



LOCAL PENSION BOARD – 8 FEBRUARY 2023

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

PENSION FUND VALUATION – CONSULTATION RESULTS, FINAL ASSUMPTIONS AND RESULTS

Purpose of the Report

1. The purpose of this report is to inform the Local Pension Board of the results of the consultations on the draft Funding Strategy Statement (FSS) and draft Investment Strategy Statement (ISS), the final assumptions used in the valuation and the whole fund results.

Background

2. Each Local Government Pension Scheme (LGPS) administering authority has a statutory obligation to have an actuarial valuation carried out every three years and all Funds in England and Wales have a valuation carried out as of 31 March 2022.
3. The major purpose of the actuarial valuation is for the actuary to set employer contribution rates for a three-year period, that commences one year after the valuation date (i.e., for the period 1 April 2023 to 31 March 2026).
4. As part of the valuation Officers must review and update the Fund's Funding Strategy Statement (FSS) and Investment Strategy Statement (ISS). The FSS underpins the Fund policies and includes a table detailing the Fund's framework for setting contribution rates for differing employer groups. The ISS underpins the Fund investment policies.
5. As part of the valuation process, in December 2022 employers were written too, detailing the FSS and ISS highlighting any changes. They were invited to make comments in writing to officers during a period of consultation on both documents by the 15 January 2023.
6. A timetable of the valuation process is included in the report.

Funding Strategy Statement (FSS)

7. The Actuary and Fund Officers worked collaboratively on the Fund's FSS. Officers used this opportunity to review the "style and presentation" of the FSS, with the intention of making this easier to navigate for all parties.
8. The new style FSS, attached as Appendix A to this report, comprises two main sections, a core section and four appendices.
9. Much of the information in the new style draft FSS remains the same as the Fund's previous FSS, but for ease the key changes are highlighted in yellow. These are detailed as follows;
 - a) Contribution reductions (Point 2.3). This sets out the Fund's proposal on how to deal with long-term employers, not covered by the stability mechanism, especially for those well-funded employers.

This is designed to protect the Fund but also aims to be reasonable with the employers.

- **Employers less than 100% funded:** Pay the higher of the current rate in payment or the newly calculated rate, to increase their funding level.
- **Employers between 100% and 110% funded:** Pay a rate that falls between the existing rate in payment and the new primary rate, subject to a floor of the new primary rate, to continue to build up their funding level.
- **Employers between 110% and 120% funded:** Pay new primary rate only, to maintain their funding level.
- **Employers above 120% funded:** Pay the new primary rate, with some reduction via negative secondary rate, to gradually reduce their funding level down.

Short-term employers, typically admission bodies, are subject to different rules. In general, these bodies will pay their new Primary rate with any surplus or deficit spread over their time horizon.

- b) Prepayment of contributions (Point 2.9). There is no change to the Fund's current approach for the prepayment of contributions, however this is now more explicit in the FSS.
- c) Early retirement on ill-health grounds (Point 3.2). There is no change to the Fund's current approach to ill health risk mitigation, however this is now more explicit in the FSS.
- d) Risk and control – For best practice the FSS now includes a link to the Fund's risk register (Appendix C – C1). The risk register will continue to be reviewed by Officers.

- e) Employer covenant assessment and monitoring (Appendix C – C6). There is no change to the Fund's current approach, however this is now more explicit in the FSS.
- f) Climate risk and TCFD reporting (Appendix C – C7). This makes the Fund's approach more explicit in the FSS.
- g) The Fund has updated the assumptions applied at cessation following an employer's exit from the Fund (Appendix D – D5). This proposed change moves away from a gilts-based cessation for employers exiting the Fund with no guarantor.

Consultation replies (FSS)

- 10. There were only a very small number of replies from employers on the FSS and all related to a wider general understanding of the document. No employers made suggested changes to the FSS. The draft FSS will be presented to the Local Pension Committee in March 2023 for approval.

Investment Strategy Statement (ISS)

- 11. The ISS details the Fund's investment strategy. It is periodically reviewed at least every three years in line with the valuation.
- 12. The Local Pension Committee seeks to invest in accordance with the ISS any Fund money that is not needed immediately to make payment from the Fund. Decisions affecting the Fund's ISS are taken with appropriate advice from the Fund's advisers.
- 13. The Local Pension Committee makes decisions based on a long-term investment strategy with regular reviews, usually annually in the form of the asset allocation review. This is with the aim to maximise investment returns of the Fund whilst maintaining an acceptable level of risk.

Consultation replies (ISS)

- 14. There were no replies from employers on the ISS. The draft ISS will be presented to the Local Pension Committee in March 2023 for approval.

Net Zero Climate Strategy

- 15. In addition to the FSS and ISS consultations, the Fund prepared a Net Zero Climate Strategy, and a consultation took place with all relevant stakeholders that closed on the 5 February 2023. The Fund employers were informed about this in writing.
- 16. The Strategy looks to address the risk of climate change to the Fund by reducing its carbon emissions whilst maintaining investment returns. A separate report to the Local Pension Board covers this. Officers are working

through the results of the consultation and will provide a summary to the Local Pensions Committee in March 2023.

