glasgow as at 31 March 2019.

A full valuation of the liabilities will take place in line with regulation as at 31 March 2020.

For the interim period, the contribution requirements for each employer will remain in line with the 2017 valuation carried out by the respective scheme actuaries at the time.

**Contribution Requirement**

| | 2018/19 | 2019/20 | 2020/21 |
|---|---|---|---|
| **First Aberdeen** | 33% plus | 33% plus | 33% plus |
| (as a percentage of payroll) | £1,500,000 | £1,500,000 | £1,500,000 |
| **First Glasgow** | 0% | 0% | 0% |
| | Due to the surplus determined as at 31 March 2017 | | |

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

**Assumptions Used to Calculate Funding Target**

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

**Actuarial Statement**

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

The actuarial value of promised retirement benefits at the accounting date, calculated in line with International Accounting Standards 26 (IAS 26) assumptions, is estimated to be £217.3m (2019 £80.9m). Included within the calculation for 2020 is an amount of £1.7million by way of an estimate of the effect of the McCloud judgement. These figures are used for the statutory accounting purposes by Aberdeen City Council Transport Fund and complies with the requirements of IAS 26.

These calculations are only prepared for the purposes of IAS 26 and have no validity in other circumstances. It is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

The full statement by the Scheme Actuary, including notes on the McCloud judgement, can be found in Appendix 1.

## Note 2: Contributions Receivable

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | **£'000** | **£'000** |
| | | |
| **Employees' Normal Contributions** | **72** | **129** |
| | | |
| Employers' Normal Contributions | 385 | 408 |
| Employers' Deficit Recovery Contributions | 1,558 | 1,500 |
| **Total Employers' Contributions** | **1,943** | **1,908** |
| | | |
| **Total** | **2,015** | **2,037** |

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | **£'000** | **£'000** |
| | | |
| Scheduled Bodies | 2,015 | 2,037 |
| | | |
| **Total** | **2,015** | **2,037** |

## Note 3: Benefits Payable

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | **£'000** | **£'000** |
| | | |
| Pensions | 3,243 | 7,061 |
| Commutation and Lump Sum Retirement Benefits | 337 | 1,734 |
| Lump Sum Death Benefits | 328 | 324 |
| | | |
| **Total** | **3,908** | **9,119** |

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | **£'000** | **£'000** |
| | | |
| Scheduled Bodies | 3,908 | 9,119 |
| | | |
| **Total** | **3,908** | **9,119** |

## Note 4: Payment to and on Account of Leavers

There were no payments to and on Account of Leavers.

**Note 5: Management Expenses**

| | 2018/19 | 2019/20 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Pension Fund Staffing Costs – Administration | 33 | 40 |
| Information Technology | 11 | 12 |
| Supplies and Services | 3 | 4 |
| Accommodation | 2 | 3 |
| Printing and Publications | 1 | 1 |
| **Administration Expenses Total** | **50** | **60** |
| | | |
| Pension Fund Staffing Costs – Investment | 5 | 8 |
| Pension Fund Committee | 0 | 1 |
| External Audit Fee | 1 | 1 |
| Actuarial Fees | 20 | 34 |
| General Expenses | 5 | 5 |
| **Oversight and Governance Expenses Total** | **31** | **49** |
| | | |
| Investment Management | 212 | 163 |
| Custody Fees | 19 | 18 |
| **Investment Management Expenses Total** | **231** | **181** |
| | | |
| **Management Expenses Grand Total** | **312** | **290** |

## Note 6: Investment Income

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | **£'000** | **£'000** |
| | | |
| Fixed Interest Securities | 7 | 113 |
| | | |
| Pooled Investments | 108 | 44 |
| | | |
| Interest on Cash Deposits | 14 | 40 |
| | | |
| Other (including P/L from Currency & Derivatives) | (25) | 27 |
| | | |
| **Total** | **104** | **224** |
| | | |
| **Tax -** | | |
| Withholding Tax – Fixed Interest Securities | 0 | 0 |
| Withholding Tax – Pooled | 0 | 0 |
| | | |
| **Total Tax** | **0** | **0** |
| | | |
| **Net Total** | **104** | **224** |

**Note 7a: Investment Assets**

Reconciliation of Movements in Investments and Derivatives:

| | Market Value 31 March 2019 | Purchases | Sales | Change in Market Value | Market Value 31 March 2020 |
|---|---|---|---|---|---|
| | **£’000** | **£’000** | **£’000** | **£’000** | **£’000** |
| | | | | | |
| Fixed Interest | 27,793 | 145,755 | (8,310) | (304) | 164,934 |
| Pooled Investments | 76,192 | 223,147 | (158,301) | (5,756) | 135,282 |
| | | | | | |
| | **103,985** | **368,902** | **(166,611)** | **(6,060)** | **300,216** |
| | | | | | |
| **Other** | | | | | |
| Cash | 4,321 | | | | 8,733 |
| Investment Income Due | 3 | | | | 148 |
| Investment Sales Amount Receivable | 918 | | | | 0 |
| Investment Purchases Amount Payable | (3,999) | | | | (675) |
| | | | | | |
| **Net Investment Assets** | **105,228** | | | | **308,422** |

| | Market Value 31 March 2018 | Purchases | Sales | Change in Market Value | Market Value 31 March 2019 |
|---|---|---|---|---|---|
| | **£’000** | **£’000** | **£’000** | **£’000** | **£’000** |
| | | | | | |
| Fixed Interest | 1,117 | 25,095 | 0 | 1,581 | 27,793 |
| Pooled Investments | 97,060 | 26,402 | (52,714) | 5,444 | 76,192 |
| | | | | | |
| | **98,177** | **51,497** | **(52,714)** | **7,025** | **103,985** |
| | | | | | |
| **Other** | | | | | |
| Cash | 1,621 | | | | 4,321 |
| Investment Income Due | 0 | | | | 3 |
| Investment Sales Amount Receivable | 0 | | | | 918 |
| Investment Purchases Amount Payable | 0 | | | | (3,999) |
| | | | | | |
| **Net Investment Assets** | **99,798** | | | | **105,228** |

