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20 September 2019
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To: All Members of the Avon Pension Fund Committee

Bath and North East Somerset Councillors: Bruce Shearn (Chair), Shaun Stephenson-McGall (Vice-Chair), Chris Dando, Paul May and Manda Rigby

Co-opted Voting Members: Councillor John Cato (North Somerset Council), Councillor Steve Pearce (Bristol City Council), Councillor Toby Savage (South Gloucestershire Council), William Liew (HFE Employers), Wendy Weston (Trade Unions), Pauline Gordon (Independent Member), John Finch (Independent Member) and Shirley Marsh (Independent Member)

Chief Executive and other appropriate officers
Press and Public

Dear Member

Avon Pension Fund Committee: Friday, 27th September, 2019

Please find attached a **SUPPLEMENTARY AGENDA DESPATCH** of late papers which were not available at the time the agenda was published. Please treat these papers as part of the agenda.

Papers have been included for the following items:

10. APPROVAL OF FSS (POST CONSULTATION) - TO FOLLOW (Pages 3 - 76)

Yours sincerely

Sean O'Neill
for Chief Executive

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Bath & North East Somerset Council		
MEETING:	AVON PENSION FUND COMMITTEE	
MEETING DATE:	27 SEPTEMBER 2019	AGENDA ITEM NUMBER
TITLE:	FUNDING STRATEGY STATEMENT 2019	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
List of attachments to this report: Appendix 1 – Funding Strategy Statement Appendix 2 – Comments from Employing Bodies Appendix 3 – Pension Board comments Appendix 4 – CIPFA guidance checklist		

1 THE ISSUE

- 1.1 The Local Government Pension Scheme (LGPS) regulations require each administering authority to prepare and publish a Funding Strategy Statement (FSS). The FSS sets out the key assumptions which the actuary has used in preparing the actuarial valuation and, in those cases where the Administering Authority has some discretion, the policies adopted by the Administering Authority. The Committee approved a draft FSS at its meeting on 21 June 2019 which has been circulated to the employing bodies for comment.
- 1.2 An updated draft FSS is attached as Appendix 1 which, after consideration by Fund Officers and the Actuary, takes into account the comments received from the employing bodies following the consultation period. The Actuary will attend the meeting to discuss the comments and any changes to the draft FSS.
- 1.3 As the body responsible for agreeing the Funding Strategy, the Committee must consider the FSS within the regulatory framework;
 - a) Ensure that the benefits paid out in the future will be reasonably met (the Solvency Objective)
 - b) That the amount paid in annually covers the current cost of the pension benefit accrued
 - c) That current pension debt is not deferred for future generations to fund (the Long Term Cost Efficiency Objective).
- 1.4 Given the FSS includes regulatory/legal matters that are yet to be resolved/confirmed, delegated authority is requested for Officers to finalise before 31/03/20 having taken advice from the Actuary.
- 1.5 Individual employer results will be disseminated in October and November. An Investment Forum to explain the outcome at the whole Fund level to employers will be arranged for 4Q19.

2 RECOMMENDATION

The Committee:

- 2.1 Notes the feedback responses received, and the proposed amendments to the FSS.**
- 2.2 Approves the FSS as set out in Appendix 1, subject to the insertion of information which can only be included when the actuarial valuation is complete.**
- 2.3 Delegates the refinement and finalisation of the draft FSS to Fund Officers, with assistance of Fund Actuary.**

3 FINANCIAL IMPLICATIONS

- 3.1 The actuarial costs for reviewing the FSS is included in the 2019 actuarial valuation fee and is provided for in the 2019/20 budget.

4 BACKGROUND

- 4.1 The LGPS regulations require each administering authority to prepare and publish a FSS. The key points of the regulation for the FSS are as follows:-
 - After consultation with all employing bodies, the administering authority must prepare and publish their funding strategy
 - In preparing the FSS, the administering authority must have regard to:
 - (i) FSS guidance issued by CIPFA
 - (ii) The Investment Strategy Statement (ISS) under Regulation 12 of the LGPS (Management and Investment of Funds) Regulations 2016
 - The FSS must be revised and published whenever there is a material change in either the policy on the matters set out in the FSS or the Statement of Investment Principles/ISS.
 - The Fund's actuary must have regard to the FSS as part of the valuation process.
- 4.2 The FSS sets out all the key assumptions which the actuary has used in preparing the actuarial valuation, together with the Administering Authority's policies in the areas where the Administering Authority has discretion to manage the funding position of the Fund.
- 4.3 Procedurally, the Fund's actuary cannot finalise the valuation until the FSS has been approved by the Committee.
- 4.4 There are significant outstanding regulatory /legal matters that will need to be included in the FSS as they will affect the contributions and /or funding policy (e.g. McCloud remedy and moving to 4 year valuation cycles). These may be resolved between now and 31 March 2020 when the FSS will be published. If not, how the Fund will manage such issues will need to be included in the FSS. As these are regulatory in nature, it is recommended that Officers are given delegated powers to finalise the FSS having received full advice from the Actuary.
- 4.5 Given the proposed changes to the regulations, it is reasonable to assume that the FSS will be reviewed before the next valuation in 2022. Any revisions will be brought to Committee for full consideration.

- 4.6 The draft FSS was circulated to the employing bodies with comments required by 22 August 2019. Those comments which have been received are summarised in Appendix 2.
- 4.7 The Pension Board have reviewed the draft FSS and conclude that it complies with the valuation. Their comments are in Appendix 3. In line with their recommendation, a checklist of compliance is provided in Appendix 4.
- 4.8 In light of some of the comments received via the consultation, some changes to the draft have been proposed. Details of the changes are set out in the next section.
- 4.9 The draft FSS for approval is attached as Appendix 1, estimates certain information that can only be confirmed once the valuation and associated analysis has been completed. Once the valuation is finalised, the FSS will be updated and published.

5 COMMENTS ON RESPONSES FROM EMPLOYING BODIES

- 5.1 The consultation asked specifically for comments about:
 - a) The appropriateness of the assumptions and in particular those that relate to them e.g. the pay increases you expect to award over the next few years?
 - b) In relation to the affordability of contributions and in particular whether there is any particular year over 2020/2023 which will be more challenging. This will help us form a view on any further flexibility required.
 - c) Whether the level of detail was sufficient and whether they need anything further in terms of information / meeting etc. to understand the content and implications
- 5.2 The responses are summarised by employer in Appendix 2. They highlight the severe funding pressures in the public sector that mean that increases in contributions would be difficult to fund resulting in services being cut. Specifically, the universities cited the Augar Report as creating uncertainty about future revenues, unitary authorities cited the fact that the Local Government Funding Review was only set for 1 year resulting in uncertainty about future funding streams and academies cited the September to September funding cycle, requiring flexibility. The main areas of comments on the contents of the FSS are summarised as follows:
 - a) Whether the margin for prudence in the assumptions are too high in relation to:
 - (i) The long term salary Increase assumption set at CPI plus 1.5% (a long term average of 3.9% p.a.) is too high given recent pay awards have been in line with inflation at best.
 - (ii) The lower asset out performance target used in the discount rate (from CPI+2.2% to CPI +1.75% for past service liabilities and from CPI +2.75% to CPI + 2.25% for future service).
 - (iii) Longevity improvements given that the rate of mortality had increased (i.e. more deaths than previously)
 - (iv) In relation to GAD Section 13 assumptions which uses a higher discount rate.
 - b) The deficit recovery period (DRP) should not automatically reduce by 3 years. The rationale for shortening the deficit recovery period was unclear. In addition, those employers with a DRP less than 12 years challenged whether it should reduce regardless of contribution levels versus the previous valuation.

