REPORT OF THE GROUP DIRECTOR, FINANCE AND CORPORATE RESOURCES

Pension Fund Actuarial Valuation 2019 - Introduction **Pension Board** **20th March 2019**	**Classification** **PUBLIC** **Ward(s) affected** **ALL**	**Enclosures** **4** **AGENDA ITEM NO.**

1. INTRODUCTION

1.1 This report provides an introduction to the 2019 valuation process and sets out an indicative timetable. It covers measures discussed with the Fund actuary to address potential timetabling issues resulting from late data provision and summarises the latest developments with regards to the use of the LGPS Scheme Advisory Board and Treasury Cost Cap mechanisms

2. RECOMMENDATIONS

2.1 The Pension Board is recommended to note the report.

3. RELATED DECISIONS

- Pensions Committee 29th March 2017 - Pension Fund Actuarial Valuation 2016 – Valuation Report

4. COMMENTS OF THE GROUP DIRECTOR, FINANCE AND CORPORATE RESOURCES

4.1 The triennial valuation outcome is sensitive to both the actuarial and financial assumptions made within the valuation, and the membership data used; significant variations to either the assumptions or the data used could impact the Fund's financial position. Given the relationship between the Pension Fund and the Council, the inputs to the triennial valuation can therefore directly impact on the level of resources available for other Council services.

4.2 It is therefore critical that both the Pensions Committee and Pension Board have a sound understanding of the valuation process and the assumptions used.

4.3 There are no direct financial implications arising from this report

5. COMMENTS OF THE DIRECTIOR OF LEGAL AND GOVERNANCE

5.1 Regulation 62 of the Local Government Pension Scheme (LGPS) Regulations 2013 prescribes that each administering authority must obtain:

- an actuarial valuation of the assets and liabilities of each of its pension funds as at 31st March 2016 and on 31st March in every third year afterwards;
- a report by an actuary in respect of the valuation; and
- a rates and adjustments certificate prepared by an actuary

5.2 The role of the Pension Board is prescribed by Section 106 of the LGPS Regulations 2013 and includes the following:

- Securing compliance with the Local Government Pension Scheme Regulations 2013 and any other legislation relating to the governance and administration of the Scheme and any connected scheme
- Securing compliance with any requirements imposed by the Pensions Regulator in relation to the Scheme and any connected scheme
- Ensuring the effective and efficient governance and administration of the Scheme and any connected scheme

5.3 Further details of the suggested functions of local pension boards are provided by statutory guidance ((Local Government Pension Scheme (LGPS) Guidance on the creation and operation of Local Pension Boards in England and Wales). The guidance considers the triennial valuation as being appropriate for the remit of local pension boards.

5.4 Taking into account the role of the Pension Board as set out in the Regulations and statutory guidance, the consideration of the 2019 valuation process would appear to properly fall within the Board's remit

6. 2019 VALUATION PROCESS

6.1 A draft Valuation timetable produced by the fund actuary is attached at Appendix 1. Officers of the Fund have already met with the actuary to discuss the proposed timetable and consider measures to address issues resulting from late data provision. It is likely that the Fund will need to use multiple cuts of data as the data held by Equiniti improves; this will impact the overall cost of the valuation but should help to increase the accuracy of data provided. A draft timetable and roadmap are provided at Appendices 1 and 2; however, these are indicative only.

6.2 The fund actuary is now carrying out additional modelling work to assist the fund in setting financial assumptions for the valuation. The work will focus on stochastic modelling considering the impact of different asset outperformance assumptions on the probability of the Fund reaching full funding across various timescales. This work will then be used to inform the discount rate used in the valuation.

6.3 The 2019 valuation was expected to be affected by the LGPS Scheme Advisory Board cost cap mechanism. Cost control mechanism are now in place across all the public service pension schemes and it was widely expected that reductions in member costs would lead to these being triggered prior to the 2019 valuation. That process has now been paused as the result of a Court of Appeal case – further information is provided in section 7.