### Note 7b: Transfer of Strathclyde Transport Fund Assets

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| Cash | 0 | 180,500 |
| | | |
| Pooled Investment – Unit Trust | 0 | 35,888 |
| | | |
| **Total** | **0** | **216,388** |

### Note 8: Analysis of Investments

| | 2018/19 | 2019/20 |
|---|---:|---:|
| | £'000 | £'000 |
| | | |
| **Fixed Interest Securities** | | |
| | | |
| **UK** | | |
| Public Sector Quoted | **27,793** | **164,934** |
| | | |
| | | |
| **Pooled Funds – Additional Analysis** | | |
| | | |
| **UK** | | |
| Fixed Income | 28,569 | 66,554 |
| Unit Trusts | 25,750 | 49,292 |
| | | |
| **Overseas** | | |
| Unit Trusts | 21,873 | 19,436 |
| **Subtotal Pooled Funds** | **76,192** | **135,282** |
| | | |
| Cash Deposits | 4,321 | 8,733 |
| Investment Income Due | 3 | 148 |
| Investment Sales Amount Receivable | 918 | 0 |
| | | |
| **Investment Assets Total** | **109,227** | **309,097** |
| | | |
| **Investment Liabilities** | | |
| | | |
| Investment Purchases Amount Payable | (3,999) | (675) |
| | | |
| **Investment Liabilities Total** | **(3,999)** | **(675)** |
| | | |
| **Net Investment Assets** | **105,228** | **308,422** |

## Note 9: Investments Analysed by Fund Manager

| Investment Assets | 31 March 2019 | | 31 March 2020 | |
|---|---|---|---|---|
| | £'000 | % | £'000 | % |
| | | | | |
| Schroders | 105,000 | 99.8 | 103,888 | 33.7 |
| Transition | 0 | 0.0 | 204,105 | 66.2 |
| ACC Loans Fund Deposit | 228 | 0.2 | 429 | 0.1 |
| | | | | |
| **Net Investment Assets** | **105,228** | **100.0** | **308,422** | **100.0** |

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

| Security | Market Value 31 March 2019 | % of Net Investment Assets | Market Value 31 March 2020 | % of Net Investment Assets |
|---|---|---|---|---|
| | £'000 | | £'000 | |
| | | | | |
| LGIM Active Corporate Bond | 0 | 0.0 | 33,830 | 11.0 |
| Schroder Pension Mgt Life DGF Series 8 | 0 | 0.0 | 21,703 | 7.0 |
| Vanguard Investment Series US Investment Grade Cred Index ACC NAV | 15,194 | 14.4 | 15,924 | 5.2 |
| Blackrock Asset Management UK Aquila Life Currency Work Ex UK Equity | 6,286 | 6.0 | 5,031 | 1.6 |
| SIF Diversified Completion CLS P Accumulation | 10,556 | 10.0 | 11,665 | 3.8 |
| SSGA Lux MG GL Treasury Bond Index GBP | 11,984 | 11.4 | 12,884 | 4.2 |
| Vanguard Investment series Global Stock Index FD-INST USD SHS | 5,660 | 5.4 | 4,925 | 1.6 |
| Schroder Pension Management Life Risk | 8,393 | 8.0 | 8,419 | 2.7 |
| Schroder Matching Plus Synthetic Index Linked Gilt FDI ACC | 7,116 | 6.8 | 6,320 | 2.0 |
| UK Gilt 0.125% IL 10/8/2048 | 10,149 | 9.6 | 10,414 | 3.4 |
| UK Treasury 0.125% IL 22/3/2044 | 8,802 | 8.4 | 1,478 | 0.5 |
| UK Treasury 0.125% IL 22/3/2058 | 6,175 | 5.9 | 6,232 | 2.0 |

## Note 10: Stock Lending

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

Collateral is held at a minimum of 108% in respect of each borrower, consisting of Government Debt, UK and Overseas Equities.

There was no stock lending in operation as at 31 March 2020.

## Note 11: Financial and Non-Financial Instruments

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

| 31 March 2019 | | | | 31 March 2020 | | |
|---|---|---|---|---|---|---|
| **Designated as Fair Value through Profit & Loss** | **Assets at Amortised Cost** | **Financial Liabilities at Amortised Cost** | | **Designated as Fair Value through Profit & Loss** | **Assets at Amortised Cost** | **Financial Liabilities at Amortised Cost** |
| **£’000** | **£’000** | **£’000** | | **£’000** | **£’000** | **£’000** |
| | | | **Financial Assets** | | | |
| | | | | | | |
| 27,793 | | | Fixed Interest | 164,934 | | |
| 76,192 | | | Pooled | 135,282 | | |
| | 4,321 | | Cash | | 8,733 | |
| | 921 | | Other Investment Balances | | 148 | |
| | 488 | | Debtors | | 1,178 | |
| | | | | | | |
| **103,985** | **5,730** | **0** | **Subtotal** | **300,216** | **10,059** | **0** |
| | | | | | | |
| | | | **Financial Liabilities** | | | |
| | | | | | | |
| | | (3,999) | Other Investment Balances | | | (675) |
| | | (416) | Creditors | | | (772) |
| | | | | | | |
| **103,985** | **5,730** | **(4,415)** | | **300,216** | **10,059** | **(1,447)** |
| | | | | | | |
| | | **105,300** | **Financial Instruments Total** | | | **308,828** |
| | | | | | | |
| **0** | | | **Non - Financial Instruments** | **0** | | |
| | | | | | | |
| **103,985** | **5,730** | **(4,415)** | | **300,216** | **10,059** | **(1,447)** |
| | | **105,300** | **Net Assets of the Fund** | | | **308,828** |

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

| 31 March 2019 | | 31 March 2020 |
|---|---|---|
| **£’000** | | **£’000** |
| | | |
| | **Financial Assets** | |
| 7,025 | Fair Value through Profit and Loss | (6,060) |
| | | |
| | **Financial Liabilities** | |
| 0 | Fair Value through Profit and Loss | 0 |
| | | |
| **7,025** | **Net Gains and Losses on Financial Instruments** | **(6,060)** |
| | | |
| | **Non-Financial Instruments** | |
| 0 | Fair Value through Profit and Loss | 0 |
| | | |
| **7,025** | **Net Gains and Losses of the Fund** | **(6,060)** |

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

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

### Level 1

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

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

### Level 2

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

### Level 3

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

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

The values of the investments in unquoted private equity/debt and infrastructure are based on valuations provided by the general partners to the funds in which Aberdeen City Council Transport Fund has invested.