- c) Disagreement that deficit contributions should be maintained at the expected monetary amounts from the preceding valuation.
- d) Employers in surplus should be allowed greater flexibility to accelerate the runoff over 12 years.
- e) McCloud could significantly affect employer contribution rates and employers requested clarification on the how it will be allowed for.

5.3 The Actuary has responded to the comments as follows:

- a) Margin for Prudence in assumptions:
 - (i) **An overall margin for prudence** is built into the actuarial assumptions in order to ensure the Fund can reasonably achieve the solvency and long term cost efficiency objectives set out in the FSS. Equally the margin for prudence allows the Fund Actuary to aim to keep contributions as 'constant as possible' at each valuation as it can be varied within reasonable bounds depending on a number of factors. Prudence is also required under the Regulations and guidance and is important for protecting the tax payers against adverse events e.g. market or economic downturn which could mean the Fund would not meet its primary objective to meet benefits as they fall due.
 - (ii) **Long term salary assumption** – the short term pay assumption reflects the immediate issue of current and near term pay awards which can be reasonably predicted in conjunction with the employers. For the last valuation this was generally set at 1% p.a. (or higher) from 2016 to 2020 for public sector employers based on the information available at that time. However this assumption has been breached by for most employers for the period from 2016 to 2019 resulting in an increase in liabilities. Based on the recent announcements regarding public sector pay for this valuation the short term award is to be set at a minimum of 2% p.a. for the 4 years to 2023 at the Fund level but at 2%, 2.5% or 3% at employers' request. This assumption includes an allowance for average incremental increases where applicable.

The long term award assumption reflects the expectation over the next few decades which is of course harder to predict with any certainty. However, it must be set to ensure it is reasonable (based on evidence) and also to meet the solvency and long term cost efficiency objective. It must also be considered in light of the short term award assumption. The long term award is set at CPI +1.5% p.a. as this takes into account annual increments, promotions and restructurings which on past evidence has caused salary growth to exceed CPI over time. For example the evidence from the scheme employers in the data from the shows that the average pay increase over the last two valuations (the period from 2013 to 2019) has been broadly CPI + 1.7% p.a. so it can be seen in times of austerity the combination of general pay awards and increments can be material.

- (iii) **The discount rate** reflects the expected real return over CPI generated by the investment strategy as this is what determines the long term cost of the LGPS as liabilities (benefits payments) predominately are linked to CPI inflation. Fundamentally the higher this return the lower the contributions required from employers will be in the long term. Given the point in the economic cycle and strong asset growth over the last 6 years, most investment managers and advisors are reducing their expectations for real

returns. Based on analysis, since 2016 valuation the median expected real return (i.e. that the strategy has a 50% chance of at least achieving this median return) for our strategy has fallen by 0.8% p.a. to CPI + 2.7%. Over the same period nominal gilt yields have fallen from 2.2% to 1.5%. Therefore, the investment return assumptions have been reduced to reflect the lower expected returns; however the full reduction has not been implemented resulting in a lower margin of prudence. The Fund has risk management strategies in place which support a less prudent margin in this assumption. The Actuary has recommended this reduction in the discount rate to take this into account and also so that the Fund reasonably meets its Solvency and Long Term Cost efficiency objectives. This will be reviewed from valuation to valuation taking account all relevant factors.

(iv) **Longevity assumption** – there are two drivers of the mortality assumptions, the actual mortality rate for the Fund (based on actual Fund experience over the last 13 years) and the expectations of future improvements in longevity. For the 2019 valuation the actuary has used the data from the Fund (and other LGPS Funds) and the latest CMI (Continuous Mortality Index) data gathered from a wide range of pension funds (including the LGPS) and insurance companies to reset the baseline mortality rate which reflects that the improvement in longevity is slowing. For example, the valuation assumes that a male aged 45 now will live to 89.6 compared to 91.3 in 2016 which shows the slowdown in the expected rate of improvement in life expectancy based on this new data. More detail is shown in the FSS.

(v) **Comparison the GAD discount rate.** GAD's SCAPE discount rate (currently CPI+2.4% but was CPI + 3% for the 2016 valuations so shows a fall as per the Actuary's recommendation for the valuation discount rate) is used to value the liabilities of the unfunded schemes (which are funded solely by tax receipts) and bears no relevance to the discount rate used for funded schemes. It reflects the OBR's assessment of long term real GDP growth which is currently around 2.2% above CPI. GAD uses this discount rate when it reviews the LGPS valuation outcomes merely to use a consistent discount rate for comparison only, irrespective of the investment strategy or the demographic characteristics of any individual LGPS Fund. This means that at each valuation the discount rate used by the Actuary could be higher or lower than this depending on the factors noted above.

b) **Automatic 3 year reduction in DRP with 12 year medium term target.** One of the requirements under the regulations is that the funding strategy addresses intergenerational fairness and does not unreasonably defer pension costs to future taxpayers (referred to as Long Term Cost Efficiency). Therefore, the target to get to a 100% solvency must be funded over a reasonable period of time. The reduction of 3 years is simply maintaining this timeframe at this valuation.

The FSS provides flexibility to manage DRP based on the covenant of the employer. Where there is a strong covenant and a reduction in the DRP by 3 years means the employer is paying less contributions overall compared to its current funding plan then the cash saving will accrue to the employer.

Where an employer has a DRP below 12 years, the DRP will be maintained if their covenant is sufficient to support the liabilities in the longer term. However, DRPs will not be extended, even if below 12 years, unless there are exceptional circumstances.

In both scenarios and employer will be able to use a shorter recovery period (increased contributions) e.g. where its participation in the Fund is of a fixed length

- c) **Maintaining monetary amounts of contributions from previous valuation.** The funding plan is designed to ensure that over time sufficient contributions are paid in and ideally kept as constant as possible. The principle is that total contributions should not reduce unless there is a genuine saving/improvement; the split between primary and secondary contributions can be altered. Therefore, if the improvement in the funding level means that the reduction in deficit contributions is larger than the increase in future service contributions, then the employer will generally pay less unless there is a concern over its covenant and maintaining the same contributions are affordable and does not detriment the employer covenant. This is to protect employers in the Fund.
- d) **The run off of surpluses should be accelerated.** Surpluses will generally be run off over 12 years, subject to a total employer contribution of zero, to provide as constant as possible contribution rates. A deficit (or material reduction in surplus) can arise within a short period due to adverse experience e.g. market downturn and a surplus acts as a potential buffer against this so; therefore the rate at which surpluses are run down is one element of managing this risk prudentially to achieve the Long Term Cost Efficiency objective. Taking this into account means that using the 12 years is a reasonable balance as it corresponds to the target for deficits to be recovered in the long term so is equitable. If the employer is expected to exit the Fund within a shorter timeframe, then a shorter run off plan can be agreed taking into account the potential termination position of the employer.
- e) **McCloud costs.** It is not anticipated that the final remedy will be known before the valuation is completed by 31 March 2020. The FSS has been amended to set out how any potential increase in costs will be dealt with in a reasonable manner as required by the guidance from MHCLG.

5.4 In light of the responses received, the proposed changes to the draft FSS are as follows:

- a) Greater clarity about achieving solvency and long term cost efficiency
- b) Clarified the reduction in DRP by 3 years, medium term target of 12 years and how this delivers long term cost efficiency.
- c) Made it explicit that if DRP is below 12 years it will be maintained.
- d) Clarified wording on how the McCloud liabilities will be calculated and that employers will have choice to either include in contribution rate or to make a provision and pay backdated contributions once the remedy is known
- e) Included explanation of the margin of prudence in the investment return assumption used in the discount rate.

