Finance Department
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Report of: Corporate Director of Resources

Meeting of:	**Date**	**Agenda item**	**Ward(s)**
Pension Board/Pensions Sub-Committee	3 December 2019		n/a

Delete as appropriate	~~Exempt~~	Non-exempt

SUBJECT: 2019 ACTUARIAL VALUATION – DRAFT FUNDING STRATEGY STATEMENT

1. Synopsis

1.1 The Council must produce a Funding Strategy Statement (FSS) a requirement by The Local Government Pension Scheme Regulations 2013 (as amended) ("the 2013 Regulations") and the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 ("the 2014 Transitional Regulations") (collectively; "the Regulations") provide the statutory framework from which the Administering Authority is required to prepare a Funding Strategy Statement (FSS). Under the Regulations, the administering authority must prepare, maintain and publish a written statement setting out their funding strategy. In doing so the administering authority must consult with such persons as they feel appropriate. The Fund's actuary must have regard to the FSS in carrying out the formal actuarial valuation of the Fund.

A Funding Strategy Statement will be prepared by London Borough of Islington (the Administering Authority) to set out the funding strategy for the Islington Council Pension Fund (the "Fund"), in accordance with Regulation 58 of the Local Government Pension Scheme Regulations 2013 (as amended) and guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

1.2 This report informs the pension board and pensions sub-committee of the main issues that employers admitted into the Fund are to be consulted on, in the draft FSS, as part of the 2019 actuarial review.

2. Recommendations

2.1 To review and note a summary of the main updates in the draft FSS , that employers are going to be consulted on between December and January 2020.

2.2 Agree that officers with the Fund Actuary update the FSS for consultation with Employers admitted into the Islington Fund .

3. Background

Introduction

3.1 The 2019 actuarial valuation is now underway and as part of the process preparatory work is being undertaken to determine the funding position and investment strategy review that can support sustainable contributions from employers.

3.1.1 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.

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.

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3.1.2 The draft FSS is being prepared and, the main updates since the last valuation include the following:

a) An update for the latest Regulations i.e. to reflect the introduction of Exit Credits that were introduced in 2018.

b) Review of the discount rate - Expected return analysis has been performed to inform the decision on the appropriate discount rate for the 2019 valuation. The discount rate is expressed as the "real" expected asset return above CPI. Following a period of strong investment returns, the outlook is now for lower returns in the future. Therefore, following discussions between the Actuary, Officers and Members, it will be proposed to reduce the expected level of real return above CPI for past service from CPI +2.2% p.a. at the 2016 valuation (CPI+2.3% for the Council) to CPI+1.8% p.a., to maintain an appropriate level of prudence in the discount rate. It will also be proposed to reduce the discount rate for future service from CPI +2.75% p.a. at the 2016 valuation to CPI+2.25% p.a.

c) It is also proposed to make an allowance for additional real returns of up to 0.2% p.a. to be earned during the Council's recovery period. A similar approach was adopted at the 2016 valuation, reflecting the long-term covenant of the Council and is based upon potential investment strategy changes that will support the additional return assumption without a corresponding increase in risk. This to ensure the Council's budgetary requirements are met based on the outcomes of the valuation calculations discussed with the Actuary, Officers and Members.

d) 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 rate of increase experienced in short-term since the 2016 valuation was less than was built into the assumptions. This has been incorporated into the assumptions for the 2019 valuation along with an adjustment to the longer-term projection to reflect current views.

e) Alongside the long term salary increase assumption of CPI+1.5% p.a., it is proposed to allow for expected short term pay restraint of 2% p.a.(covering both headline increases and incremental drift) up to 31 March 2023 although employers will be able to opt for the long-term assumption only should they wish.

f) There is a proposed reduction in the average deficit recovery period of 3 years, which is generally equivalent to maintaining the same end date as the 2016 deficit recovery plan. This would apply to employers, subject to covenant and affordability considerations, and has been incorporated into the assumptions.

