WIRRAL COUNCIL

PENSION COMMITTEE

19 SEPTEMBER 2016

SUBJECT:	**GOVERNMENT ACTUARY'S DEPARTMENT – SECTION 13 DRY RUN REPORT**
WARD/S AFFECTED:	**ALL**
REPORT OF:	**STRATEGIC DIRECTOR OF TRANSFORMATION AND RESOURCES**
RESPONSIBLE PORTFOLIO HOLDER:	
KEY DECISION?	**NO**

1.0 EXECUTIVE SUMMARY

1.1 This report updates Members on the recent publication of the Government Actuary's Department (GAD) Section 13 'dry run' report, based on the 2013 round of fund valuations.

The purpose of the 'dry run' is to inform the approach and analysis for the first statutory report, concomitant with the 2016 round of ninety-one separate fund valuations.

1.2 The dry run report and appendices can be accessed from the Scheme Advisory Board website at:

http://lgpsboard.org/images/Reports/Section13DryRun20160711.pdf

http://lgpsboard.org/images/Reports/Section13DryRunAppendices20160711.pdf

2.0 BACKGROUND AND KEY ISSUES

2.1 The Independent Public Service Pension Commission's review of the sustainability of public service pension schemes led to numerous recommendations to change the structure and strengthen the governance framework of the LGPS – these resulted in the enactment of the Public Service Pension Act 2013.

In particular, there was a recommendation to publish centrally collated comprehensive data covering all LGPS funds, raising awareness of the need for consistency and transparency in the management of funding across the LGPS. This data is to include comparisons of key assumptions about investment growth and differences in deficit recovery plans amongst the funds.

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2.2 As such, Section 13 of the Act requires the Government Actuary to report on the funding reviews and employer contribution rates following each triennial valuation of the LGPS for the purpose of assessing whether the following four main cornerstones are achieved:

- **Compliance -** whether the fund's valuation is in accordance with the scheme's regulations

- **Consistency -** has the fund's valuation been carried out in a way which is not inconsistent with the other fund valuations within the LGPS

- **Solvency -** is the rate of employer contributions set at an appropriate level to ensure the solvency of the pension fund

- **Long term cost efficiency -** is the rate of employer contributions set at an appropriate level to ensure the long term cost-efficiency of the scheme, so far as relating to the pension fund.

2.3 The provisions within Section 13 provide for remedial action in circumstances where funds do not meet the above stated requirements.

COMPLIANCE

2.4 GAD reported no evidence of material non-compliance with the Scheme regulations, specifically the requirement to undertake a valuation exercise having due regard to the administering authorities' Funding Strategy Statements and Statements of Investment Principles within statutory timescales.

CONSISTENCY

2.5 A number of inconsistencies were identified between the valuations in terms of the approach taken, the assumptions used and disclosures which make meaningful comparison of local valuation results unachievable.

2.6 The analysis unveiled a wide range of financial assumptions without explanation within the reports as to whether the assumptions are solely driven by local circumstances. In addition, there appears to be no common understanding of what constitutes "prudence" as outlined within the CIPFA guidance quoted in Regulation 58 of the LGPS Regulations 2013.

2.7 As the valuation is a tool to set the balance between contributions and reliance on future investment return, it is for each Fund to determine their own pace of funding in conjunction with their own investment and risk appetite.

As such GAD acknowledges that there are significant challenges in achieving full consistency in the short term, although it is expected that there should be a narrowing of the range of assumptions used, where local experience cannot be used to justify differences.

2.8 The Scheme Advisory Board has developed a number of key performance indicators in regard a framework for consistent reporting across individual funds. To achieve the stated aims of Section 13, GAD recommend that funds publish the SAB's standard reporting metrics within the valuation reports to facilitate transparent and robust comparison. A chart showing how the relative ranking of funds by funding ratio has changed as a result of the standardised basis is on page 39 of the 'dry run' report.

2.9 Stakeholders should be aware that it is crucial that the standardised basis published within the 'dry run' report should not be used for anything other than a comparison tool, as the underlying discount rate bears no relation to any individual fund's investment or risk profile.

SOLVENCY

2.10 The requirement to set contributions to meet scheme liabilities as they arise does not compel a pension fund to be 100% funded at all times. For the purposes of Section 13, the rate of employer contributions was deemed by GAD to be set at a level to ensure solvency if:

- the rate of employer contribution is set to target full funding over an appropriate period, using appropriate actuarial assumptions in comparison with other funds, and

- employers have the financial capacity to increase employer contributions should future events demand.