6 PRELIMINARY WHOLE FUND RESULT

- 6.1 The final actuarial outcome will be reported to Committee at March 2020 meeting, however preliminary whole Fund results (based on the proposed assumptions to assess solvency and future service plus updated demographic assumptions) are set out below:

	£m
Assets	4,820
Liabilities	5,078
Deficit	258
Average Funding Level	95%
Average Employer future service contribution rate	17.1% p.a.

These results will be subject to change as the valuation is completed for each employer – in particular any changes in the assumption for short term pay award and the impact of the employers moving into the lower risk investment strategy. The impact of McCloud on employer contributions over 2020/23 will be considered with individual employers as per the policy set out in the FSS.

7 RISK MANAGEMENT

7.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. In addition it monitors the benefits administration, the risk register and compliance with relevant investment, finance and administration regulations. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

8 CLIMATE CHANGE

8.1 The Fund is implementing a digital strategy across all its operations and communications with stakeholders to reduce its internal carbon footprint. The Fund acknowledges the financial risk to its assets from climate change and is in the process of addressing this through its strategic asset allocation to Low Carbon Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee.

9 OTHER OPTIONS CONSIDERED

9.1 None.

10 CONSULTATION

10.1 The Council's Monitoring Officer and Section 151 Officer have had the opportunity to input to this report and have cleared it for publication.

Contact person	Liz Woodyard, Investments Manager 01225 395306
Background papers	CIPFA Pensions Panel (guidance on preparing FSS) Correspondence with actuary Responses to FSS from employing bodies
Please contact the report author if you need to access this report in an alternative format	

FUNDING STRATEGY STATEMENT

AVON PENSION FUND

[DATE]

BATH AND NORTH EAST SOMERSET COUNCIL

This Funding Strategy Statement has been prepared by Bath and North East Somerset Council (the Administering Authority) to set out the funding strategy for the Avon 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).

EXECUTIVE SUMMARY

Ensuring that the Avon Pension Fund (the “Fund”) has sufficient assets to meet its pension liabilities in the long-term is the fiduciary responsibility of the Administering Authority (**BATH AND NORTH EAST SOMERSET COUNCIL**). The Funding Strategy adopted by the Avon Pension Fund will therefore be critical in achieving this.

The purpose of this Funding Strategy Statement (“FSS”) is to set out a clear and transparent funding strategy that will identify how each Fund employer’s pension liabilities are to be met going forward.

The details contained in this Funding Strategy Statement will have a financial and operational impact on all participating employers in the Avon Pension Fund.

It is imperative therefore that each existing or potential employer is aware of the details contained in this statement.

Given this, and in accordance with governing legislation, all interested parties connected with the Avon Pension Fund have been consulted and given opportunity to comment prior to this Funding Strategy Statement being finalised and adopted. This statement takes into consideration all comments and feedback received.



MEETING THE FUND’S SOLVENCY OBJECTIVE

The Administering Authority’s long term objective is for the Fund to achieve a 100% solvency level over a reasonable time period. Contributions are set in relation to this objective which means that once 100% solvency is achieved, if assumptions are borne out in practice, there would be sufficient assets to pay all benefits earned up to the valuation date as they fall due. However, because financial and market conditions/outlook change between valuations, the assumptions used at one valuation may need to be amended at the next to meet the primary objectives. This in turn means that contributions will be subject to change from one valuation to another. This objective is considered on an employer specific level when setting individual contribution rates so each employer has the same fundamental objective in relation to their liabilities.

The general principle adopted by the Fund is that the assumptions used, taken as a whole, will be chosen sufficiently prudently for this objective to be reasonably achieved in the long term at each valuation.

The funding strategy set out in this document has been developed alongside the Fund’s investment strategy on an integrated basis taking into account the overall financial and demographic risks inherent in the Fund to meet the objective for all employers over different periods. The funding strategy includes appropriate margins to allow for the possibility of events (e.g. material reduction in investment returns, economic downturn and higher inflation outlook)

leading to a worsening of the funding position which would normally lead to volatility of contribution rates at future valuations if these margins were not included. This prudence is required by the Regulations and guidance issued by professional bodies and Government agencies to assist the Fund in meeting its primary solvency objective. The level of prudence has been quantified by the Actuary to provide protection against future adverse experience in the long term. Individual employer results will also have regard to their covenant strength and the investment strategy applied to the asset shares of those employers.



LONG TERM COST EFFICIENCY

Employer contributions are also set in order to achieve long term cost efficiency. Long-term cost-efficiency requires that any funding plan must provide equity between different generations of taxpayers. This means that the contributions must not be set at a level that is likely to give rise to additional costs in the future which fall on later generations of taxpayers or put too high a burden on current taxpayers. The funding parameters and assumptions e.g. deficit recovery period must have regard to this requirement which means a level of prudence is needed. Furthermore, the FSS must have regard to the desirability of maintaining as nearly constant a primary rate of contribution as possible.

When formulating the funding strategy, the Administering Authority has taken into account these key objectives and also considered the implications of the requirements under Section 13(4)(c) of the Public Service Pensions Act 2013. As part of these requirements the Government Actuary's Department (GAD) must, following an actuarial valuation, report on whether the rate of employer contributions to the Fund is set at an appropriate level to ensure the "solvency" of the pension fund and "long term cost efficiency" of the Scheme so far as it relates to the Fund.

DEFICIT RECOVERY PLAN AND CONTRIBUTIONS



As the solvency level of the Fund is [95]% at the valuation date i.e. the assets of the Fund are less than the liabilities, a deficit recovery plan needs to be implemented such that additional contributions are paid into the Fund to meet the shortfall.

Deficit contributions paid to the Fund by each employer will be expressed as cash amounts (flat or increasing year on year) and it is the Fund's objective that any funding deficit is eliminated as quickly as the participating employers can reasonably afford given other competing cost pressures. This may result in some flexibility in recovery periods by employer which would be at the sole discretion of the Administering Authority. The recovery periods will be set by the Fund, although employers will be free to select any shorter deficit recovery period if they wish. Employers may also elect to make prepayments of contributions which could result in a cash saving over the valuation certificate period.

The medium term objective is to recover any total Fund deficit over an average period of [12] years which in the long term provides equity between different generations of taxpayers whilst ensuring the deficit payments are eliminating a sufficient proportion of the capital element of the deficit, thereby reducing the interest cost. This will be periodically reviewed depending on the maturity profile of the Scheme. Subject to affordability considerations and individual circumstances, where a deficit exists and depending on the level of the deficit, a guiding principle will be to maintain the total contributions at the prescribed monetary levels from the preceding valuation (allowing for any indexation in these monetary payments over the recovery period). For those employers who are

recovering deficit over a shorter period than [12] years, then their recovery period will be expected to remain the same if their covenant is of sufficient strength to support the liabilities in the long term. However, where an employer is expected to exit the Fund, then in normal circumstances, the deficit would be recovered over the remaining period to exit. Full details are set out in this FSS.

The average recovery period for the Fund as a whole is [13] years at this valuation which is [3] years shorter than the average recovery period from the previous valuation. Subject to affordability and other considerations individual employer recovery periods would also be expected to reduce at this valuation.

Where there is a material increase in contributions required at this valuation, in certain circumstances the employer will be able to 'phase in' contributions over a period of [3] years in a pattern agreed with the Administering Authority and depending on the affordability of contributions as assessed in the covenant review of an employer. Equally employers will be able to align their contributions changes with their financial year if this does not end on 31 March.