6.4 The process and assumptions used for the valuation will be considered in detail by the Pensions Committee at its June 2019 meeting. A further update will be provided to the Board in November 2019.

7. COST CAP MECHANISMS

7.1 A mechanism for assessing the value of pensions (the “cost control mechanism” or “cost cap”) was introduced for all public service pension schemes as part of the Hutton reforms. The cap is intended to periodically assess the cost of the providing pensions to ensure that the reforms are affordable and sustainable. The process measures changes in member costs (those relating to assumptions about the profile of scheme members) only; if these have moved from a pre-determined target, changes to the scheme design or member contributions must be implemented to bring costs back within the target range. Changes to employer costs (those relating to assumptions that are financial or technical in nature).

7.2 Unlike the other public service schemes, the LGPS has two cost cap mechanisms in operation. One is the employer cost cap, operated by HM Treasury, with the other being the future service cost cap operated by the LGPS Scheme Advisory Board (SAB). Both processes are currently undertaken triennially in line with local valuations. Two different mechanisms are in place as the HM Treasury process is designed to make information about the cost of providing public service pensions comparable between schemes. The SAB process allows the SAB to take account of factors specific to the LGPS (e.g. the 50/50 scheme or differences in the lump sum commutation rate).

7.3 Both mechanisms will trigger changes to either the scheme design or member contributions if costs differ from the target cost by more than 2% in either direction. The HM Treasury process uses a target employer contribution cost of 14.6%, whilst the SAB process uses a target total cost of 19.5% with a 2:1 ratio of employer to member contributions. More information on the two process is provided in the SAB briefing note at Appendix 3.

7.4 The HM Treasury process has already taken place for the other public service schemes; indicative outcomes have been breaches of the cost cap floor requiring benefit improvements in excess of 3% of payroll For the LGPS, the SAB process takes place prior to finalisation of the Treasury calculations. The outcome of the Board’s process was a total scheme future service cost of 19%; as the target for the process is 19.5% the Board agreed to consider recommendations to return the total cost back to the target. If accepted by Government, the Board’s recommendations around changes to scheme design could then have been taken into account in the finalisation of the Treasury cost cap calculations, potentially avoiding automatic benefit changes.

7.5 At the end of January, Government announced a pause to the cost cap mechanism across the public services following a Court of Appeal judgement. In December 2018, the Court ruled that the ‘transitional protection’ (or underpin) offered to members within ten years of retirement as part of the Hutton reforms amounted to unlawful age discrimination. The Government is seeking permission to appeal this decision. However, if this is unsuccessful, the Court will require steps to be taken to compensate employees who were transferred to the new schemes. A copy of the statement from Government can be found at Appendix 4.

7.6 This decision is highly significant for the LGPS and other public service schemes) and produces considerable uncertainty about if, when and how benefits and member contributions will be affected in the LGPS. This in turn impacts the 2019 local fund valuations, which were to have allowed for scheme changes resulting from the cost cap process.

7.7 Officers have discussed the issue with the fund actuary and have agreed that in the absence of any clear messages from LGPS Scheme Advisory Board (SAB) and/or MHCLG, the 2019 valuations will proceed on the basis of the current benefit and member contribution structure, ignoring the cost cap process for the meantime. As and when there are developments the actuary will consider how best to incorporate into the 2019 valuation contribution-setting process. The actuary will also be liaising with other firms to ensure consistency across all LGPS Funds, as far as is practical, regardless of who their actuary is.

7.8 Officers will continue to monitor developments from the Local Government Association (LGA), SAB or the Ministry for Housing, Communities and Local Government (MHCLG).

Ian Williams
Group Director, Finance & Corporate Resources

Report Originating Officers: Rachel Cowburn ☎020-8356 2630
Financial considerations: Michael Honeysett ☎020-8356 3332
Legal comments: Sean Eratt ☎020-8356 6012

Appendices
Appendix 1 – Indicative Valuation Timetable
Appendix 2 – Valuation Roadmap
Appendix 3 – SAB Cost Control Briefing Note
Appendix 4 – Government statement on cost cap pause