worcestershire countycouncil

AGENDA ITEM 7

PENSIONS COMMITTEE
17 MARCH 2020

ACTUARIAL VALUATION AND FINAL PENSION FUND STRATEGY STATEMENT (FSS)

Recommendation

1. **The Chief Financial Officer recommends that:**

   a) **The Final Funding Strategy Statement (Appendix 1) be noted and the Committee be asked to comment on the changes to the FSS that were agreed at the Committee meeting in December 2019;**

   b) **The Initial draft of the 2019 Valuation rates and adjustment certificate (Appendix 2) be considered and noted; and**

   c) **The Chief Financial Officer be granted delegated authority to undertake any dealings with exit credits with the exception of those above £0.5m which may only be undertaken in consultation with the Chairman of the Pensions Committee.**

Background

2. As detailed in the December 2019 report, every three years, in line with legislation, the Fund Actuary, Mercer, carries out a full Actuarial Valuation of the Fund to calculate how much the employers in the Scheme need to contribute going forward to ensure that its liabilities, the pensions due to current and future pensioners, will be paid as they fall due.

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

4. The FSS was agreed at Committee on the 13 December 2019 and any further updates delegated to Fund officers on the proviso that the FSS was not expected to change fundamentally in between now and when the actuarial valuation is signed off by the actuary in March 2020. It was highlighted that there were a few areas where enabling wording had been included for anticipated changes to the LGPS Regulations following consultation with the key stakeholders. These may need to be removed, if the amendment Regulations are not laid ahead of the valuation sign off date and reinstated at a future FSS review. The changes to the FSS are reported back to Committee for completeness.

Updates made to the FSS agreed in December 2019

5. The areas that have been updated since the FSS provided in December 2019.

a) Removed the reference to some of the Regulations which the actuary does not expect to be implemented by 31 March 2020, e.g. all references to Deemed Employer Status, Deferred Debt, review of contributions etc. (throughout);
b) Funding level quoted to allow for the whole Fund result to be the aggregate of the individual employers, now the pot allocations have been agreed (page 2 and 16);
c) Added further wording regarding the investment pots and equity protection (predominantly page 2 and 23 and Appendix F 'Investment Pot Risk Management Policy page 42);
d) Updated the minimum risk funding level (page 16) allowing for negative real return vs CPI and more prudent mortality, as discussed with the actuary;
e) Added in a reference to allow flexibility to adjust CPI assumptions on the anticipated reform of RPI (page 24 and page 37);
f) Updated the recovery period / surplus spreading wording (pages 29) now that most of the employer results have been finalised; and
g) Updated the termination minimum risk basis life expectancy assumption (page 37) to a more prudent mortality assumption, as discussed with the actuary.

Investment Strategies / Pots

6. To recap, in order that the Fund delivers on its key objectives (ensuring that each employer takes the appropriate level of investment risk, giving each the best opportunity possible to achieve its long-term funding objective whilst increasing certainty of cost), the Fund has introduced three distinct investment strategies (High, Medium and Low risk).

7. With regards to the investment pots, the actuary has provided a Fund risk management framework of how the pots will be monitored (Appendix F of the FSS) which reference has also been included in the 2020 Investment Strategy Statement (ISS) on this agenda. This will be reviewed periodically as part of the governance of the risk management framework to be finalised with the actuary. The ISS has been updated to include reference to the investment pots. Investment 'pots'.

8. The narrative assumes that the Fund has implemented alternative investment strategies with differential levels of investment risk with effect from 1 April 2020. The pot an employer sits in will be reflected in the relevant employer asset share, funding basis and contribution requirements aim is to provide greater control over employer's exposure to investment risk **(Page 17 of FSS)**

Exit Credits

9. A partial Government response on Changes to the Local Valuation Cycle and the Management of Employer Risk covering Exit Credits was published on 27 February 2020 and come into force on 20 March 2020. The response to the remaining parts of the consultation e.g. moving to a 4-year valuation cycle are promised "in due course" and no timescale is given.

10. This change was intended to clarify the position on Exit Credits payable to employers exiting from a Fund where there are risk sharing arrangements between the employer and the original contracting authority and is backdated to apply from 14 May 2018 when Exit Credits were first introduced into the LGPS. Whilst the Regulations undoubtedly provide the regulatory support to Funds when they

determine their policies on payment of Exit Credits, whether they provide absolute clarity to Pension Funds is perhaps debatable in terms of how the process is governed.

11. The key points from the response and the Regulations are as follows:

a) The Pension Fund may determine, at their absolute discretion, the amount of any exit credit payment due, having regard to any "relevant considerations";
b) The relevant considerations specifically cover any risk sharing arrangements in force although the Pension Fund is not obliged to enquire into the precise risk sharing arrangements adopted;
c) It is up to the parties to set out why the arrangements made by them make payment of an exit credit appropriate which will include any risk sharing arrangements;
d) Pension Funds should adopt a fair and reasonable exit credits policy which should be set out in their Funding Strategy Statement;
e) Any Exit Credit already paid cannot be reclaimed or adjusted as the Pension Fund will have been deemed to have exercised their discretion; and
f) The period that any Exit Credit payable must be paid is extended from 3 to 6 months.

12. Worcestershire Pension Fund policy around exit credits has been provided for within the FSS on pages 14 and 15 covering instances where employers have and do not have guarantors participating in the Fund.

13. The level of exit credit will no doubt vary dependent on the employers funding levels and risk sharing agreements in place. It is therefore recommended that the Chief Financial Officer be granted delegated authority to undertake any dealings with exit credits with the exception of those above £0.5m which may only be undertaken in consultation with the Chairman of the Pensions Committee.

Initial draft of the 2019 Valuation rates and adjustment certificate

14. The actuary has provided an initial draft of the 2019 valuation rates and adjustment certificate (Appendix 2). Please note this is a working draft and is therefore subject to adjustment up to the point of sign off e.g. for any amendment to the employer contributions that may be agreed as well as confirmation of auditor requirements for certifying prepayment contributions. For this version the actuary has currently used the same approach that was used for the 2016 valuation to certify a 3-year deficit lump sum prepayment i.e. certifying this as a 3-separate lump sum amounts in respect of each contribution year. The actuary has also asked the Committee to note there may be some further formatting changes and adjustment to the notes as they finalise the draft report.

Contact Points

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Supporting Information

- Funding Strategy Statement (Appendix 1)
- Initial draft of the 2019 Valuation rates and adjustment certificate (Appendix 2)

Background Papers

In the opinion of the proper officer (in this case the Chief Financial Officer) the background papers relating to the subject matter of this report are

Funding Strategy Statement Committee report December 2019