The Government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. Therefore, the Fund has considered its policy in relation to costs that could emerge from the McCloud judgment in line with the guidance from the Scheme Advisory Board in conjunction with the Actuary. The judgment would have the effect of removing the current age criteria applied to the underpin implemented in 2014 for the LGPS. This underpin therefore would apply to all active members as at 1 April 2012. The relevant costs have been quantified and notified to employers. Employers will be able to choose to pay these estimated costs over 2020/23 in their certified contributions. Alternatively, they will need to make allowance within their budgets and backdated contributions would be payable once the remedy is known.



ACTUARIAL ASSUMPTIONS

The actuarial assumptions used for assessing the funding position of the Fund and the individual employers, the "Primary" contribution rate, and any contribution variations due to underlying surpluses or deficits (i.e. the "Secondary" rate) are set out in Appendix A to this FSS.

The discount rate in excess of CPI inflation (the "real discount rate") has been derived from the expected return on the Fund's assets based on the long term strategy set out in its Investment Strategy Statement (ISS). When assessing the appropriate prudent discount rate, consideration has been given to the level of expected asset returns in excess of CPI inflation (i.e. the rate at which the benefits in the LGPS generally increase each year).

The assumption for the long term expected future real returns has fallen since the last valuation. This is principally due to a combination of expectations for the returns on the Fund's assets and the level of inflation in the long term. Also, as the Fund has implemented a number of risk management strategies since the last valuation, the expected volatility of returns has fallen i.e. provides more certainty to outcomes. This is also taken into account by the Actuary when proposing the assumptions and at this valuation means that the level of prudence has been reduced. The assumption has therefore been adjusted so that in the Actuary's opinion, when allowing for the resultant employer contributions emerging from the valuation, the Fund can reasonably be expected to meet the Solvency and Long Term Cost Efficiency objectives.

Taking into account the above, the Fund Actuary is proposing that the long term real return over CPI inflation assumptions for determining the past service liabilities should be [1.75]% per annum and [2.25]% per annum for determining the future service (“primary”) contribution rate. This compares to 2.2% per annum and 2.75% per annum respectively at the last valuation.

The Fund has improved its “lower risk investment strategy” (previously described as the “corporate bond” strategy) that it offers to employers so that it is better matched to the risk profile of the employer’s liabilities. Existing “corporate bond” employers will be transitioned into the lower risk investment strategy with effect from 1 April 2019. This strategy exhibits a lower investment risk than the current whole fund strategy. If an employer is deemed to have a weaker covenant than others in the Fund, is planning to exit the Fund or would like to target a lower risk strategy, the Administering Authority has the discretion to move that employer (typically following discussions with the employer) into this investment strategy to protect the Fund as a whole. The current overall Fund investment strategy (as set out in the Investment Strategy Statement) will be known as the “higher risk investment strategy”.

The lower risk investment strategy is predominately linked to corporate bond investment assets that match the liabilities of the employers within it (as a minimum this will be reviewed following each actuarial valuation). In these circumstances, the discount rate is directly linked to yields on corporate bonds within the lower risk investment strategy. In addition, the strategy has exposure to the Liability Driven Investment (“LDI”) portfolio to provide protection against changes in market inflation expectations. The discount rate assumption used for employers’ liabilities who fall into this category is linked directly to the lower risk strategy assets.

Within the next valuation cycle, the Fund will consider the merits of implementing a medium risk investment strategy. This strategy will have a lower level of growth assets compared with the higher risk whole Fund strategy.

The demographic assumptions are based on the Fund Actuary’s bespoke analysis for the Fund taking into account the experience of the wider LGPS where relevant.

EMPLOYER ASSET SHARES



The Fund is a multi-employer pension scheme that is not formally unitised and so individual employer asset shares are calculated at each actuarial valuation. This means it is necessary to make some approximations in the timing of cashflows and allocation of investment returns when deriving the employer asset share.

At each review, cashflows into and out of the Fund relating to each employer, any movement of members between employers within the Fund, along with investment return earned on the asset share, are allowed for when calculating asset shares at each valuation. In addition, the asset shares maybe restated for changes in data or other policies.

Other adjustments are also made on account of the funding positions of orphan bodies which fall to be met by all other active employers in the Fund.



FUND POLICIES

In addition to the information/approaches required by overarching guidance and Regulation, this statement also summarises the Fund’s approach and policies in a

number of key areas:

1. Covenant assessment and monitoring

An employer's financial covenant underpins its legal obligation and crucially the ability to meet its financial responsibilities to the Fund now and in the future. The strength of covenant to the Fund effectively underwrites the risks to which the Fund is exposed, including underfunding, longevity, investment and market forces.

The strength of employer covenant can be subject to substantial variation over relatively short periods of time and, as such, regular monitoring and assessment is vital to the overall risk management and governance of the Fund. The employers' covenants will be assessed and monitored objectively in a proportionate manner and their ability to meet their obligations in the short and long term will be considered when determining an individual employer's funding strategy.

The Fund will continue to monitor changes in covenant in conjunction with the funding position over the inter-valuation period which will enable the Fund to anticipate and pre-empt any material issues arising and thus adopt a proactive approach in partnership with the employer. More details are provided in **Appendix F** in this statement.

2. Admitting employers to the Fund

Various types of employers are permitted to join the LGPS under certain circumstances, and the conditions upon which their entry to the Fund is based and the approach taken is set out in **Appendix B**. Examples of new employers include:

- Mandatory Scheme Employers - for example new academies (see later section)
- Designated bodies - those that are permitted to join if they pass a resolution
- Admission bodies - usually arising as a result of an outsourcing or an entity that provides some form of public service and their funding primarily derives from local or central government.
- [Employers may also join the Fund under the 'Deemed Employer' route. Further information on this is set out within **Appendix B**.]

[Drafting Note – This has been added following the consultation published by the MHCLG on 10 January 2019 (found here: <https://www.gov.uk/government/consultations/local-government-pension-scheme-fair-deal-strengthening-pension-protection>). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

The key objective for the Fund is to only admit employers where the risk to the Fund is mitigated as far as possible. The different employers pose different risks to the Fund and the risk management policy for existing and new employers applied is set out in **Appendix E**.

Certain employers may be required to provide a guarantee or alternative security before entry will be allowed.

3. New academy conversions and multi-academy trusts

Current Fund policy regarding the treatment of schools when converting to academy status is for the new academy to inherit the school's share of the historic local authority deficit prior to its conversion. This deficit is calculated as the capitalised deficit funding contributions (based on the

local authority deficit recovery period) the school would have made to the Fund had it not converted to academy status, subject to a minimum asset share of nil.

In cases where numerous academies which participate in the Fund are in the same Multi-Academy Trust, the Fund is willing to allow a combined funding position and average contribution requirements to apply. Notwithstanding this, the Fund will continue to track the constituent academies separately on an approximate basis, in the interests of transparency and clarity around entry and exit of individual academies to the Trust in future.

The full policy is shown in **Appendix D**.

4. Termination policy for employers exiting the Fund

When an employer ceases to participate within the Fund, it becomes an exiting employer under the Regulations. The Fund is then required to obtain an actuarial valuation of that employer's liabilities in respect of the benefits of the exiting employer's current and former employees along with a termination contribution certificate.

Where there is no guarantor who would subsume the liabilities of the exiting employer, the Fund's policy is that a discount rate linked to investment returns on the lower risk investment strategy and a more prudent longevity assumption is used for assessing liabilities on termination. Any exit payments due should be paid immediately although instalment plans will be considered by the Administering Authority on a case by case basis. Any exit credits (surplus assets over liabilities) will be paid from the Fund to the exiting employer within 3 months of completion of the cessation assessment by the Actuary. The Administering Authority will seek to modify this approach on a case by case basis if circumstances warrant it [for example it may work with the outsourcing scheme employer to adjust any exit payment or exit credit to take into account any risk sharing arrangements which exist between the exiting employer and the outsourcing scheme employer.].

