

## REPORT OF THE GROUP DIRECTOR, FINANCE & CORPORATE RESOURCES

<b>DRAFT FUNDING STRATEGY STATEMENT</b>	Classification <b>Public</b>	Enclosures One
	Ward(s) affected  <b>ALL</b>	
<b>Pensions Committee</b> <b>24th January 2017</b>		

### 1. INTRODUCTION

- 1.1 This report introduces a draft Funding Strategy Statement for consultation with employers and other interested parties in the Pension Fund. Under the Local Government Pension Scheme Regulations 2013 the Administering Authority is required to publish a Funding Strategy Statement setting out its approach to funding the liabilities of the Pension Fund.

### 2. RECOMMENDATION

#### 2.1 The Pensions Committee is recommended to:

- **Agree the draft Funding Strategy Statement for consultation with employers and other interested parties**

### 3. RELATED DECISIONS

- Pensions Committee 19<sup>th</sup> September 2016 – Pension Fund Actuarial Valuation 2016 – Initial Report
- Pensions Sub-Committee 16<sup>th</sup> January 2014 – Funding Strategy Statement approved following 2013 valuation

### 4. COMMENTS OF THE GROUP DIRECTOR, FINANCE & CORPORATE RESOURCES

- 4.1 The Funding Strategy Statement forms part of the broader framework for funding and management of the London Borough of Hackney Pension Fund. It sets out how the Fund will approach the future funding of its liabilities and the recovery periods for recovering any deficit. Without sound financial management of the Pension Fund, the Council and other employers in the Pension Fund could see increased volatility in their contribution rates and increases in the cost of providing for the benefits of scheme members.

### 5. COMMENTS OF THE DIRECTOR, LEGAL

- 5.1 The Constitution delegates to the Pensions Committee the function of setting the overall strategic objectives for the Pension Fund.
- 5.2 Regulation 58 of the Local Government Pension Scheme Regulations 2013 requires the Council as an administering authority to publish and maintain a funding strategy statement.
- 5.3 When preparing, maintaining or publishing the funding strategy statement, the Council is required to make such revisions as it considers appropriate following

material change to the policy set out in the statement; any revisions must be made following consultation with such persons as the Authority considers appropriate.

5.5 When reviewing the funding strategy statement, the Council is required to have regard to: (a) the CIPFA Pensions Panel Guidance on Preparing and Maintaining a Funding Strategy Statement; and (b) the Council's statement of investment principles/Investment Strategy Statement

5.6 There are no immediate legal implications arising from this report.

## **6. BACKGROUND/TEXT OF THE REPORT**

6.1 The Pension Fund is required by statute to publish a Funding Strategy Statement (FSS), to keep the Statement under review and to revise it whenever there is a material change in the policy set out within it.

6.2 The FSS set out in the main Appendix has been drawn up by the Fund's actuary, Hymans Robertson, in conjunction with Officers of the Council. The Pension Fund has previously published a FSS following the 2013 valuation and this has been updated to reflect changes made for the 2016 valuation. It is proposed that this now be consulted upon with the Fund's employers, the investment advisor and other interested parties. Following a period of consultation, any proposed amendments will be brought to this Committee for ratification.

6.3 As set out in the FSS the objectives of the statement are to:

- ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due for payment;
- ensure that employer contribution rates are reasonably stable where appropriate;
- minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return (NB., this will also minimise the costs to be borne by Council Tax payers);
- reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and
- use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

6.4 In addition to the above the FSS also sets out the different treatments for different types of employers ranging from tax raising bodies such as the Council and other scheduled bodies such as Academies to Community and Transferee Admission Bodies. Various factors are considered during the contribution setting process, including the funding target (the assets required to pay member benefits), the time horizon and the probability of reaching the funding target over that time horizon. Each of these factors may be varied according to employer type, as this will influence the level of risk posed by each employer.

6.5 The draft FSS also covers the links to investment strategy which are set out in the Statement of Investment Principles. As Members will recognise the investment strategy is set for the longer term for the Fund and considerable time has been spent

at recent Committee meetings including dedicated strategy meetings to consider the longer term investment strategy for the Fund including looking at options for risk reduction over the longer term, should the funding level improve.

