TEESSIDE PENSION FUND

Administered by Middlesbrough Council

AGENDA ITEM 7

TEESSIDE PENSION BOARD REPORT

7 NOVEMBER 2016

STRATEGIC DIRECTOR FINANCE, GOVERNANCE & SUPPORT – JAMES BROMILEY

SECTION 13 DRY RUN REPORT

1. PURPOSE OF THE REPORT

1.1 To inform Members of the Teesside Pension Board (the Board) of the of the Government Actuary Department (GAD) LGPS Section 13 Dry Run Report.

2. RECOMMENDATION

2.1 That Members review and note the Report (Appendix A), and pass any comments.

3. FINANCIAL IMPLICATIONS

3.1 There are no financial implications from this report.

4. SECTION 13

4.1 Section 13 refers to the relevant section in the Public Service Pension Act 2013, which states:

> **13 Employer contributions in funded schemes**
>
> (1) This section applies in relation to a scheme under section 1 which is a defined benefits scheme with a pension fund.
>
> (2) Scheme regulations must provide for the rate of employer contributions to be set at an appropriate level to ensure—
>
> (a) the solvency of the pension fund, and
>
> (b) the long-term cost-efficiency of the scheme, so far as relating to the pension fund.
>
> (3) For that purpose, scheme regulations must require actuarial valuations of the pension fund.
>
> (4) Where an actuarial valuation under subsection (3) has taken place, a person appointed by the responsible authority is to report on whether the following aims are achieved—

(a) the valuation is in accordance with the scheme regulations;

(b) the valuation has been carried out in a way which is not inconsistent with other valuations under subsection (3); and

(c) the rate of employer contributions is set as specified in subsection (2).

(5) A report under subsection (4) must be published; and a copy must be sent to the scheme manager and (if different) the responsible authority.

(6) If a report under subsection (4) states that, in the view of the person making the report, any of the aims in that subsection has not been achieved—

(a) the report may recommend remedial steps;

(b) the scheme manager must—

(i) take such remedial steps as the scheme manager considers appropriate, and

(ii) publish details of those steps and the reasons for taking them.

(c) the responsible authority may—

(i) require the scheme manager to report on progress in taking remedial steps; and

(ii) direct the scheme manager to take such remedial steps as the responsible authority considers appropriate.

(7) The person appointed under subsection (4) must, in the view of the responsible authority, be appropriately qualified.

4.2 For the LGPS, the responsible authority (4) is the Secretary of State for Communities and Local Government, and the person appointed (7) is GAD. In the LGPS, the Administering Authorities are the scheme managers (5).

4.3 GAD were asked to undertake a Dry Run Report based on the 2013 actuarial valuations for each Fund in England & Wales. The results are published at:

http://www.lgpsboard.org/images/Reports/Section13DryRun20160711.pdf, and
http://www.lgpsboard.org/images/Reports/Section13DryRunAppendices20160711.pdf

4.4 Section 13 will apply for the first time to the 2016 round of LGPS (England & Wales) separate fund valuations. The purpose of the dry run is to allow GAD to refine their approach and help administering authorities prepare for the first 2016 report. The expected 2016 report is expected to be available by late 2018 or early 2019.

5. DRY RUN REPORT – FINDINGS

5.1 GAD's report reviewed the main aims of Section 13 to ensure they were achieved by the LGPS Funds of England & Wales:

- Compliance – whether a fund's valuation is in accordance with the scheme regulations;
- Consistency – whether the fund's valuation has been carried out in a way which is not inconsistent with the other funds valuations within the LGPS, i.e. it should be relatively straight-forward to compare the valuations of two LGPS funds.
- Solvency – whether the rate of employer contributions is set at an appropriate level to ensure the solvency of the pension fund; and
- Long-term cost efficiency – whether the rate of employer contributions is set at an appropriate level to ensure the long-term cost-efficiency of the scheme, so far as relating to the pension fund.

5.2 There was no evidence of material non-compliance with the regulations.

5.3 There were inconsistencies between the valuations in terms of approach taken, assumptions used and disclosure. GAD conclude these inconsistencies make meaningful comparison of local valuation results difficult. However, GAD have used standardised assumptions to standardise valuation results and provide comparison of funds on solvency and long-term cost efficiency.

5.4 On the standardised basis, the Teesside Fund's valuation 2013 result moved from 101% to 103% funded, and from first to fourth best funded in England & Wales (see chart on page 38 of the Dry Run Report).

5.5 Solvency means that the rate of employer contributions should be set at "such a level as to ensure that the scheme's liabilities can be met as they arise". GAD do not regard that this means that a pension fund should be 100% funded at all times. Rather, and for the purposes of section 13, we consider that the rate of employer contributions shall be deemed to have been set at an appropriate level to ensure solvency of the pension fund if:

- The rate of employer contributions is set to target a funding level for the whole fund (assets divided by liabilities) of 100% over an appropriate time period and using appropriate actuarial assumptions (where appropriateness is considered in both absolute and relative terms in comparison with other funds); and *either*
- Employers collectively have the financial capacity to increase employer contributions, should future circumstances require, in order to continue to target a funding level of 100%; *or*
- There is an appropriate plan in place should there be, or if there is expected in future to be, no or a limited number of fund employers, or a material reduction in the capacity of fund employers to increase contributions as might be needed.

5.6 In assessing whether the conditions in paragraph 5.5 are met, we will have regard to:

Risks already present:

- Funding level on the SAB standard basis;

- The extent to which the fund continues to be open to new members. If the fund is closed to new members or is highly mature, we will focus on the ability to meet additional cash contributions;
- The ability of the fund to meet benefits due (without constraining investment policy); and
- The ability of tax raising authorities to meet employer contributions.

Emerging risks:

- The cost risks posed by changes in the value of the scheme liabilities (to the extent that these are not matched by changes to the scheme assets);
- The cost risks posed by changes to the value of scheme assets (to the extent that these are not matched by changes to the scheme liabilities);
- The proportion of scheme employers without tax raising powers or without statutory backing; and
- How the risks above compare with the pensionable payroll of scheme employers, and the wider income of sponsoring employers as a whole.

5.7 GAD scored each measure using a RAG rating (Red/Amber/Green), where:

- RED – Indicates a potentially material issue that may contribute to a recommendation for remedial action.
- AMBER – Indicates a possible risk.
- GREEN – Indicates no material issues that may contribute to a recommendation for remedial action.

5.8 The Teesside Fund's results are shown on page 45 of the Dry Run Report, with only one Amber result – Asset Shock. Asset shock measures the change in average employer contribution rates as a percentage of payroll after a 15% fall in value of return-seeking assets (equities, property and alternative investments).

5.9 GAD report on whether the rate of employer contributions to the pension fund are set at an appropriate level to ensure the long-term cost efficiency of the scheme, so far as relating to the pension fund.

5.10 The Public Service Pension Act 2013 states that: "Long-term cost-efficiency implies that the rate must not be set at a level that gives rise to additional costs. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the time."

5.11 GAD concluded that, overall, the rate of employer contributions were set at an appropriate level to ensure long term cost efficiency if the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual, with an appropriate adjustment to that rate for any surplus or deficit in the fund.

5.12 Again, GAD scored each fund against a number of measures using a RAG Rating. The Teesside Fund's results were all Green, see page 38 of the Appendices to the Dry Run Report.

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