Where there is a **guarantor** who would subsume the assets and liabilities of the outgoing employer, the policy is that any deficit or surplus would be subsumed into the guarantor and taken into account at the following valuation. This is subject to agreement from all interested parties who will need to consider any separate agreements that have been put in place between the exiting employer and the guarantor.

[An employer may continue to participate in the Fund with no contributing members and utilise the "Deferred Debt" Arrangements at the sole discretion of the Administering Authority which will be subject to a satisfactory covenant review on an ongoing basis. In this circumstance they will be treated as per any other participating employer in relation to overall funding strategy (including potentially requiring a final exit payment at some point) allowing for the covenant.]

[Drafting Note – This section has been adjusted following the consultation published by the MHCLG on 8 May 2019 (found here: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/800321/LGPS_valuation_cycle_reform_consultation.pdf). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

5. Insurance arrangements

The Fund has implemented an internal captive insurance arrangement in order to pool the risks associated with ill health retirement costs. The captive has been designed for employers that could be materially affected by the ill health retirement of one of their members. The captive

arrangement has been considered when setting the employer contribution rates for the eligible employers. More details are provided in **Appendix G**.

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APPENDICES

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1

INTRODUCTION

The Local Government Pension Scheme Regulations 2013 (“the 2013 Regulations”), the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 (“the 2014 Transitional Regulations”) and the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (all as amended) (collectively: “the Regulations”) provide the statutory framework from which the Administering Authority is required to prepare a Funding Strategy Statement (FSS). The key requirements for preparing the FSS can be summarised as follows:

- After consultation with all relevant interested parties involved with the Avon Pension Fund the Administering Authority will prepare and publish their Funding Strategy;
- In preparing the FSS, the Administering Authority must have regard to:
 - the guidance issued by CIPFA for this purpose; and
 - the Investment Strategy Statement (ISS) for the Scheme published under Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (as amended);
- The FSS must be revised and published whenever there is a material change in either the policy set out in the FSS or the ISS.

BENEFITS

The benefits provided by the Avon Pension Fund are specified in the governing legislation contained in the Regulations referred to above. Benefits payable under the Avon Pension Fund are guaranteed by statute and thereby the pensions promise is secure for members. The FSS addresses the issue of managing the need to fund those benefits over the long term, whilst at the same time facilitating scrutiny and accountability through improved transparency and disclosure.

The Fund is a defined benefit arrangement with principally final salary related benefits from contributing members up to 1 April 2014 and Career Averaged Revalued Earnings (“CARE”) benefits earned thereafter. There is also a “50:50 Scheme Option”, where members can elect to accrue 50% of the full scheme benefits in relation to the member only and pay 50% of the normal member contribution.

EMPLOYER CONTRIBUTIONS

The required levels of employee contributions are specified in the Regulations. Employer contributions are determined in accordance with the Regulations (which require that an actuarial valuation is completed every three years by the actuary, including a rates and adjustments certificate specifying the “primary” and “secondary” rate of the employer’s contribution).

PRIMARY RATE

The “Primary rate” for an employer is the contribution rate required to meet the cost of the future accrual of benefits including ancillary death in service and ill health benefits together with administration costs. It is expressed as a percentage of pensionable pay, ignoring any past service surplus or deficit, but allowing for any employer-specific circumstances, such as its membership

profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer's covenant.

The Primary rate for the whole fund is the weighted average (by payroll) of the individual employers' Primary rates.

SECONDARY RATE

The "Secondary rate" is an adjustment to the Primary rate to reflect any past service deficit or surplus, to arrive at the rate each employer is required to pay. The Secondary rate may be expressed as a percentage adjustment to the Primary rate, and/or a cash adjustment in each of the [three] years beginning 1 April in the year following that in which the valuation date falls.

The Secondary rate is specified in the rates and adjustments certificate.

For any employer, the rate they are actually required to pay is the sum of the Primary and Secondary rates.

Secondary rates for the whole fund in each of the [three years] shall also be disclosed. These will be calculated as the weighted average based on the whole fund payroll in respect of percentage adjustments and as a total amount in respect of cash adjustments.

2

PURPOSE OF FSS IN POLICY TERMS

Funding is the making of advance provision to meet the cost of accruing benefit promises. Decisions taken regarding the approach to funding will therefore determine the rate or pace at which this advance provision is made. Although the Regulations specify the fundamental principles on which funding contributions should be assessed, implementation of the funding strategy is the responsibility of the Administering Authority, acting on the professional advice provided by the actuary.

The Administering Authority's long term objective is for the Fund to achieve a 100% solvency level over a reasonable time period and then maintain sufficient assets in order for it to pay all benefits arising as they fall due.

The purpose of this Funding Strategy Statement is therefore:

- to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward by taking a prudent longer-term view of funding those liabilities;
- to establish contributions at a level to "secure the solvency of the pension fund" and the "long term cost efficiency",
- to have regard to the desirability of maintaining as nearly constant a primary rate of contribution as possible.

The intention is for this strategy to be both cohesive and comprehensive for the Fund as a whole, recognising that there will be conflicting objectives which need to be balanced and reconciled. Whilst the position of individual employers must be reflected in the statement, it must remain a single strategy for the Administering Authority to implement and maintain.

3

AIMS AND PURPOSE OF THE FUND

THE AIMS OF THE FUND ARE TO:

- manage employers' liabilities effectively and ensure that sufficient resources are available to meet all liabilities as they fall due
- enable employer contribution rates to be kept at a reasonable and affordable cost to the taxpayers, mandatory, resolution and admitted bodies, while achieving and maintaining fund solvency and long term cost efficiency, which should be assessed in light of the profile of the Fund now and in the future due to sector changes
- maximise the returns from investments within reasonable risk parameters taking into account the above aims.

THE PURPOSE OF THE FUND IS TO:

- receive monies in respect of contributions, transfer values and investment income, and
- pay out monies in respect of scheme benefits, transfer values, exit credits, costs, charges and expenses as defined in the Regulations.

4

RESPONSIBILITIES OF THE KEY PARTIES

The efficient and effective management of the pension fund can only be achieved if all parties exercise their statutory duties and responsibilities conscientiously and diligently. The key parties for the purposes of the FSS are the Administering Authority (in particular the Pensions Committee), the individual employers and the Fund Actuary and details of their roles are set out below. Other parties required to play their part in the fund management process are bankers, custodians, investment managers, auditors and legal, investment and governance advisors, along with the Local Pensions Board created under the Public Service Pensions Act 2013.

KEY PARTIES TO THE FSS

The **Administering Authority** should:

- operate the pension fund
- collect employer and employee contributions, investment income and other amounts due to the pension fund as stipulated in the Regulations
- pay from the pension fund the relevant entitlements as stipulated in the Regulations
- invest surplus monies in accordance the Regulations
- ensure that cash is available to meet liabilities as and when they fall due
- take measures as set out in the Regulations to safeguard the fund against the consequences of employer default
- manage the valuation process in consultation with the Fund's actuary
- prepare and maintain a FSS and an ISS, both after proper consultation with interested parties, and
- monitor all aspects of the Fund's performance and funding, amending the FSS/ISS as necessary
- effectively manage any potential conflicts of interest arising from its dual role as both fund administrator and a scheme employer, and
- establish, support and monitor a Local Pension Board (LPB) as required by the Public Service Pensions Act 2013, the Regulations and the Pensions Regulator's relevant Code of Practice.