- 6.6 The FSS furthermore includes a number of detailed appendices covering key points around responsibilities, risks and regulations and the following points set these out in more detail.
- 6.7 Appendix A – Regulatory Framework for the FSS which sets out the purpose of the Statement as defined by The Department for Communities and Local Government (DCLG):
- “to establish a **clear and transparent fund-specific strategy** which will identify how employers’ pension liabilities are best met going forward;
  - to support the regulatory framework to maintain **as nearly constant employer contribution rates as possible**; and
  - to take a **prudent longer-term view** of funding those liabilities.”
- 6.8 Appendix B – Responsibilities of the key parties, i.e. the Administering Authority, individual employers, the Fund Actuary and other parties such as the investment advisers, investment managers, legal advisers, etc.
- 6.9 Appendix C – Key Risks and Controls:
- **Financial Risks** – includes assets failing to deliver returns in line with anticipated returns, inappropriate long term investment strategy, falls in risk-free returns on Government bonds giving rise to value placed on liabilities, underperformance relative to benchmark by the Fund’s investment managers, pay and price inflation significantly higher than anticipated, impact of increased employer contributions on service delivery and ceased employers giving rise to additional costs. **Controls** – includes prudent longer term return assumptions, taking specialist advice, inter-valuation monitoring, reviewing investment strategy options, measuring performance relative to bond targets, stabilisation modelling, quarterly investment and funding monitoring, making employers aware of possible consequences of decision, stabilisation for some employer, phased contribution increases, guarantees, cessation calculations and recovery of deficit amounts.
  - **Demographic Risks** - includes pensioners living longer, fund maturity i.e. declining active membership, deteriorating patterns of early retirements and reductions in payroll leading to insufficient deficit payments,. **Controls** – include setting mortality assumptions which allow for some increased longevity, specific fund mortality monitoring, ongoing monitoring of cashflows and maturity profiling of the Fund, monitoring ill health experience, charging employers for non ill-health retirements and seeking deficit contributions paid as lump sums rather than percentage of payroll.
  - **Regulatory Risks** – includes changes to national pension requirements and/or HMRC rules, time/cost/reputational risk associated with DCLG intervention triggered by Section 13 and changes by Government to particular employer participation in the LGPS. **Controls** – include ensuring that the Administering Authority considers consultations issued by Government and comments where appropriate and taking advice from the Fund Actuary re: Section 13.
  - **Governance Risk** – Administering Authority unaware of structural changes in employer membership, actuarial advice not sought, noted or proves to be insufficient, failure to carry out termination valuations on a cessation of an

employer or employers ceasing with insufficient reserves to meet liabilities at cessation. **Controls** – include monitoring employer membership and any changes to the employer that may impact on it, collecting deficit contributions as lump sums, Administering Authority maintaining a close working relationship with its advisers, seeking guarantees from another scheme employer and being alert to possible financial problems facing employers.

- 6.10 Appendix D – The calculation of Employer contributions covering the difference in the calculation at a whole Fund level compared to individual employer level, how the Primary and Secondary contribution rates are calculated and the treatment of different types of employers, how the Funding level is calculated and what affects the results for individual employers
- 6.11 Appendix E – Actuarial Assumptions, sets out the actuarial assumptions used and the standard funding basis (ongoing), as well as the assumptions behind this (investment returns/discount rate, expected salary growth, pensions increase, life expectancy and other wider assumptions.)
- 6.12 Appendix F – Glossary - sets out key terms used in both the FSS and the Actuarial Valuation.
- 6.14 The Committee are asked to approve the draft Funding Strategy Statement for consultation with interested parties and will receive an updated Statement following the consultation period. An Employer Forum is being arranged for employers to discuss the outcome of the valuation with the Fund Actuary and to highlight to employers the issues set out in the FSS.

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## **Appendix**

Appendix 1 – Funding Strategy Statement plus appendices