2.11 There are ten solvency measures utilised by GAD, these are linked to present and emerging risk factors to determine a RAG flag matrix to illustrate a fund's solvency position. The methodology to define the analysis is contained within Appendix E of the 'dry run' report and results displayed within table F1 in Appendix F.

As identified within the report, the findings show that MPF's solvency rating is green for all measures except the 'asset shock' measure which received an amber rating. Asset shock relates to the change in average employer contribution rates as a percentage of payroll after a 15% fall in value of return –seeking assets.

2.12 The Fund actuary (Mercer) has fed back to GAD that the metric to measure asset shock and perceived affordability of increased contributions can significantly distort the outcome, depending on whether councils have shed staff due to budget cuts.

It has therefore been suggested that any variance in employer contribution rates should be assessed against local authority income, instead of payroll, as a fairer reflection of the ability of employers to shoulder the risk of asset shock. GAD has acknowledged that the 'asset shock' measure will require reconsideration prior to the next published report.

2.13 It has been MPF's long term view that the fundamental key to a successful funding regime is the requirement to retain an element of prudence within the actuarial assumptions to cope with adverse events which put pressure on contributions. The level of prudence adopted should be disclosed in the funding plan to ensure transparency and to promote greater understanding of the objectives of the funding plan to the constituent employers.

LONG TERM COST EFFICIENCY

2.14 The Act implies that "long term cost efficiency" means that employer contribution rates must not be set at a level that gives rise to additional costs, for example, by deferring costs to the future which would then lead to greater overall costs than if provided for at the present time.

2.15 To assess long term cost efficiency, ten measures were applied with regard to a number of absolute and relative considerations - as outlined in Appendix G with each fund's score documented within table HI in Appendix H, again using the RAG flag scoring matrix.

2.16 MPF was scored as green against all long term cost efficiency measures, indicating that that there are no material issues that may contribute towards a recommendation for remedial action to ensure long-term cost efficiency of contributions.

2.17 The Act permits GAD to change considerations or metrics to increase clarity in the analysis as its reporting methodology evolves.

3.0 RELEVANT RISKS

3.1 There is a risk that the league tables and the measures used will affect behaviour to the extent that they may actually lead to decision- making being unduly influenced by the measures applied by GAD, as opposed to the Fund's own circumstances.

4.0 OTHER OPTIONS CONSIDERED

4.1 Not relevant for this report.

5.0 CONSULTATION

5.1 Not relevant for this report.

6.0 OUTSTANDING PREVIOUSLY APPROVED ACTIONS

6.1 None associated with the subject matter.

7.0 IMPLICATIONS FOR VOLUNTARY, COMMUNITY AND FAITH GROUPS

7.1 Not relevant for this report.

8.0 RESOURCE IMPLICATIONS: FINANCIAL; IT; STAFFING; AND ASSETS

8.1 Officers will assess the Section 13 reporting measurements as part of the 2016 valuation process, but do not believe the funding regime will be unduly influenced as a result of the robust and sensible metrics inherent within the extant funding philosophy.

8.2 However, from a wider governance perspective and to support good risk management, the Fund intends to put the following measures in place for the 2016 valuation;

- a “CPI plus” funding approach which provides a clear link between investment strategy, the funding assumptions and risk objectives;
- covenant measurements and supporting tools to assess individual employer risk and to monitor these risks on an ongoing basis;
- bespoke risk management strategies incorporating clear approaches to manage specific liability, investment and employer risks;
- data quality reporting and error resolution operational processes to help improve Fund data and valuation accuracy.

9.0 LEGAL IMPLICATIONS

9.1 There are none arising from this report

10 EQUALITIES IMPLICATIONS

10.1 Has the potential impact of your proposal(s) been reviewed with regard to equality?

No, because Department of Communities and Local Government undertake equality impact assessments with regard to the cost management of the LGPS.

11.0 CARBON REDUCTION AND ENVIRONMENTAL IMPLICATIONS

11.1 There are none arising from this report

12.0 PLANNING AND COMMUNITY SAFETY IMPLICATIONS

12.1 There are none arising from this report

13.0 RECOMMENDATION

13.1 It is recommended that Members should consider the Section 13 measures as an integral part of the valuation, but any decisions on funding should be based on the Fund’s own circumstances, risk profile and long term objectives.

14.0 REASON/S FOR RECOMMENDATION/S

14.1 There is a requirement for Members of the Pension Committee to be kept up to date with legislative and best practice guidance as part of their decision making role.

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BRIEFING NOTES HISTORY

Briefing Note	Date