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

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

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

**Note 13a: Fair Value – Basis of Valuation**

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

| Description of Asset | Valuation Hierarchy | Basis of Valuation | Observable and Unobservable Inputs | Key Sensitivities affecting the Valuations Provided |
|---|---|---|---|---|
| Market Quoted Investments | Level 1 | Published bid market price ruling on the final day of the accounting period | Not required | Not required |
| Quoted Bonds | Level 1 | Fixed interest securities are valued at a market value based on current yields | Not required | Not required |
| Exchange Traded Pooled Investments | Level 1 | Closing bid value on published exchanges | Not required | Not required |
| Pooled Investments – Overseas Unit Trusts and Property Funds | Level 2 | Closing bid price where bid and offer prices are published.<br><br>Closing single price where single price published | NAV-based pricing set on a forward pricing basis | Not required |

| Values at 31 March 2020 | Quoted Market Price<br>Level 1 | Using Observable Inputs<br>Level 2 | With Significant Unobservable Inputs<br>Level 3 | Total |
|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 |
| | | | | |
| Financial Assets at Fair Value through Profit and Loss | 300,216 | 0 | 0 | **300,216** |
| Non-Financial Assets at Fair Value through Profit and Loss | 0 | 0 | 0 | **0** |
| Financial Liabilities at Fair Value through Profit and Loss | 0 | 0 | 0 | **0** |
| | | | | |
| **Net Investment Assets (Fair Value)** | **300,216** | **0** | **0** | **300,216** |

| Values at 31 March 2019 | Quoted Market Price<br>Level 1 | Using Observable Inputs<br>Level 2 | With Significant Unobservable Inputs<br>Level 3 | Total |
|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 |
| | | | | |
| Financial Assets at Fair Value through Profit and Loss | 103,985 | 0 | 0 | **103,985** |
| Non-Financial Assets at Fair Value through Profit and Loss | 0 | 0 | 0 | **0** |
| Financial Liabilities at Fair Value through Profit and Loss | 0 | 0 | 0 | **0** |
| | | | | |
| **Net Investment Assets (Fair Value)** | **103,985** | **0** | **0** | **103,985** |

**Note 13b: Transfers between Levels 1 and 2**

There were no transfers between Level 1 and 2.

### Note 13c: Reconciliation of Fair Value Measurements within Level 3

There are no Fair Value Measurements at Level 3 within the ACC Transport Fund. Therefore, no reconciliation is required.

### Note 13d: Sensitivity of Assets Valued at Level 3

There are no assets valued at Level 3 within the ACC Transport Fund. Therefore, no sensitivity analysis is required.

### Note 14: Risk arising from Financial and Non-Financial Instruments

The Fund's primary long term risk is that the Fund's assets will fall short of its liabilities (i.e. promised benefits payable to members). Therefore, the aim of investment risk management is to minimise the risk of an overall reduction in the value of the Fund and to maximise the opportunity for gains across the whole Fund portfolio.

The Fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) and credit risk to an acceptable level. In addition, the Fund manages its liquidity risk, ensuring there is liquidity to meet the Fund's forecast cash flows.

The Fund manages these investment risks as part of its overall Pension Fund Risk Management Strategy.

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

### Market Risk

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

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

In general, excessive volatility in market risk is managed through the diversification of the portfolio in terms of geographical location, industry sectors and individual securities.

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

**Other Price Risk – Sensitivity Analysis**

Following analysis of historical data and expected investment return movement during the financial year and in consultation with the Fund's Investment Advisor, the Fund has determined that the following movements in market price risk are reasonably possible for the 2019/20 reporting period.

| **Asset Type** | **Potential Market Movements (+/-)** |
|---|---|
| | |
| Cash | 1.0% |
| UK Bonds | 7.5% |
| Overseas Bonds | 7.5% |
| UK Equities | 16.5% |
| Overseas Equities | 20.5% |
| Pooled – Diversified Growth Funds | 12.5% |

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

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

| **Asset Type** | **Value as at 31 March 2020** | **% Change** | **Value on Increase** | **Value on Decrease** |
|---|---|---|---|---|
| | **£'000** | | **£'000** | **£'000** |
| | | | | |
| UK Bonds | 231,488 | 7.5 | 235,124 | 227,852 |
| UK Equities | 15,924 | 16.5 | 18,778 | 13,070 |
| Overseas Equities | 19,436 | 20.5 | 24,378 | 14,494 |
| Pooled – Diversified Growth Funds | 33,368 | 12.5 | 34,918 | 31,818 |
| | | | | |
| **Total** | **300,216** | | **313,198** | **287,234** |

| Asset Type | Value as at 31 March 2019 | % Change | Value on Increase | Value on Decrease |
|---|---|---|---|---|
| | **£'000** | | **£'000** | **£'000** |
| | | | | |
| UK Bonds | 56,362 | 7.5 | 60,589 | 52,135 |
| UK Equities | 15,194 | 16.0 | 17,625 | 12,763 |
| Overseas Equities | 21,873 | 20.5 | 26,357 | 17,389 |
| Pooled – Diversified Growth Funds | 10,556 | 12.5 | 11,876 | 9,236 |
| | | | | |
| **Total** | **103,985** | | **116,447** | **91,523** |