g) Updates to the Fund policies included within it (e.g. admission and termination) to allow for the potential Regulation and guidance changes. Whilst these are still at the consultation stage, it is important that they are built into the FSS as they may be implemented before the valuation report is signed off. The key changes which have been incorporated are as follows:

i) **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 and if, as expected, it is not implemented the wording in the draft FSS will fall away

ii) **McCloud judgment** - These are age discrimination cases brought in respect of the firefighters 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/the cost management process will need to be quantified as reasonably as possible based on the information available. This is in line with the guidance from the Scheme Advisory Board. The potential impact of the McCloud judgment on contribution outcomes will be communicated to employers as part of the consultation on the FSS to ensure that they are aware of the budget risk and are able to make provisions accordingly.

iii) **4 yearly valuation cycle and interim valuations/employer contribution reviews** – MHCLG have proposed to amend the local fund valuation cycle of the LGPS from the current three year (triennial) cycle to a four year (quadrennial) one with effect from 2024. It is proposed to phase this in by requiring a valuation in 2022, 2024 and 4 years thereafter. It is also proposed to introduce a power for LGPS funds to undertake interim valuations (in full or in part) and allow LGPS administering authorities to amend an employer’s contribution rate in between valuations. The situations when this would be applied will therefore be incorporated into the FSS.

iv) **Deferred employers** - the introduction of a 'deferred employer' status that would allow funds to defer the triggering of an exit payment for certain employers who have a sufficiently strong covenant.

v) **Deemed employers** - This is an alternative route to the admitted body route for achieving pension protection. It relates to employers which have employees working for a third party but fall under the deemed employer for the purposes of the Regulations. An update to Fund policies will therefore be required.

Further updates on the progress of these Regulatory issues will be provided to the Board and Committee in due course.

3.1.3 Members are asked to note the updates and agree that officers with the Fund Actuary update the FSS for consultation with Employers admitted into the Islington Fund. The results of the consultation will be reported to Members at the March meeting so that an informed decision can be made to approve the final version of FSS for publication by end of March.

4. Implications

4.1 Financial implications

4.1.1 The cost of providing actuarial advice is part of fund management and administration fees charged to the pension fund.

4.2 Legal Implications

The Local Government Pension Scheme Regulations 2013 (as amended) ("the 2013 Regulations" and the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 ("the 2014 Transitional Regulations") (collectively; "the Regulations") provide th statutory framework from which the Administering Authority is required to prepare a Funding Strategy Statement (FSS).

Prior to agreeing the statement, the Council must have proper regard to any comments received from the consultees.

4.3 Environmental Implications and contribution to achieving a net zero carbon Islington by 2030:

None applicable to this report. Environmental implications will be included in each report to the Pension Board Committee as necessary. The current agreed investment strategy statement for pensions outlines the policies and targets set to April 2022 to reduce the current and future carbon exposure by 50% and 75% respectively compared to when it was measured in 2016 and also invest 15% of the fund in green opportunities. The link to the full document is https://www.islington.gov.uk/~/media/sharepoint-lists/public-records/finance/financialmanagement/adviceandinformation/20192020/20190910londonboroughofislingtonpensionfundinvestmentstrategystatement.pdf

4.4 **Resident Impact Assessment**

None applicable to this report. The council must, in the exercise of its functions, have due regard to the need to eliminate discrimination, harassment and victimisation, and to advance equality of opportunity, and foster good relations, between those who share a relevant protected characteristic and those who do not share it (section 149 Equality Act 2010). The council has a duty to have due regard to the need to remove or minimise disadvantages, take steps to meet needs, in particular steps to take account of disabled persons' disabilities, and encourage people to participate in public life. The council must have due regard to the need to tackle prejudice and promote understanding.

4.4.1 An equalities impact assessment has not been conducted because this report is an update on existing exercise and the consultation of employers will mitigate any inequality issues.

5. Conclusion and reasons for recommendation

5.1 Members asked to review and note the updates to prepare the draft FSS for employers' consultation.

Background papers:
None

Final report clearance:

Signed by: Corporate Director of Resources Date

Received by:

Head of Democratic Services Date

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