The **Individual Employer** should:

- deduct contributions from employees' pay correctly after determining the appropriate employee contribution rate (in accordance with the Regulations)
- pay all contributions, including their own as determined by the actuary, promptly by the due date
- develop a policy on certain discretions and exercise those discretions as permitted within the regulatory framework
- make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain have regard to the Pensions

Regulator's focus on data quality and comply with any requirement set by the Administering Authority in this context

- notify the Administering Authority promptly of any changes to membership which may affect future funding.
- Understand the pensions impacts of any changes to their organisational structure and service delivery model.
- Understand that the quality of the data provided to the Fund will directly impact on the assessment of the liabilities and contributions. In particular, any deficiencies in the data would normally result in employer paying higher contributions than otherwise would be the case if the data was of high quality.

The **Fund Actuary** should:

- prepare valuations including the setting of employers' contribution rates at a level to ensure fund solvency after agreeing assumptions with the Administering Authority and having regard to their FSS and the Regulations
- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters such as pension strain costs, ill health retirement costs etc
- provide advice and valuations on the termination of admission agreements
- provide advice to the Administering Authority on bonds and other forms of security against the financial effect on the Fund of employer default
- assist the Administering Authority in assessing whether employer contributions need to be revised between valuations as required by the Regulations
- advise on funding strategy, the preparation of the FSS and the inter-relationship between the FSS and the ISS, and
- ensure the Administering Authority is aware of any professional guidance or other professional requirements which may be of relevance to the Fund Actuary's role in advising the Fund.

5

SOLVENCY FUNDING TARGET

Securing the “solvency” and “long term cost efficiency” is a regulatory requirement. To meet these requirements, the Administering Authority’s long term funding objective is for the Fund to achieve and then maintain sufficient assets to cover 100% of projected accrued liabilities (the “funding target”) assessed on an ongoing past service basis including allowance for projected final pay where appropriate. In the long term, the employer rate would ultimately revert to the Future Service or Primary Rate of contributions.

SOLVENCY AND LONG TERM EFFICIENCY

Each employer’s contributions are set at such a level to achieve full solvency in a reasonable timeframe. Solvency is defined as a level where the Fund’s liabilities i.e. benefit payments, can be reasonably met as they arise.

Employer contributions are also set in order to achieve long term cost efficiency. Long-term cost-efficiency implies that the rate must not be set at a level that is likely to give rise to additional costs in the future. 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 appropriate time.

When formulating the funding strategy, the Administering Authority has taken into account these key objectives and also considered the implications of the requirements under Section 13(4)(c) of the Public Service Pensions Act 2013. As part of these requirements the Government Actuary’s Department (GAD) must, following an actuarial valuation, report on whether the rate of employer contributions to the Fund is set at an appropriate level to ensure the “solvency” of the pension fund and “long term cost efficiency” of the Scheme so far as it relates to the Fund.

DETERMINATION OF THE SOLVENCY FUNDING TARGET AND DEFICIT RECOVERY PLAN

The principal method and assumptions to be used in the calculation of the funding target are set out in **Appendix A**.

Underlying these assumptions are the following two tenets:

- that the Fund is expected to continue for the foreseeable future; and
- favourable investment performance can play a valuable role in achieving adequate funding over the longer term.

This allows the Fund to take a longer term view when assessing the contribution requirements for certain employers.

In considering this the Administering Authority, based on the advice of the Actuary, will consider if this results in a reasonable likelihood that the funding plan will be successful potentially taking into account any changes in funding after the valuation date up to the finalisation of the valuation by 31 March 2020 at the latest.

As part of each valuation separate employer contribution rates are assessed by the Fund Actuary for each participating employer or group of employers. These rates are assessed taking into

account the experience and circumstances of each employer, following a principle of no cross-subsidy between the distinct employers in the Fund.

The Administering Authority, following consultation with the participating employers, has adopted the following objectives for setting the individual employer contribution rates arising from the 2019 actuarial valuation.

The employer contributions will be expressed and certified as two separate elements:

- the Primary rate: a percentage of pensionable payroll in respect of the cost of the future accrual of benefits and ancillary death in service and ill health benefits
- the Secondary rate: a schedule of % of pay adjustments or lump sum monetary amounts over 2020/23 in respect of an employer's surplus or deficit (including phasing adjustments)

DEFICIT RECOVERY PLAN

It is the Fund's objective that any funding deficit is eliminated as quickly as the participating employers can reasonably afford based on the Administering Authority's view of the employer's covenant and risk to the Fund.

Recovery periods will be set by the Fund on a consistent basis across employer categories where possible and communicated as part of the discussions with employers. This will determine the minimum contribution requirement and employers will be free to select any shorter deficit recovery period and higher contributions if they wish, including the option of prepaying the deficit contributions in one lump sum either on an annual basis or a one-off payment. This will be reflected in the monetary amount requested via a reduction in overall deficit contributions payable. The Administering Authority does retain ultimate discretion in applying these principles for individual employers on grounds of affordability and covenant strength.

The key principles when considering deficit recovery are as follows:

- Subject to consideration of affordability, as a general rule the deficit recovery period will reduce by at least 3 years for employers at this valuation when compared to the preceding valuation. This is to target full solvency over a similar (or shorter) time horizon. This is to maintain (as far as possible) equity between different generations of taxpayers and to protect the Fund against the potential for an unrecoverable deficit. The deficit recovery period will be set to at least cover the expected interest costs (actual interest costs will vary in line with investment performance) on the deficit.
- Employers will have the freedom to adopt a recovery plan on the basis of a shorter period if they so wish. Subject to affordability considerations and other factors a bespoke period may be applied in respect of particular employers where the Administering Authority considers this to be warranted). The average recovery period adopted by all employers will be set out within the Actuary's report. Employers will be notified of their individual deficit recovery period as part of the provision of their individual valuation results.
- A medium term recovery period target has been set at [12] years which in the long term provides equity between different generations of taxpayers whilst ensuring the deficit payments are eliminating a sufficient proportion of the capital element of the deficit, thereby reducing the interest cost. For those employers who are recovering deficit over a shorter period than [12] years, then their recovery period will be expected to remain the same if their covenant is of sufficient strength to support the liabilities in the long term. However, where an employer is

expected to exit the Fund then in normal circumstances, the deficit would be recovered over the remaining period to exit.

