WIRRAL COUNCIL

PENSION COMMITTEE

3 FEBRUARY 2019

SUBJECT:	**FUNDING STRATEGY STATEMENT**
WARD/S AFFECTED:	**ALL**
REPORT OF:	**DIRECTOR OF PENSIONS**
KEY DECISION?	**YES**

1.0 EXECUTIVE SUMMARY

1.1 The LGPS Regulations require each administering authority to prepare and publish a Funding Strategy Statement (FSS). The final proposed Funding Strategy Statement is attached as Appendix 1. It incorporates the proposals on the funding strategy. There will be minor drafting changes between now and the statutory deadline of 31 March 2020.

1.2 A draft FSS was sent out to employers as part of the consultation process during November 2019 and feedback was requested. In order to assist employers with the consultation, the Fund Actuary communicated the key FSS changes at employer meetings in November.

1.3 A number of comments were received from employers following the consultation, and the FSS has been updated to reflect the comments made, particularly in relation to the policy on the prepayment of contributions. A summary of the comments and changes made are set out within this report.

1.4 The principal decision areas for the Committee are:

- The actuarial assumptions, deficit recovery plans and updated policies;
- Allowance in the FSS for the McCloud judgment; impact plus commentary on the considerations around the Cost Management Process in light of the judgment;
- The amendments regarding the policy on prepayment of employer contributions for employers and the operation of the policy.

1.5 The Fund officers request that the Committee delegate the refinement and finalisation of the FSS before the deadline of 31 March 2020.

2.0 BACKGROUND AND KEY ISSUES

2.1 The LGPS Regulations provide the statutory framework under which the Administering Authority is required to prepare and publish a Funding Strategy Statement (FSS) alongside each actuarial valuation. The Fund Actuary must have regard to the FSS as part of the actuarial valuation process.

2.2 The FSS must also be revised and published whenever there is a material change in either the policy set out in the FSS or the Investment Strategy Statement.

2.3 A draft FSS was prepared and sent to employers as part of the consultation (see from section 2.4 for employer comments). The FSS incorporated the following updates:

a) Review of the discount rate – An expected return analysis has been performed to determine the appropriate discount rate that should apply to the 2019 valuation. The discount rate is set to meet the primary objectives of the Fund which are to maintain solvency and long-term cost efficiency as per the Regulations and guidance in force.

b) The discount rate is expressed as the “real” expected asset return above CPI, given the benefits (i.e. liabilities) predominately increase with CPI increases. Given the current market and economic outlook there is an expectation of lower future real returns in the longer term. For the principal assumptions affecting the major employers we are proposing to reduce the expected level of real return above CPI for past service (benefits accrued up to the valuation date) by 0.25% p.a. from CPI +2% p.a. at the 2016 valuation to CPI+1.75% p.a., to maintain an appropriate level of prudence in the discount rate to meet the primary objectives. The discount rate to determine the future service contributions (benefits to be earned by current members in the future) has also been reduced from CPI +2.75% p.a. at the 2016 valuation to CPI+2.25% p.a. For those employers whose assets are invested in the medium risk investment strategy, a further reduction to the discount rates (for both past and future service) has been made.

c) Updates to the life expectancy assumptions following analysis performed on the Fund’s membership. The analysis indicates that whilst life expectancy is still increasing, the trend of improvement in longevity is beginning to taper off and this has been incorporated into the assumptions.

d) The notional period to recover a deficit (or run off a surplus of assets over liabilities) used is generally 3 years shorter than the period from the previous valuation. For the majority of the statutory employers, the recovery period has reduced from 19 years to 16 years. This is equivalent to a continuation of the 2016 recovery plan end date for most employers to achieve a 100% solvency or funding level. This would apply to employers, subject to covenant, risk and affordability considerations, and has been incorporated into the assumptions. For individual employers, their circumstances can mean a different approach is taken resulting in a bigger or smaller change to the period. This is dependent on the overall risk and affordability assessment for that employer with a view to maintaining contributions at an acceptable level in order to protect taxpayers.

e) The termination policy will require further technical review by the Fund Actuary regarding the appropriate life expectancy and inflation assumptions due to changes after the valuation date. Drafting notes have been included to highlight where changes may still be made prior to finalisation.

f) Updates to the FSS and the Fund policies included within it to allow for the potential Regulation changes as follows:

- **The Cost Management Process -** The cost management process was set up by HMT, with an additional strand set up by the Scheme Advisory Board (for the LGPS). The aim of this was to control costs for employers and taxpayers via adjustments to benefits and/or employee contributions. The outcomes of the cost management process were expected to be implemented from 1 April 2019. However, this has now been put on hold due to the McCloud case discussed below. Wording to set out the background of this issue has been included within the FSS.