**Interest Rate Risk**

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

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

The Fund's direct exposure to interest rate movements as at 31 March 2019 and 31 March 2020 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value:

| Asset type | As at 31 March 2019 | As at 31 March 2020 |
|---|---|---|
| | **£'000** | **£'000** |
| | | |
| Cash and Cash Equivalents | 4,321 | 8,733 |
| Cash Balances | 1 | 733 |
| Fixed Interest Securities | 56,362 | 231,488 |
| | | |
| **Total** | **60,684** | **240,954** |

**Interest Rate Risk Sensitivity Analysis**

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

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

| **Exposure to Interest Rate Risk** | **Asset Values as at 31 March 2020** | **Impact** | |
|---|---|---|---|
| | | **+1%** | **-1%** |
| | **£'000** | **£'000** | **£'000** |
| | | | |
| Cash and Cash Equivalents | 8,733 | 8,820 | 8,646 |
| Cash Balances | 733 | 740 | 726 |
| Fixed Interest Securities | 231,488 | 233,803 | 229,173 |
| | | | |
| **Total** | **240,954** | **243,363** | **238,545** |

| **Exposure to Interest Rate Risk** | **Asset Values as at 31 March 2019** | **Impact** | |
|---|---|---|---|
| | | **+1%** | **-1%** |
| | **£'000** | **£'000** | **£'000** |
| | | | |
| Cash and Cash Equivalents | 4,321 | 4,364 | 4,278 |
| Cash Balances | 1 | 1 | 1 |
| Fixed Interest Securities | 56,362 | 56,926 | 55,798 |
| | | | |
| **Total** | **60,684** | **61,291** | **60,077** |

**Currency Risk**

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Fund (£UK). The Fund holds both monetary and non-monetary assets denominated in currencies other than £UK.

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

The following table summarises the Fund's currency exposure as at 31 March 2020 and as at the previous year end:

| Currency Exposure – Asset Type | Asset Value as at 31 March 2019 | Asset Value as at 31 March 2020 |
|---|---:|---:|
| | **£'000** | **£'000** |
| | | |
| Overseas Unit Trusts | 21,873 | 19,436 |
| | | |
| **Total Overseas Assets** | **21,873** | **19,436** |

**Currency Risk – Sensitivity Analysis**

Following analysis of historical data in consultation with the Fund's investment advisors, the Fund considers the likely volatility associated with foreign exchange rate movements to be 10.0%.

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

A 10.0% strengthening/weakening of the pound against the various currencies in which the Fund holds investments would increase/decrease the net assets to pay benefits as follows:

| Assets Exposed to Currency Risk | Asset Value as at 31 March 2020 | Potential Market Movement | |
|---|---:|---:|---:|
| | | **+10.0%** | **-10.0%** |
| | **£'000** | **£'000** | **£'000** |
| | | | |
| Overseas Unit Trust | 19,436 | 21,380 | 17,492 |
| | | | |
| **Total** | **19,436** | **21,380** | **17,492** |

| Assets Exposed to Currency Risk | Asset Value as at 31 March 2019 | Potential Market Movement | |
|---|---:|---:|---:|
| | | **+10.2%** | **-10.2%** |
| | **£'000** | **£'000** | **£'000** |
| | | | |
| Overseas Unit Trust | 21,873 | 24,104 | 19,642 |
| | | | |
| **Total** | **21,873** | **24,104** | **19,642** |

**Credit Risk**

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

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

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

The Fund believes it has managed its exposure to credit risk and has had no experience of default or uncollectable deposits. The Fund's cash holding at 31 March 2020 was £9,466,000 and at 31 March 2019 £4,322,000. This was held with the following institutions:

| **Summary** | **Rating** | **Balance as at 31 March 2019** | **Balance as at 31 March 2020** |
|---|---|---|---|
| | | **£'000** | **£'000** |
| | | | |
| **Bank Deposit Accounts** | | | |
| ACC Loans Fund Deposit | N/A | 228 | 429 |
| HSBC | A+ | 4,093 | 8,304 |
| | | | |
| **Subtotal** | | **4,321** | **8,733** |
| | | | |
| **Bank Current Accounts** | | | |
| | | | |
| HSBC | A+ | 0 | 731 |
| Clydesdale Bank | A- | 1 | 2 |
| | | | |
| **Total** | | **4,322** | **9,466** |

**Liquidity Risk**

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

The Fund defines liquid assets as assets that can be converted to cash within three months. Illiquid assets are those assets which will take longer than three months to convert into cash. There were no illiquid assets as at 31 March 2020 and 31 March 2019.

**Note 15a: Long Term Assets**

| | 31 March 2019 | 31 March 2020 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Lifetime Tax Allowance | 296 | 269 |
| | | |
| **Total Long Term Assets** | **296** | **269** |

**Note 15b: Current Assets**

| | 31 March 2019 | 31 March 2020 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Employees' Contributions due | 1 | 3 |
| Employers' Contributions due | 5 | 132 |
| Sundry Debtors | 185 | 41 |
| **Subtotal** | **191** | **176** |
| | | |
| Bank | 1 | 733 |
| | | |
| **Total Current Assets** | **192** | **909** |

**Note 15c: Current Liabilities**

| | 31 March 2019 | 31 March 2020 |
|---|---|---|
| | £'000 | £'000 |
| | | |
| Sundry Creditors | 132 | 285 |
| Benefits Payable | 284 | 487 |
| | | |
| **Total Current Liabilities** | **416** | **772** |

**Note 16: Related Party Transactions**

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

The cost of these services for the Aberdeen City Council Transport Fund was £53,751 (2018/19 - £41,893).

Prior to the remittance of excess cash to the investment fund managers, surplus cash is invested as a temporary loan with the Council. At the year end this amounted to £429,000 (2018/19 - £228,000) for the Aberdeen City Council Transport Fund.

Interest was received from the Council of £2,590 (2018/19 - £1,584) for the Aberdeen City Council Transport Fund.