Assumptions – June 2022

17. There are several assumptions used in the Fund Valuation. These were taken to the Pension Committee on the 10 June 2022 and were provisionally approved for the 2022 Fund Valuation. However, they remained under review given the ongoing financial uncertainty and rising inflation in 2022, and the CPI assumption was raised slightly from 2.7% to 2.9% and taken to Committee on the 18 November 2022 for approval.

18. The final assumptions used in the valuation are detailed in the following table.

Assumption	Approach
Future investment return	4.4% p.a. Based on the Fund's agreed 75% prudence level; the Fund's investment strategy has a 75% likelihood of achieving annualised return of 4.4% pa over the next 20 years.
Benefit Revaluation and Pensions Increase	2.9% p.a. Based on the annualised (average) CPI outcome modelled over the next 20 years
Salary Increases	0.5% above 2.9% CPI inflation
Longevity	A long-term trend of 1.5% annual improvements
Others	Model using the Leicestershire Fund data and based on the Club Vita analysis

19. The Fund aims to have employer funding levels around 110%. This is designed to provide a buffer against significant shocks in the markets.

20. These assumptions will be presented to the Local Pension Committee in March 2023 for approval.

Indicative Whole Fund Result

21. Using the assumptions detailed above the indicative funding position for the whole Fund improved from 89% at the 31 March 2019 valuation, to 105% at the 31 March 2022 valuation.

22. This is a welcome improvement, driven in the main by higher-than-expected investment return. Over the three-year valuation period (between 2019 and 2022) the expected investment return was 11.8%, but the actual investment return was 34.3% (a difference of 22.5%), impacting on the funding position positively by £867m. However, it is important to note this is not a guide for future investment growth.

23. The improved whole Fund funding position has generally improved individual employer funding positions too. Individual employer rates have been calculated and all employers were written to in December 2022 with their individual indicative rates (April 2023 to March 2026). The methodology detailed in the FSS and highlighted in point 9 of this report was used to establish employer rates for the long-term employers.
24. A small number of employers contacted Officers in December 2022 after receiving their rates, but only for a broader understanding of the valuation.
25. No employer has requested a recalculation of their rates.
26. Five of the largest employers requested revised calculations to help them decide whether to make payment of all their secondary rate as cash in 2023/24. The Fund Actuary is working through these cases, but it is important to note early payment does not guarantee lower rates in future and brings its own element of risk. This will be raised with these employers before they make a final decision.
27. The Pension Fund AGM took place on the 12 December 2022 and the Fund Actuary attended virtually to provide a presentation on the valuation. All the employers were invited and were provided the opportunity to discuss their individual rates with the Actuary and Officers. Only a very small number of employers attended in person and no valuation questions were raised during or after the meeting.

Timeline

28. The latest valuation timeline is detailed as follows.

Date	Topic	Action or Awareness
August/September 2021	Mid-valuation funding update	Board/Committee – done
September 2021	Provide Hymans Robertson with stabilised employer data	Pension Section - done
September/October 2021	Calculate indicative stabilised employer rates	Hymans Robertson – done
November 2021	Agree principles for the 2022 assumptions	Committee - done
March 2022	Results of the stabilised employer modelling	Committee – done
April 2022	Provide the stabilised employers with their indicative rates. 1 April 2023 to 31 March 2026	Pension Section/Stabilised employers – done

June 2022	Detail proposed valuation assumptions	Committee – done
August 2022	Provide Hymans with all Fund data	Pension Section – done
August/September 2022	Review selected employer's financial health	Pension Section – done
September 2022	Review proposed key policy changes to the Funding Strategy Statement	Committee – Meeting cancelled due to the Queen's passing. Will now be taken to November Committee
September/October 2022	Calculate Whole Fund results	Hymans Robertson - done
October/November 2022	Whole Fund valuation results	Board/Committee – done
November 2022	Investment Strategy Statement Draft Funding Strategy Statement (full)	Committee – done
November 2022 (through to January 2023)	Provide the other employers with their indicative rates. 1 April 2023 to 31 March 2026. Start a consultation with employers on the Funding Strategy Statement and Investment Strategy Statement (subject to possible amendments for the climate strategy)	Pension Section/Fund employers – done
January 2023	Changes to Funding Strategy Statement and Investment Strategy Statement	Pension Section/Fund employers – done
February/March 2023	Final assumptions and Funding Strategy Statement and Investment Strategy Statement finalised	Committee/Board – current stage
March 2023	Final valuation report produced with final employer rates	Hymans Robertson
April 2023 to March 2026	Employer rates implemented	Pension Section/Fund employers

Recommendation

29. It is recommended that the Board notes;

- a) The revised Funding Strategy Statement which will be presented to the Local Pension Committee for approval in March 2023;
- b) The revised Investment Strategy Statement that will be presented to the Local Pension Committee for approval in March 2023;
- c) The final assumptions that will be presented to the Local Pension Committee for approval in March 2023;
- d) The 105% indicative whole fund valuation result.

Equality and Human Rights Implications

30. There are no equality or human rights implications arising from the recommendations in this report.

Appendix

Appendix A – Fund’s Draft Funding Strategy Statement

Appendix B – Fund’s Draft Investment Strategy Statement

Background Papers

Local Pension Board Report 26 October 2022 – [Pension Fund Valuation – Funding Strategy Statement and Indicative Whole Fund Results](#)

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