- **McCloud judgment -** These are age discrimination cases brought in respect of the firefighter and judges' schemes, relating to protections provided when the public sector schemes were changed (which was on 1 April 2014 for the LGPS and 1 April 2015 for other public sector schemes). It is not known how these cases will affect the LGPS or the cost management process at this time and is almost certainly not going to be known by the time the valuation is signed off. The potential impact of McCloud has been quantified for each employer and the approach has been set out within the FSS. This is in line with the guidance from the Scheme Advisory Board. This has been communicated to employers alongside their valuation results to ensure that they are aware of the budget risk and are able to make provisions accordingly.

2.4 A consultation with employers regarding on the updates to the draft FSS took place during November 2019. In order to assist employers with the consultation, the Fund Actuary communicated the key FSS changes at employer meetings in November. Following this, a number of comments/queries were received from employers:

- A number of employers commented that the improvement in funding positions that have arisen at 2019 (resulting in reduced deficit contribution requirements) have provided them with an opportunity to prepay future service contributions, in exchange for an annual £ saving. This is to assist them with managing their budgets.
- An employer commented on the treatment of employers upon termination e.g. the circumstances when the assets and liabilities would be subsumed by the guarantor. They raised the possibility of including this wording within the Admission Agreement at the point that the employer enters the Fund.
- An employer asked further questions about the likelihood of the McCloud costs varying from the estimate provided. They also asked for clarity on whether they have to pay the additional cost into the Fund or is there an alternative available.
- An employer requested further clarity on recovery periods within the FSS for employers in surplus.
- The draft for consultation did not include the proposed changes to the investment strategy as the review had not been completed at that time. An employer asked the Fund to provide the strategy.

2.5 The Fund has replied to all queries from employers. As a result of the queries raised within the consultation, the Fund has updated the wording on prepayment of contributions.

The prepayment of future service contributions is a pilot policy that the Fund intends to introduce for a small number of larger employers. The intention of the pilot policy is to assess whether it would be practical (both administratively and in terms of treasury management) to allow all employers the option of prepaying their future service contributions at the start of the year in order to achieve a £ saving. The Fund must also ensure compliance with Regulations and Auditors. As this is a pilot, the full policy has not been incorporated into the FSS.

2.6 Once the FSS has been approved by the Committee, it will be refined and finalised by the Fund Officers in conjunction with the Fund Actuary to allow for the final valuation results and the remaining drafting notes set out within the document. The deadline for finalisation of the draft FSS is 31 March 2020.

3.0 RELEVANT RISKS

3.1 The actuarial valuation is a vital Governance tool to control the risks relating to the funding position and employer contributions requirements which have a material impact on budgets and local services. The funding strategy (along with the investment strategy) used to inform the actuarial valuation is a key determinant of the overall financial risk levels in the Fund. The FSS is a crucial document setting out the overall governance and controls in place to manage these risks on a whole Fund and individual employer level.

4.0 OTHER OPTIONS CONSIDERED

4.1 Not relevant for this report.

5.0 CONSULTATION

5.1 A consultation with employers on the key changes to the FSS took place during November 2019.

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 None associated with the subject matter

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

8.1 Further analysis by the Fund Actuary and discussion with Fund Officers is required to determine the appropriate assumptions to adopt within the termination policy.

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?

The differing characteristics and financial strength of employers have been reviewed to ensure that appropriate contribution easements have been applied equitably across all employers to prevent adverse risk falling on any individual employer.

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 The Committee approves the draft Funding Strategy Statement.

13.2 That Committee delegates the refinement and finalisation of the draft FSS by 31 March 2020 to officers.

14.0 REASON/S FOR RECOMMENDATION/S

14.1 It is the responsibility of the Pension Committee to agree the Funding Strategy.

REPORT AUTHOR Yvonne Murphy
Head of Pensions Administration
Telephone (0151) 242 1333
Email yvonnemurphy@wirral.gov.uk

BRIEFING NOTES HISTORY

Briefing Note	Date
FUNDING STRATEGY STATEMENT	**Draft Funding Strategy Statement 29.10.2018**