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CITY OF WOLVERHAMPTON COUNCIL	**Pensions Board** 22 January 2019

Report Title	Preparations for 2019 Actuarial Valuation	
Originating service	Pension Services	
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Recommendation for noting:

The Board is asked to note:

1. The report and the associated preparatory work and planning for the 2019 actuarial valuation of both the West Midlands Pension Fund (the Main Fund) and the West Midlands Integrated Transport Authority Fund (the WMITA Fund).

1.0 Purpose

1.1 To provide the Board with an overview of the 2019 actuarial valuation process, deliverables and context in preparation for the review of funding strategy and employer contribution rates.

2.0 Background

2.1 The Administering Authority of each LGPS pension fund must obtain an actuarial valuation as at 31 March 2019 in accordance with the requirements of Regulation 62 of the Local Government Pension Scheme Regulations 2013.

The primary aims of the actuarial valuation are to;

- Review the financial position of the Fund (assets relative to the expected cost of providing accrued pension benefits) relative to its objective for full funding;
- Assess the cost of benefits expected to accrue in the future;
- Where appropriate, and following consultation, revise the Funding Strategy Statement and Investment Strategy Statement.
- Taking the above into account, determine the appropriate level of employer contributions for the three-year period commencing April 2020.

2.2 The Funding Strategy Statement (FSS) together with the Rates and Adjustments actuarial certificate and actuary's valuation report summarise the outcome of the valuation (approach, assumptions and contribution requirement) and form the formal documentation the Administering Authority is required to put in place before 31 March 2020. In setting the contribution requirements for participating employers, the Fund actuary details a primary and secondary rate in the Rates and Adjustments certificate.

2.3 The primary rate of contribution, as defined by Regulation 62(5), is the employer's share of the cost of benefits accruing in each of the three years beginning 1 April 2020. In addition, employers may pay a secondary contribution as required under Regulation 62(7) set to address any funding deficit. This secondary rate is based on individual employer circumstances and so adjustments are made for each employer. Funding strategy and contribution rates cannot be considered in isolation – the funding review will incorporate an assessment of employer covenant risk and will be carried out in conjunction with the investment strategy review.

2.4 This report provides an outline of the Fund (employer and member) and regulatory changes since the 2016 valuation which may impact on funding discussions in 2019/20.

3.0 Main Fund 2016 actuarial valuation outcome

3.1 The valuation as at 31 March 2016 showed a funding shortfall of £2,650m based on the assumptions made for calculating the funding target. This represented a funding level of 81%.

3.2 The actuary certified a Primary Rate – the amount required to cover the cost of future benefit accrual and ensure solvency, expressed as a percentage of active member pay (the overall average employer contribution rate) of 18.6% of Pensionable Pay.

3.3 The shortfall was expected to be recovered through additional employer contributions as specified for each employer over their deficit recovery period. At Fund level, recovery of the shortfall of £2,650m required a total deficit contribution (secondary contribution) of £165m per annum increasing at 3.9% per annum for 20 years.

3.4 Contributions for each individual employer were set as a combination of a percentage of payroll to cover the expected cost of the employer's active member benefit accrual and a cash lump sum amount to meet the employer's share of deficit contributions due under the recovery plan. These are recorded in the Rates and Adjustments actuarial certificate which covers contributions due to April 2020 and is legally binding.

4.0 WMITA Fund 2016 actuarial valuation outcome

4.1 The valuation as at 31 March 2016 showed a funding shortfall of c£105m based on the assumptions made for calculating the funding target. This represented a funding level of 82%.

4.2 The actuary certified a Primary Rate, for the single active employer, of 25.1% of Pensionable Pay.

4.3 The shortfall was to be recovered through additional employer contributions as specified for each employer over the deficit recovery period in each case. The contributions of £325,000 per annum due from Preston Bus Limited anticipate recovery of the deficit in just over nine years from the valuation date. For West Midlands Travel Limited the level of deficit contributions was set at £7.3million per annum for 2017/18 increasing at 2.3% p.a.