- For any employers assessed to be in surplus, their individual contribution requirements will be adjusted to such an extent that any surplus is used (i.e. run-off) over a [12] year period in line with the medium term recovery period target for the whole Fund, subject to a total employer contribution minimum of zero. If an employer is expected to exit the Fund before this period, contribution requirements will be set to target a nil termination deficit within reasonable expectations (subject to periodic review).
- Where increases (or decreases) in employer contributions are required from 1 April 2020, following completion of the 2019 actuarial valuation, the increase (or decrease) from the rates of contribution payable in the year 2020/21 may be implemented in steps depending on affordability of contributions as determined by the administering authority. This will be notified to employers as part of the valuation process.. However, where a surplus exists or where there has been a reduction in contributions paid in respect of an employer's deficit at the valuation, the Fund would not consider it appropriate for any increase in contributions paid in respect of future accrual of benefits to be implemented in steps.
- For employers that do not have a financial year end of 31 March 2020 (e.g. 31 July 2020), the Fund can, at the employers request before 28th February 2020 allow the employer to continue to pay their current contribution plan until their financial year end date. The new contribution plan would then be implemented after this date (i.e. 1 August 2020 if the year-end is 31 July 2020).
- As part of the process of agreeing funding plans with individual employers, the Administering Authority will consider the use of contingent assets and other tools such as bonds or guarantees that could assist employing bodies in managing the cost of their liabilities or could provide the Fund with greater security against outstanding liabilities.
- It is acknowledged by the Administering Authority that, whilst posing a relatively low risk to the Fund as a whole, a number of smaller employers may be faced with significant contribution increases that could seriously affect their ability to function in the future. The Administering Authority therefore would be willing to use its discretion to accept an evidence-based affordable level of contributions for the organisation for the three years 2020/2023. Any application of this option is at the ultimate discretion of the Fund officers and Section 151 officer in order to effectively manage risk across the Fund. It will only be considered after the provision of the appropriate evidence as part of the covenant assessment and also the appropriate professional advice.
- For those bodies identified as having a weaker covenant, the Administering Authority will need to balance the level of risk plus the solvency requirements of the Fund with the sustainability of the organisation when agreeing funding plans.
- Notwithstanding the above principles, the Administering Authority, in consultation with the actuary, has also had to consider whether any exceptional arrangements should apply in particular cases.

EMPLOYERS EXITING THE FUND

- Employers must notify the Fund as soon as they become aware of their planned exit date. Where appropriate, or at the request of the Scheme Employer, the Fund will review their certified contribution in order to target a fully funded position at exit. Consideration will be given to any cap and collar arrangements when reviewing contribution rates. The costs of the

contribution rate review will be payable by the employer or the outsourcing Scheme Employer (where necessary).

- On the cessation of an employer's participation in the Fund, in accordance with the Regulations, the Fund Actuary will be asked to make a termination assessment.

The policy for employers who have a guarantor participating in the Fund:

The residual assets and liabilities and hence any surplus or deficit will transfer back to the guarantor. This is subject to agreement from all interested parties who will need to consider any separate agreements that have been put in place between the exiting employer and the guarantor. If all parties do not agree, then the following arrangements will apply:

- In the case of a surplus, the Fund will pay this directly to the exiting employer within 3 months of completion of the cessation assessment by the Actuary (despite any other agreements that may be in place).
- In the case of a deficit, in order to maintain a consistent approach, the Fund will seek to recover this from the exiting employer in the first instance although if this is not possible then the deficit will be recovered from the guarantor either as a further contribution collection or at the next valuation.

In some instances, the outgoing employer may only be responsible for part of the residual deficit or surplus as per the separate risk sharing agreement and, if the parties are in agreement, the surplus would be retained by the Fund in favour of the outsourcing employer/guarantor. This would only occur if the Administering Authority is made aware of any such arrangement. [For the avoidance of doubt, where the outgoing employer is not responsible for any costs under a risk sharing agreement then no exit credit will be paid as per the Regulations, provided that the Fund is aware of the provisions of the risk sharing agreement. In the case of an employer participating under the deemed employer route this would be automatically applied.]

If a guarantor unjustifiably deviates from the Fund's policy (e.g. to subsume the residual assets, liabilities and any surplus or deficit of an exiting employer), any future termination events will, unless the situation is remedied, be treated in line with the approach adopted for employers without a guarantor in the Fund (e.g. the guarantor will be required to pay the termination deficit as a lump sum cash payment at the time of exit, any surplus would also be paid by the Fund to the guarantor at this point). The higher risk valuation funding basis will still be adopted in this case.

The policy for employers who do not have a guarantor participating in the Fund:

- In the case of a surplus, the Fund pays the exit credit to the exiting employer following completion of the termination process (within 3 months of completion of the cessation assessment by the Actuary).
- In the case of a deficit, the Fund would require the exiting employer to pay the termination deficit to the Fund as a lump sum cash payment (unless agreed otherwise by the Administering Authority at their sole discretion) following completion of the termination process.

Where an employer with no guarantor leaves the Fund and leaves liabilities with the Fund which the Fund must meet without recourse to that employer, the valuation of the termination payment will be calculated using a discount rate based on the lower risk investment strategy and a more prudent life expectancy assumption. Further details are set out in the Termination Policy in Appendix C.

The Administering Authority can vary the treatment on a case by case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary [and, for example, may adjust any exit payment or exit credit to take into account any risk sharing arrangements which exist between the exiting employer and other Fund employers].

[Subject to sufficient financial covenant and at the sole discretion of the Administering Authority an employer may continue to participate in the Fund with no contributing members under the Deferred Debt arrangement.]

The termination policy [(including Deferred Debt arrangements)] is set out in **Appendix C**.

[Drafting Note – This has been added following the consultation published by the MHCLG on 8 May 2019 (found here: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/800321/LGPS_valuation_cycle_reform_consultation.pdf). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

7

LINK TO INVESTMENT POLICY AND THE INVESTMENT STRATEGY STATEMENT (ISS)

The results of the 2019 valuation show the liabilities to be [xx]% covered by the current assets, with the funding deficit of [95]% being covered by future deficit contributions.

In assessing the value of the Fund's liabilities in the valuation, allowance has been made for growth asset out-performance as described below, taking into account the investment strategy adopted by the Fund, as set out in the ISS.

It is not possible to construct a portfolio of investments which produces a stream of income exactly matching the expected liability profile. However, it is possible to construct a portfolio which represents the "minimum risk" investment position which would deliver a very high certainty of real returns above assumed CPI inflation. Such a portfolio would consist of a mixture of long-term index-linked, fixed interest gilts and possible swaps.

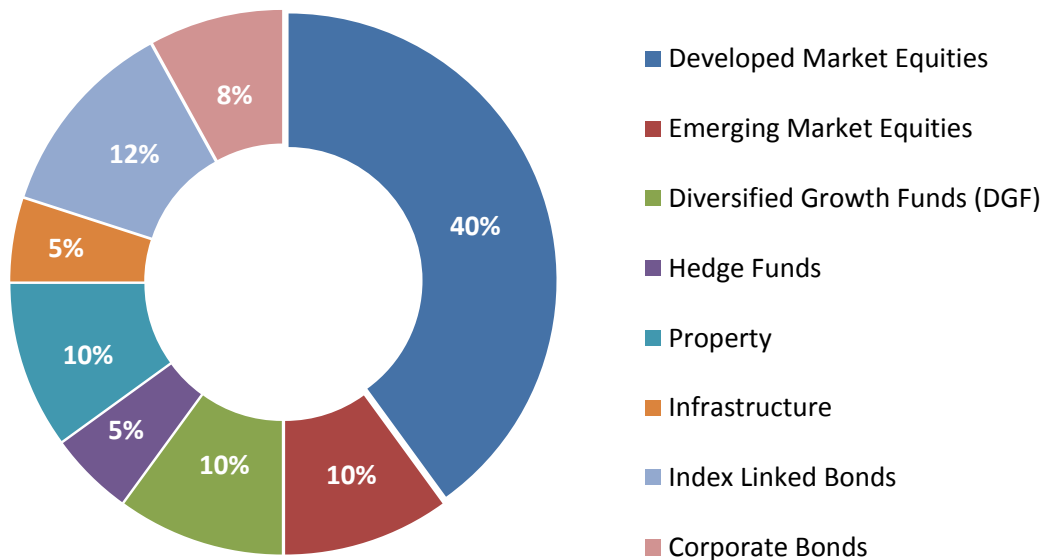
Investment of the Fund's assets in line with this portfolio would minimise fluctuations in the Fund's funding position between successive actuarial valuations.