## Note 17: Contingent Assets/Liabilities

UK and European law require pension schemes to provide equal benefits to men and women in respect of service after 17 May 1990. This includes providing equal benefits accrued from that date to reflect the differences in Guaranteed Minimum Pensions (GMPs). To allow the government to continue to meet these requirements an interim solution was introduced which means that public sector pension schemes are required to provide full Consumer Price Index (CPI) pension increases on GMP benefits for members who reach State Pension Age between 6 April 2016 and 5 April 2021. The UK Government may extend this for members reaching State Pension Age from 6 April 2021 onwards or will adopt a long-term methodology known as conversion. Currently, the additional cost of extending GMP cannot be quantified.

## Note 18: Key Management Personnel

Certain employees of Aberdeen City Council hold key positions in the financial management of the Aberdeen City Council Transport Fund. However, they are not members of the Aberdeen City Council Transport Fund.

## Note 19: Investment Principles

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

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

## Note 20: Critical Judgements in applying Accounting Policies

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

The items in the Net Assets Statement at 31 March 2020 for which there is a significant risk of material adjustments in the forthcoming financial year are shown below:

| Item | Uncertainties | Effect if Actual Results Differ from Assumptions |
| --- | --- | --- |
| Actuarial present value of promised retirement benefits | Estimation of the net liability to pay pensions depends on several complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on Pension Fund assets. | The methodology used by the Scheme Actuary is in line with accepted guidelines. Further to the Fund's liability being calculated every three years, an update of the funding position is calculated by the Scheme Actuary every 3 months. Further information can be found in Note 1. |

**Note 21: Events after the Balance Sheet Date**

The Unaudited Statement of Accounts was authorised for issue by the Chief Officer - Finance on 30 June 2020. Events taking place after this date are not reflected in the Annual Accounts or Notes. Where events taking place before this date provided information about conditions existing at 31 March 2020, the figures in the Annual Accounts and Notes have been adjusted in all material respects to reflect the impact of this information. No such adjustments have been required.

Along with the rest of the world, the Pension Fund has felt the force of the COVID-19 pandemic, not only in asset value and returns but also in the way we go about our daily business. While asset values and returns have retracted as a result of market volatility, the Fund remains above benchmark, however, there remains uncertainty and potential volatility yet to be experienced.

The Pension Fund has shown its resilience by adapting to alternative working environments to ensure service delivery and most importantly to continue the payment of pensions.

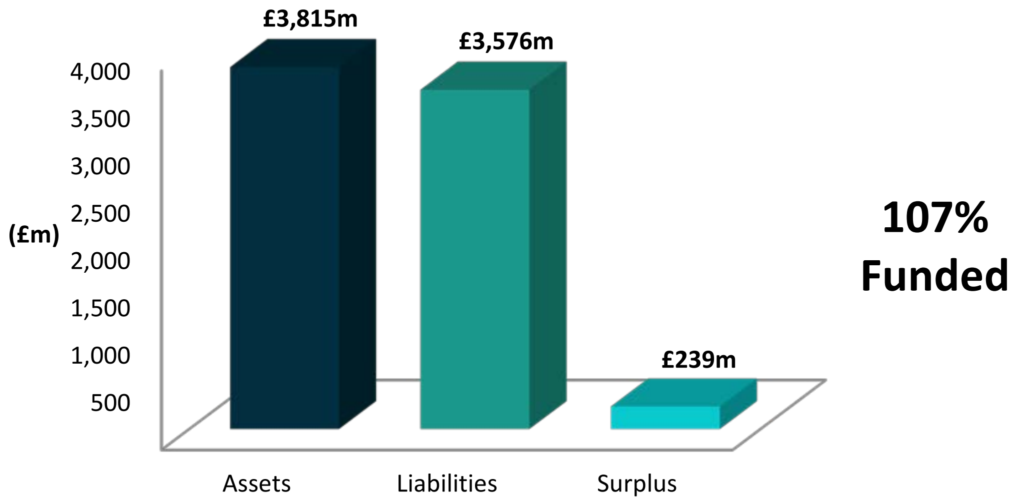
# Appendix 1 – Statement by the Consulting Actuary

**ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2020 - STATEMENT BY THE CONSULTING ACTUARY**

This statement has been provided to meet the requirements under Regulation 55 (1)(d) of The Local Government Pension Scheme (Scotland) Regulations 2018.

**North East Scotland Pension Fund**

An actuarial valuation of the North East Scotland Pension Fund was carried out as at 31 March 2017 to determine the contribution rates with effect from 1 April 2018 to 31 March 2021.




On the basis of the assumptions adopted, the Fund's assets of £3,815 million represented 107% of the Fund's past service liabilities of £3,576 million (the "Solvency Funding Target") at the valuation date. The surplus at the valuation was therefore £239 million.

The valuation also showed that a Primary contribution rate of 22.0% of pensionable pay per annum was required from employers. The Primary rate is calculated as being sufficient, together with contributions paid by members, to meet all liabilities arising in respect of service after the valuation date.

The funding objective as set out in the Funding Strategy Statement (FSS) is to achieve and then maintain a solvency funding level of 100% of liabilities (the solvency funding target). In line with the FSS, where a surplus exists at the effective date of the valuation a plan will be put in place which allows contribution offsets to refund any surplus.

The FSS sets out the process for determining the spread period in respect of each employer (or the recovery period for those employers with a deficit in the Fund). At the last actuarial valuation, the average spread/recovery period adopted was approximately 24 years, and the total initial surplus reclaimed on a whole fund level (the "Secondary rate" for 2019/20) was approximately £12.8 million per annum.

Further details regarding the results of the valuation are contained in the formal report on the actuarial valuation dated 28 March 2018.

In practice, each individual employer's position is assessed separately and the contributions required are set out in the report. In addition to the certified contribution rates, payments to cover additional liabilities arising from early retirements will be made to the Fund by the employers.

The funding plan adopted in assessing the contributions for each individual employer is in accordance with the FSS. Any different approaches adopted, e.g. with regard to the implementation of contribution increases and surplus offset periods, are as determined through the FSS consultation process.

