



## **LOCAL PENSION COMMITTEE – 3 MARCH 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 provide the Local Pension Committee with an update concerning the outcome of consultation on the draft Funding Strategy Statement (FSS) and draft Investment Strategy Statement (ISS) and seeks the Board's approval of the final versions of both strategies.
2. The report also seeks approval of the final assumptions used in the 2022 Fund valuation and the indicative whole fund valuation result.

#### **Background**

3. 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.
4. 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).
5. 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.
6. 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.
7. A timetable of the valuation process is included in the report.

### **Funding Strategy Statement (FSS)**

8. 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.
9. The new style FSS, attached as Appendix A to this report, comprises two main sections, a core section and four appendices.
10. Much of the information in the new style draft FSS remains the same as the Fund's previous FSS. The key changes are 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 (Taskforce on Climate Financial Disclosures) 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)**

- 11. 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 was presented to the Local Pension Board on the 8 February 2023 and the Board supported it.
- 12. There has been one subsequent change to the draft FSS, requested by the Fund Actuary. This is highlighted in green on page 8 (section 4.2). This is a new paragraph making it explicit that benefits of members likely to be affected by the McCloud remedy, have been valued in line with expected regulations, as currently the remedy remains outstanding.
- 13. The draft FSS is now presented to the Local Pension Committee for approval.

### **Investment Strategy Statement (ISS)**

- 14. The ISS details the Fund’s investment strategy. It is periodically reviewed at least every three years in line with the valuation.
- 15. 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.
- 16. 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)**

- 17. There were no replies from employers on the ISS. The draft ISS was presented to the Local Pension Board on the 8 February 2023 and the Board

supported it. The draft ISS is now presented to the Local Pension Committee for approval.

### **Net Zero Climate Strategy**

18. 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.

19. 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 Committee is included in the agenda.

### **Assumptions – June 2022**

20. There are several assumptions used in the Fund Valuation. These were presented 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 Consumer Price Index (CPI) assumption was raised slightly from 2.7% to 2.9% and taken to Committee on the 18 November 2022 for approval.

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

<b>Assumption</b>	<b>Approach</b>
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

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

23. These assumptions are presented to the Local Pension Committee for approval.

### **Indicative Whole Fund Result**

24. 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.
25. 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.
26. 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.
27. A small number of employers contacted Officers in December 2022 after receiving their rates, but only for a broader understanding of the valuation.
28. No employer has requested a recalculation of their rates.
29. 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 provided this information in February, and the employers are considering it. It is important to note early payment does not guarantee lower rates in future and brings its own element of risk. This was highlighted to the 5 employers. Employers choosing to front load contributions will be reflected in the Actuary's final rates and adjustment certificate, provided at the end of March 2023.
30. 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.
31. Hymans Robertson the Fund Actuary has drafted the Leicestershire Pension Fund Report on the actuarial valuation at 31 March 2022. It provides a summary of the valuation and results. It does not include the final rates and adjustment certificate as this is completed at the end of March 2023. However, all the Fund employers have received their indicative employer rates for the 3 years – 1 April 2023 to 31 March 2026.

32. The final Leicestershire Pension Fund Report will also include details on the Government Actuary Department (GADs) Section 13 dashboard. This will be available at the end of March 2023. The draft report is attached as Appendix C.

### Timeline

33. The latest valuation timeline is detailed as follows.

<b>Date</b>	<b>Topic</b>	<b>Action or Awareness</b>
August/September 2021	Mid-valuation funding update	Board/Committee – <b>done</b>
September 2021	Provide Hymans Robertson with stabilised employer data	Pension Section - <b>done</b>
September/October 2021	Calculate indicative stabilised employer rates	Hymans Robertson – <b>done</b>
November 2021	Agree principles for the 2022 assumptions	Committee - <b>done</b>
March 2022	Results of the stabilised employer modelling	Committee – <b>done</b>
April 2022	Provide the stabilised employers with their indicative rates. 1 April 2023 to 31 March 2026	Pension Section/Stabilised employers – <b>done</b>
June 2022	Detail proposed valuation assumptions	Committee – <b>done</b>
August 2022	Provide Hymans with all Fund data	Pension Section – <b>done</b>
August/September 2022	Review selected employer's financial health	Pension Section – <b>done</b>
September 2022	Review proposed key policy changes to the Funding Strategy Statement	Committee – <b>Meeting cancelled due to the Queen's passing. Was taken to November Committee</b>
September/October 2022	Calculate Whole Fund results	Hymans Robertson - <b>done</b>
October/November 2022	Whole Fund valuation results	Board/Committee – <b>done</b>
November 2022	Investment Strategy Statement Draft Funding Strategy Statement (full)	Committee – <b>done</b>

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 – <b>done</b>
January 2023	Changes to Funding Strategy Statement and Investment Strategy Statement	Pension Section/Fund employers – <b>done</b>
February/March 2023	Final assumptions and Funding Strategy Statement and Investment Strategy Statement finalised	Committee/Board – <b>current stage</b>
March 2023	Final valuation report produced with final employer rates	Hymans Robertson – <b>current stage</b>
April 2023 to March 2026	Employer rates implemented	Pension Section/Fund employers

### **Recommendation**

34. It is recommended that the Local Pension Committee approves.

- a) The revised Funding Strategy Statement;
- b) The revised Investment Strategy Statement;
- c) The final assumptions used in the 2022 Fund valuation;
- d) The 105% indicative whole fund valuation result.

### **Equality and Human Rights Implications**

35. 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  
Appendix C – Report on the Actuarial Valuation 31 March 2022

**Background Papers**

Local Pension Committee 18 November 2022 – 2 reports.

Pension Fund Valuation – Indicative Whole Fund Results  
<https://politics.leics.gov.uk/documents/s172312/Pensions%20Committee%20Whole%20Fund%20Results%2018112022%20f1.pdf>

Funding Strategy Statement, Investment Strategy Statement, and Investment Advisor Objectives  
<https://politics.leics.gov.uk/documents/s172330/FSS%20ISS%20Inv%20advisor%20objectives%20-%20Committee%20Nov%202022%20f.pdf>

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