4.4 Contributions for West Midlands Travel Limited were set as a combination of a percentage of payroll to cover the expected cost of active member benefit accrual and a cash lump sum amount to meet the deficit contributions due under the recovery plan. For Preston Bus Limited, for whom there are no remaining active members, contributions were expressed solely as a cash lump sum amount in accordance with the recovery plan. The contributions due are recorded in the Rates and Adjustments actuarial certificate. Deficit contributions agreed as part of the 2016 actuarial valuation are backed by guarantee from National Express Group. The liabilities of Preston Bus are backed by guarantee from Preston City Council.

5.0 Developments since 2016

5.1 Changes to the Main Fund employer base, membership profile and experience over the three years to 31 March 2019 will impact on the outcome of the 2019 valuation, as will changes to the regulatory environment.

Employer base

5.2 As at 30 November 2018, the number and profile of employers within the Main Fund had changed significantly since the 31 March 2016 valuation and the movements are summarised in the following table:

Employer Type	Number of employers at 2016 valuation	New employers since 2016 valuation	Cessations since 2016 valuation	Number of employers as at 30 November 2018
Scheduled - District	7	0	0	7
Scheduled - Colleges/Universities	20	1	5	16
Scheduled - Academies	309	111	7	413
Scheduled - Other	22	7	3	26
Transferee admission	127	61	46	142
Community admission	59	1	9	51
Total	**544**	**181**	**70**	**655**

It is notable that there has been a significant increase in the number of Academy conversions and Transferee admissions. Over the same period, a number of Transferee admissions have ceased which reflects the turnover of service contracts with these employers.

Membership profile and experience

5.3 The membership profile of the Main Fund has also developed since the 2016 valuation with an overall increase in members across all three categories. The Fund has continued to see a net increase in membership each quarter as more joiner notifications are received. A summary of the change in membership profile is detailed below:

Membership Category	31 March 2016	In	Out	30 September 2018
Active	107,984	31,724	19,360	120,348
Deferred	94,332	18,124	7,741	104,715
Pensioner	85,558	14,535	6,688	93,405
Total	**287,874**	**64,383**	**33,789**	**318,468**

Although the overall membership profile has continued to grow, we are also seeing an increase in early leavers and retirements. Longer term the membership profile is expected to mature as local government headcount reduces and more members reach retirement age.

5.4 The membership profile of the WMITA Fund has changed significantly since the 2016 valuation, with a large reduction in active members and deferred members and an increase in pensioner members. A summary of the change in membership profile is detailed below:

Membership Category	31 March 2016	30 September 2018	Percentage change
Active	744	331	-55.51%
Deferred	903	689	-23.70%
Pensioner	3,612	3,961	9.66%
Total	5,259	4,981	-5.29%

As the Fund is closed to new members and has been for some time, the membership profile is much more mature than the Main Fund and it will continue to mature at a faster rate. Differences in the maturity of the benefit payments due from the WMITA Fund and the employers backing these liabilities (private companies) are key drivers for the difference in the funding and investment strategies for this Fund.

5.5 As part of the actuarial valuation, member movements and experience (salary growth, leavers, retirements, deaths and take-up of options such as cash and 50:50) will be reviewed and the impact on the Fund liabilities assessed to inform the approach in 2019.

Investment returns and changes in financial conditions and outlook

5.6 Investment returns and financial conditions at and around the valuation date can have a material impact on the valuation outcomes and in particular, the required employer contribution rates until the next actuarial valuation. These will be reviewed for the 2019 actuarial valuation with the Fund Actuary and Investment advisers as part of the review of funding method and assumptions.