The valuation was carried out using the projected unit actuarial method and the main actuarial assumptions used for assessing the Solvency Funding Target and the Primary rate of contribution were as follows:

| | For both past and future service liabilities (Funding Target and Primary rate of contribution) |
|---|---|
| Rate of return on investments (discount rate) | 4.15% per annum |
| Rate of pay increases (long term)* | 3.9% per annum |
| Rate of increases in pensions in payment (in excess of GMP)/deferment | 2.4% per annum |
| Rate of CPI Inflation/CARE benefit revaluation | 2.4% per annum |

* allowance was also made for short-term public sector pay restraint over a 3-year period.

The assets were assessed at market value.

The next triennial actuarial valuation of the Fund is due as at 31 March 2020. Based on the results of this valuation, the contribution rates payable by the individual employers will be revised with effect from 1 April 2021.

**The McCloud Judgment**

The "McCloud judgment" refers to a legal challenge in relation to historic benefit changes for all public sector schemes being age discriminatory. The Government announced in 2019 that this needs to be remedied for all schemes including the LGPS. This is likely to result in increased costs for some employers. This remedy is not yet agreed but guidance issued requires that each Fund sets out its policy on addressing the implications.

As they were calculated in 2017, the above funding level and Primary contribution rate do not include an allowance for the estimated cost of the McCloud judgment. However, at the overall Fund level we estimate that the cost of the judgment could be an increase in past service liabilities of broadly £24 million and an increase in the Primary Contribution rate of 1.0% of Pensionable Pay per annum.

**Impact of COVID-19**

The valuation results and employer contributions above were assessed as at 31 March 2017. In 2020 we have so far seen significant volatility and uncertainty in markets around the world in relation to the COVID-19 pandemic. This potentially has far-reaching consequences in terms of funding and risk, and these will be considered as part of the 2020 valuation process, including considering what changes (if any) should be made to contributions.

**Actuarial Present Value of Promised Retirement Benefits for the Purposes of IAS 26**

IAS 26 requires the present value of the Fund's promised retirement benefits to be disclosed, and for this purpose the actuarial assumptions and methodology used should be based on IAS 19 rather than the assumptions and methodology used for funding purposes.

To assess the value of the benefits on this basis, we have used the following financial assumptions as at 31 March 2020 (the 31 March 2019 assumptions are included for comparison):

| | 31 March 2019 | 31 March 2020 |
|---|---|---|
| Rate of return on investments (discount rate) | 2.6% per annum | 2.4% per annum |
| Rate of pay increases* | 3.7% per annum | 3.6% per annum |
| Rate of increases in pensions in payment (in excess of GMP)/deferment | 2.3% per annum | 2.2% per annum |
| Rate of CPI Inflation/CARE benefit revaluation | 2.2% per annum | 2.1% per annum |

* includes a corresponding allowance to that made in the latest formal actuarial valuation for short-term public sector pay restraint

The demographic assumptions are the same as those used in the 2017 valuation, except the post retirement mortality assumptions, which have been updated to reflect analysis carried out in 2019 (set out below). Full details of the valuation assumptions are set out in the formal report on the actuarial valuation dated 28 March 2018.

Corporate bond yields were similar at the start and end of year resulting in the same discount rate of 2.4% p.a. being used for IAS 26 purposes at the year-end as for last year. The expected long-term rate of CPI inflation decreased during the year, from 2.2% p.a. to 2.1%, which served to decrease the liabilities slightly over the year.

The value of the Fund's promised retirement benefits for the purposes of IAS 26 as at 31 March 2019 was estimated as £5,422 million, including an estimate of the potential impact of the McCloud judgment.

Interest over the year increased the liabilities by c£131 million. Allowing for net benefits accrued/paid over the period then increased the liabilities by c£87 million (this includes the impact of early retirements/augmentations, a revised estimate of the potential impact of the McCloud judgment and the impact of GMP Indexation (see comments elsewhere in this statement)). There was a decrease in liabilities of £388 million made up of "actuarial gains" (£101 million relating to changes in financial assumptions, and £287 million relating to changes in the post retirement mortality assumptions).

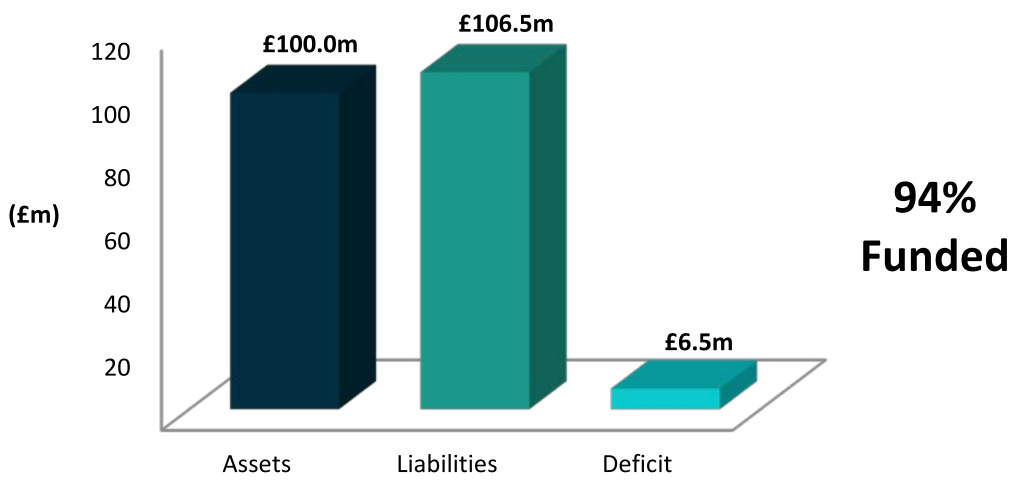
The net effect of all the above is that the estimated total value of the Fund's promised retirement benefits as at 31 March 2020 is therefore £5,252 million.

**GMP Indexation**

At present, the public service schemes are required to provide full CPI pension increases on GMP benefits for members who reach State Pension Age between 6 April 2016 and 5 April 2021. The UK Government may well extend this at some point in the future to include members reaching State Pension Age from 6 April 2021 onwards, which would give rise to a further cost to the LGPS and its employers. If the Fund were required to index-link GMP benefits in respect of those members who reach their State Pension Age after April 2021, then this would increase the Fund liabilities by about £16 million on IAS26 assumptions, and we have included this amount within the final IAS26 liability figure above.