5.7 At the 2016 actuarial valuation, the invested assets of the Main Fund were valued at £11.6bn. Over the year 1 April 2016 to 31 March 2017 the Fund assets experienced unprecedented growth of over 22%. However, during the year 1 April 2017 to 31 March 2018 the return was much lower at 3%. The asset value for the Fund stood at £15.42bn at 31 March 2018. The outlook for future investment returns has also become more uncertain, and market volatility has increased as global political and economic uncertainty continues. The position will continue to be monitored in the run up to the valuation date and reflected as required in the Funding Strategy Statement.

5.8 At the 2016 actuarial valuation, the invested assets of the WMITA Fund were valued at £463.9m (£207.7m invested plus the value of the pensioner buy-in contract held by the Fund, which was valued at £256.2m) at the valuation date. By way of update, the total WMITA assets stood at £492m as at 31 March 2018.

Regulatory change

5.9 Change to the regulations, associated guidance and oversight of LGPS funding valuations are likely to impact on the funding strategy review and the approach adopted for the 2019 valuation.

- On 14 May 2018, LGPS Amendment Regulations were published. Amongst the changes was the introduction of “Exit Credits” for employers exiting with an existing surplus. This new legislation introduces a requirement for funds to pay any surplus to employers on exit from the LGPS. As a result of this new legislation, the Fund is, in conjunction with our advisers, reviewing its Funding Strategy Statement and Termination Policy, as well as the associated legal agreements, for instance admission agreements.

- On 6 September 2018, Her Majesty’s Treasury HMT) announced a move to quadrennial national valuations undertaken by the Government Actuary’s Department (GAD) for the LGPS. These valuations with fall in line with the four-year cycle applied to other public sector pensions, with the next valuation due 31 March 2020. As a result, it is anticipated that local valuations (undertaken by Administering Authorities and their local actuary) will move to a four-year cycle, although it remains unclear at this stage how this will be implemented in practice. For now, it has been confirmed the next valuation in the LGPS will remain effective 31 March 2019, with potential for contributions to be certified for a shorter or longer period until the next review, subject to transition arrangements.

- The Government Actuary Department (GAD) published on 27 September 2018 its first full report on LGPS valuations and the appropriateness of employer contributions (as required by section 13 of the Public Sector Pensions Act 2013). The approach taken within the review may impact on funding strategy considerations and contribution profiles discussed in 2019/20.

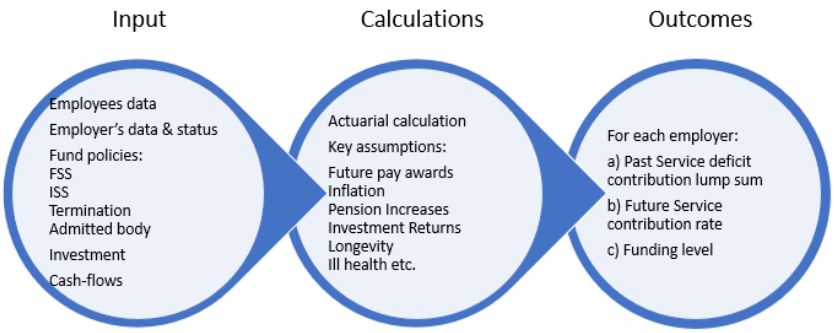
5.10 Within the GAD Section 13 report was a recommendation for the Administering Authority of the WMITA Fund to put a plan in place to ensure that the benefits of members in this Fund can continue to be paid in the event that employers’ contributions are insufficient to meet those liabilities. An update on action being taken in response to this recommendation is included within a separate report to the Board.

5.11 New CIPFA guidance is being developed on risk management within the LGPS, which will include a section on employer covenant. This, together with guidance on preparing the Funding Strategy Statement will be considered in the preparation for the 2019 review. In addition, further statutory guidance is expected to be issued by MHCLG on fund investments, following publication of the LGPS Investment Regulations 2016, which could impact on the investment strategy.