**Aberdeen City Council Transport Fund**

An actuarial valuation of the Aberdeen City Council Transport Fund was carried out as at 31 March 2017 to determine the contribution rates with effect from 1 April 2018 to 31 March 2021.



On the basis of the assumptions adopted, the Fund's assets of £100 million represented 94% of the Fund's past service liabilities of £106.5 million (the "Solvency Funding Target") at the valuation date. The deficit at the valuation was therefore £6.5 million. The valuation also showed that a Primary contribution rate of 58.5% of pensionable pay per annum was required from the employer. The Primary rate is calculated as being sufficient, together with contributions paid by members, to meet all liabilities arising in respect of service after the valuation date.

The funding objective as set out in the Funding Strategy Statement (FSS) is to achieve a solvency funding level of 100% of liabilities (the solvency funding target) over a reasonable time period and then maintain sufficient assets in order for it to pay all benefits arising as they fall due. In line with the FSS, where a shortfall exists at the effective date of the valuation a deficit recovery plan will be put in place which requires additional contributions to correct the shortfall.

The FSS sets out the process for determining the recovery plan. At the last actuarial valuation, the Administering Authority and First Aberdeen Limited agreed that First Aberdeen Limited will maintain the same level of current contributions as those agreed at the 2014 valuation, which is 33% of pensionable pay plus £1.5m p.a. At present, therefore, part of the £1.5m annual payment is being used to finance the costs in relation to future service. This means that the amount to recover the shortfall is approximately £1.2m p.a. On this basis the deficit would be expected to be removed in about 5 years from 31 March 2018.

Further details regarding the results of the valuation are contained in the formal report on the actuarial valuation dated 28 March 2018.

The valuation was carried out using the attained age actuarial method and the main actuarial assumptions used for assessing the Solvency Funding Target and the Primary rate of contribution were as follows:

| | **For both past and future service liabilities (Funding Target and Primary rate of contribution)** |
|---|---|
| Rate of return on investments (discount rate) | 1.6% per annum |
| Rate of pay increases (short term) | 2.9% per annum to 31 March 2018 |
| Rate of pay increases (long term) | 3.4% per annum |
| Rate of increases in pensions in payment (in excess of GMP)/deferment | 2.9% per annum |
| Rate of CPI Inflation/CARE benefit revaluation | 2.9% per annum |

The assets were assessed at market value.

The next triennial actuarial valuation of the Fund is due as at 31 March 2020. Based on the results of this valuation, the contribution rate payable will be revised with effect from 1 April 2021.

**The McCloud Judgment**

The "McCloud judgment" refers to a legal challenge in relation to historic benefit changes for all public sector schemes being age discriminatory. The Government announced in 2019 that this needs to be remedied for all schemes including the LGPS. This is likely to result in increased costs for some employers. This remedy is not yet agreed but guidance issued requires that each Fund sets out its policy on addressing the implications.

As they were calculated in 2017, the above funding level and Primary contribution rate do not include an allowance for the estimated cost of the McCloud judgment. However, at the overall Fund level we estimate that the cost of the judgment could be an increase in past service liabilities of less than £100,000 and a negligible increase in the Primary Contribution rate.

**Impact of COVID-19**

The valuation results and employer contributions above were assessed as at 31 March 2017. In 2020 we have so far seen significant volatility and uncertainty in markets around the world in relation to the COVID-19 pandemic. This potentially has far-reaching consequences in terms of funding and risk, and these will be considered as part of the 2020 valuation process, including considering what changes (if any) should be made to contributions.

## Actuarial Present Value of Promised Retirement Benefits for the Purposes of IAS 26

IAS 26 requires the present value of the Fund's promised retirement benefits to be disclosed, and for this purpose the actuarial assumptions and methodology used should be based on IAS 19 rather than the assumptions and methodology used for funding purposes.

To assess the value of the benefits on this basis, we have used the following financial assumptions as at 31 March 2020 (the 31 March 2019 assumptions are included for comparison):

| | 31 March 2019 | 31 March 2020 |
|---|---|---|
| Rate of return on investments (discount rate) | 2.4% per annum | 2.4% per annum |
| Rate of pay increases | 2.7% per annum | 2.6% per annum |
| Rate of increases in pensions in payment (in excess of GMP)/deferment | 2.3% per annum | 2.2% per annum |
| Rate of CPI Inflation/CARE benefit revaluation | 2.2% per annum | 2.1% per annum |

The demographic assumptions are the same as those used in the 2017 valuation for the Aberdeen City Council Transport Fund, except the post retirement mortality assumptions, which have been updated to reflect analysis carried out in 2019 (set out below). Full details of the valuation assumptions are set out in the formal report on the actuarial valuation dated 28 March 2018 (and the equivalent report for the Strathclyde No. 3 Fund).

Corporate bond yields were similar at the start and end of year resulting in the same discount rate of 2.4% p.a. being used for IAS 26 purposes at the year-end as for last year. The expected long-term rate of CPI inflation decreased during the year, from 2.2% p.a. to 2.1%, which served to decrease the liabilities slightly over the year.

The value of the Fund's promised retirement benefits for the purposes of IAS 26 as at 31 March 2019 was estimated as £80.9 million.

Interest over the year increased the liabilities by c£1.9 million. Allowing for net benefits accrued/paid over the period then decreased the liabilities by c£2.1 million (this includes the impact of early retirements/augmentations, a revised estimate of the potential impact of the McCloud judgment and the impact of GMP Indexation (see comments elsewhere in this statement)). There was a decrease in liabilities of £7.4 million made up of "actuarial gains" (£1.4 million relating to changes in financial assumptions, and £6.0 million relating to changes in the post retirement mortality assumptions).

Over the year, the Strathclyde Pension No. 3 Fund merged with the Aberdeen City Council Transport Fund. The impact at 31 March 2020 of this merger is an increase in liabilities of £144.0 million.

The net effect of all the above is that the estimated total value of the Fund's promised retirement benefits as at 31 March 2020 is therefore £217.3 million.

**GMP Indexation**

At present, the public service schemes are required to provide full CPI pension increases on GMP benefits for members who reach State Pension Age between 6 April 2016 and 5 April 2021. The UK Government may well extend this at some point in the future to include members reaching State Pension Age from 6 April 2021 onwards, which would give rise to a further cost to the LGPS and its employers. If the Fund were required to index-link GMP benefits in respect of those members who reach their State Pension Age after April 2021, then this would increase the Fund liabilities (including the liabilities that were formerly part of the Strathclyde No. 3 Fund) by about £1.7 million on IAS26 assumptions, and we have included this amount within the final IAS26 liability figure above.

**Post retirement mortality assumptions applied at 31 March 2020**

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:

**North East Scotland Pension Fund**

| Current Status | Retirement Type | Weighting |
|---|---|---|
| Annuitant | Normal Health | 114% males<br>101% females |
| | Dependant | 150% males<br>104% females |
| | Ill Health | 136% males<br>144% females |
| | Future Dependant | 146% males<br>121% females |
| Active | Normal Health | 121% males<br>101% females |
| | Ill Health | 134% males<br>151% females |
| Deferred | All | 144% males<br>116% females |
| Active/deferred | Future Dependant | 153% males<br>128% females |

**Aberdeen City Council Transport Fund**

| Current Status | Retirement Type | Weighting – former ACCTF members | Weighting – former Strathclyde members |
|---|---|---|---|
| Annuitant | Normal Health | 108% males<br>88% females | 117% males<br>94% females |
| | Dependant | 100% males<br>104% females | 145% males<br>111% females |
| | Ill Health | 132% males<br>149% females | 137% males<br>150% females |
| | Future Dependant | 128% males<br>112% females | 139% males<br>119% females |
| Active | Normal Health | 112% males<br>115% females | 112% males<br>86% females |
| | Ill Health | 128% males<br>169% females | 128% males<br>131% females |
| Deferred | All | 143% males<br>102% females | 136% males<br>110% females |
| Active/deferred | Future Dependant | 137% males<br>121% females | 140% males<br>120% females |

Paul Middleman
Fellow of the Institute and Faculty of Actuaries
Mercer Limited
**May 2020**

# Appendix 2 – Schedule of Employers

**North East Scotland Pension Fund**

| | Employers as at 31 March 2019 | New Admissions | Ceased | Employers as at 31 March 2020 |
|---|---|---|---|---|
| **Scheduled Bodies** | 11 | 0 | 0 | 11 |
| **Transferee Bodies** | 14 | 1 | 0 | 15 |
| **Admission Bodies** | 25 | 0 | 1 | 24 |
| **Total** | **50** | **1** | **1** | **50** |

**Participating Employers as at 31 March 2020:**

| | | |
|---|---|---|
| 1. | Aberdeen City Council (Administering Authority) | Scheduled |
| 2. | Aberdeenshire Council | Scheduled |
| 3. | The Moray Council | Scheduled |
| 4. | Scottish Water | Scheduled |
| 5. | Grampian Valuation Joint Board | Scheduled |
| 6. | Scottish Fire and Rescue Service | Scheduled |
| 7. | Scottish Police Authority | Scheduled |
| 8. | North East Scotland College | Scheduled |
| 9. | Moray College | Scheduled |
| 10. | Visit Scotland | Scheduled |
| 11. | NESTRANS | Scheduled |
| 12. | Robertson Facilities Management (Shire) | Transferee |
| 13. | Bon Accord Care Ltd | Transferee |
| 14. | Bon Accord Support Services Ltd | Transferee |
| 15. | Aberdeen Heat & Power Ltd | Transferee |
| 16. | Station House Media Unit | Transferee |
| 17. | Aberdeen Sports Village | Transferee |
| 18. | Sport Aberdeen | Transferee |
| 19. | Robertson Facilities Management (City) | Transferee |
| 20. | Forth & Oban Ltd | Transferee |
| 21. | Alcohol and Drugs Action | Transferee |
| 22. | Idverde UK | Transferee |
| 23. | Citymoves Dance Agency | Transferee |
| 24. | Xerox (UK) Ltd | Transferee |
| 25. | Forth and Oban Ltd (Shire) | Transferee |
| 26. | Inspire Catering Scotland LLP | Transferee |
| 27. | Aberdeen Endowments Trust | Admitted |
| 28. | North East Sensory Services | Admitted |
| 29. | Aberlour Child Care Trust | Admitted |
| 30. | Fraserburgh Harbour Commissioners | Admitted |
| 31. | Peterhead Port Authority | Admitted |
| 32. | Robert Gordon University | Admitted |
| 33. | Robert Gordon’s College | Admitted |

| | | |
|---|---|---|
| 34. | Aberdeen Cyrenians | Admitted |
| 35. | Mental Health Aberdeen | Admitted |
| 36. | Fersands & Fountain Community Project | Admitted |
| 37. | SCARF | Admitted |
| 38. | Inspire (Partnership Through Life) Ltd | Admitted |
| 39. | Archway | Admitted |
| 40. | St Machar Parent Support Project | Admitted |
| 41. | Printfield Community Project | Admitted |
| 42. | HomeStart Aberdeen | Admitted |
| 43. | Aberdeen Foyer | Admitted |
| 44. | HomeStart NEA | Admitted |
| 45. | Pathways | Admitted |
| 46. | Outdoor Access Trust for Scotland | Admitted |
| 47. | Osprey Housing | Admitted |
| 48. | Aberdeen Performing Arts | Admitted |
| 49. | Sanctuary Scotland Housing Association Ltd | Admitted |
| 50. | Scottish Lighthouse Museum | Admitted |

**Aberdeen City Council Transport Fund**

| | | |
|---|---|---|
| 1. | First Aberdeen | Scheduled |
| 2. | First Glasgow | Scheduled |