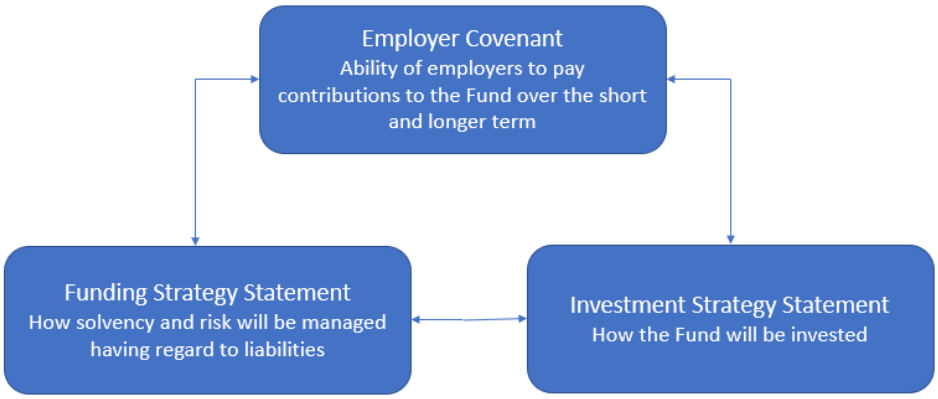
6.0 Preparatory work and planning

6.1 The process of engaging key employer groups commenced in September 2018, with a number of preliminary presentations and meetings already held in preparation for the 2019 actuarial valuation, including the recent Employer AGM on 13 November 2018.

6.2 The project outline in Appendix A summarises the key workstreams involved, emphasising the scope which is Fund-wide. Appendix B provides a high-level timetable for the 2019 valuation, including engagement with participating employers. The valuation process requires the collection of data and review of the relevant Fund policies. The Fund actuary uses this data and, based on a number of key assumptions, calculates the future benefit cashflows once for the future contribution rate for the Fund as a whole and then each employing body. This can be summarised as follows:



6.3 The process also links the valuation to the Fund's Funding Strategy Statement (FSS), employer covenant (solvency and risk) review and Investment Strategy Statement (ISS), with the balance of risk and mitigation of funding risks reflected in the review of these policy documents. The overview of the relationships is as follows:



6.4 The funding approach and assumptions will be fully reviewed and the FSS updated based on the advice of our Actuary, Graeme Muir from Barnett Waddingham. The investment strategy review will be completed alongside the funding review, to ensure the funding and investment strategies are joined-up.

7.0 Employer covenant review

7.1 The Fund has recently completed the review and procurement of its independent covenant advisors and is in the process of procuring a risk adviser and investment consultant to support the strategy, investment and contributions rate reviews which encompass the actuarial valuation.

7.2 The covenant review will form a key part of the engagement with employers prior to provisional results being released and in developing the covenant assessment and its link to establishing contribution rates for individual employers, with consideration of any measures taken to enhance covenant.

8.0 Consultation process

8.1 The Fund is required to consult with “such persons as it considers appropriate” on revision to the funding strategy.

8.2 The proposed consultation and key dates are outlined in appendix B.

9.0 Financial implications

9.1 The results of the 31 March 2019 actuarial valuation may have financial implications for participating employers in setting employer contribution rates, commencing April 2020, for the period to the next actuarial review.

10.0 Legal implications

10.1 In accordance with the LGPS Regulations, the Administering Authority of each LGPS pension fund must obtain an actuarial valuation as at 31 March 2019 and prepare and consult upon a Funding Strategy Statement (FSS) and Investment Strategy Statement (ISS).

11.0 Equalities implications

11.1 The report contains no direct equalities implications.

12.0 Environmental implications

12.1 The report contains no direct environmental implications.

13.0 Human resources implications

13.1 This report contains no direct human resources implications.

14.0 Corporate landlord implications

14.1 The report contains no direct corporate landlord implications.

15.0 Schedule of background papers

15.1 None.

16.0 Schedule of appendices

16.1 Appendix A: 2019 actuarial valuation project overview

16.2 Appendix B: High level 2019 valuation timetable