If, at the valuation date, the Fund had been invested in this portfolio, then in carrying out this valuation it would not be appropriate to make any allowance for growth assets out-performance or any adjustment to market implied inflation assumption due to supply/demand distortions in the bond markets. This would result in real return versus CPI inflation of [x%] per annum at the valuation date. On this basis of assessment, the assessed value of the Fund's liabilities at the valuation would have been significantly higher, resulting in a funding level of [xx]%. This is a measure of the level of reliance on future investment returns i.e. level of investment risk being taken.

Departure from a minimum risk investment strategy, in particular to include growth assets such as equities, gives a better prospect that the assets will, over time, deliver returns in excess of CPI inflation and reduce the contribution requirements. The target solvency position of having sufficient assets to meet the Fund's pension obligations might in practice therefore be achieved by a range of combinations of funding plan, investment strategy and investment performance.

The overall strategic asset allocation is set out in the Investment Strategy Statement.

The current strategy is:



Based on the investment strategy above and the Actuary's assessment of the return expectations for each asset class, this leads to an overall best estimate average expected return of [2.7]% per annum in excess of CPI inflation as at the valuation date. For the purposes of setting funding strategy however, the Administering Authority believes that it is appropriate to take a margin for prudence on these return expectations. This margin however, has been reduced to take account of the risk management strategies implemented to reduce the volatility of returns within the investment strategy.

A measure of overall prudence to protect against adverse experience in the future is to consider the funding level if it was assessed on a "best estimate" basis for all the principal assumptions (mainly the investment return and life expectancy). The actuary has assessed this funding level as [tbc%]. This level of prudence is built in to allow the Fund to address adverse events whilst maintain stability (within reasonable parameters) in employer contributions where appropriate.

RISK MANAGEMENT STRATEGY

In the context of managing various aspects of the Fund's financial risks, the Administering Authority has implemented a number of risk management techniques. In particular:

- Equity Protection - the Fund has implemented protection against potential falls in the equity markets via the use of derivatives. The aim of the protection is to provide further stability (or even a reduction) in employer deficit contributions (all other things equal) in the event of a significant equity market fall (although it is recognised that it will not protect the Fund in totality).
- Liability Driven Investments (LDI) – the Fund has implemented an LDI strategy in order to hedge part of the Fund's assets against changes in liabilities for one or more employers.
- Lower risk investment strategy – the Fund updated its lower risk investment strategy (previously known as the “corporate bond” strategy) with effect from 1 April 2019. This strategy is predominately linked to corporate bond investment assets that match the liabilities of the employers within it.

The principal aim of these risk management techniques is to effectively look to provide more certainty of real investment returns vs CPI inflation and/or protect against volatility in the termination position. It is designed to reduce risk and provide more stability/certainty of outcome for funding and ultimately employer contribution rates. The effect of these techniques has been allowed for in the 2019 actuarial valuation calculations and could have implications on future actuarial valuations and the assumptions adopted. Further details of the framework have been included in the ISS.

HIGHER AND LOWER RISK INVESTMENT STRATEGY

The Fund has improved its **lower risk investment strategy** (previously described as the “corporate bond” strategy) that it offers to employers. Existing “corporate bond” employers will be transitioned into the lower risk investment strategy with effect from 1 April 2019. This strategy exhibits a lower investment risk than the current whole fund strategy. If an employer is deemed to have a weaker covenant than others in the Fund, is planning to exit the Fund or it would like to target a lower risk strategy, the Administering Authority has the discretion to move that employer (typically following discussions with the employer) into this investment strategy to protect the Fund as a whole. The current Fund investment strategy will be known as the “**higher risk investment strategy**”.

The lower risk investment strategy is predominately linked to corporate bond investment assets that match the liabilities of the employers within it (as a minimum this will be reviewed following each actuarial valuation). In these circumstances, the discount rate is directly linked to the yields on the corporate bonds within the lower risk investment strategy. In addition, the strategy has exposure to the Liability Driven Investment (“LDI”) portfolio to provide protection against changes in market inflation expectations. The implementation of this improved strategy will better match the overall changes in the liabilities included in the strategy. All other things equal, this would result in greater stability of the deficit and therefore contributions for employers.

Within the next valuation cycle, the Fund will consider the merits of implementing another alternative investment strategy where the risk sits between the higher and lower risk strategies. This strategy will have a lower level of growth assets compared with the higher risk whole Fund strategy.

The applicable investment strategy will be reflected in the relevant employer's notional asset share, funding basis and contribution requirements.

8

IDENTIFICATION OF RISKS AND COUNTER-MEASURES

The funding of defined benefits is by its nature uncertain. Funding of the Scheme is based on both financial and demographic assumptions. These assumptions are specified in the actuarial valuation report. When actual experience is not in line with the assumptions adopted a surplus or shortfall will emerge at the next actuarial assessment and will require a subsequent contribution adjustment to bring the funding back into line with the target.

The Administering Authority has been advised by the actuary that the greatest risk to the funding level is the investment risk inherent in the predominantly equity based strategy, so that actual asset out-performance between successive valuations could diverge significantly from that assumed in the long term. The Actuary's formal valuation report includes a quantification of the key risks in terms of the effect on the funding position.

FINANCIAL

The financial risks are as follows:-

- Investment markets fail to perform in line with expectations
- Protection and risk management policies fail to perform in line with expectations
- Market outlook moves at variance with assumptions
- Investment Fund Managers fail to achieve performance targets over the longer term
- Asset re-allocations in volatile markets may lock in past losses
- Pay and price inflation significantly more or less than anticipated
- Future underperformance arising as a result of participating in the larger asset pooling vehicle
- An employer ceasing to exist without prior notification, resulting in a large exit credit requirement from the Fund impacting on cashflow requirements.

Any increase in employer contribution rates (as a result of these risks) may in turn impact on the service delivery of that employer and their financial position.

In practice the extent to which these risks can be reduced is limited. However, the Fund's asset allocation is kept under constant review and the performance of the investment managers is regularly monitored. In addition, the implementation of the risk management framework will help to reduce the key financial risks over time.

DEMOGRAPHIC

The demographic risks are as follows:-

- Future changes in life expectancy (longevity) that cannot be predicted with any certainty
- Potential strains from ill health retirements, over and above what is allowed for in the valuation assumptions for employers
- Unanticipated acceleration of the maturing of the Fund resulting in materially negative cashflows and shortening of liability durations

Increasing longevity is something which government policies, both national and local, are designed to promote. It does, however, result in a greater liability for pension funds.

Ill health retirements can be costly for employers, particularly small employers where one or two costly ill health retirements can take them well above the “average” implied by the valuation assumptions. Increasingly we are seeing employers mitigate the number of ill health retirements by employing HR / occupational health preventative measures. These in conjunction with ensuring the regulatory procedures in place to ensure that ill-health retirements are properly controlled, can help control exposure to this demographic risk. The Fund’s ill health captive arrangement will also help to ensure that the eligible employers are not exposed to large deficits due to the ill health retirement of one or more of their members (see further information in **Appendix G**).

Apart from the regulatory procedures in place to ensure that ill-health retirements are properly controlled, **employing bodies should be doing everything in their power to minimise the number of ill-health retirements.**

Early retirements for reasons of redundancy and efficiency do not immediately affect the solvency of the Fund because they are the subject of a direct charge.

With regards to increasing maturity (e.g. due to further cuts in workforce and/or restrictions on new employees accessing the Fund), the Administering Authority regularly monitors the position in terms of cashflow requirements and considers the impact on the investment strategy.

INSURANCE OF CERTAIN BENEFITS

The contributions for any employer may be varied as agreed by the Actuary and Administering Authority to reflect any changes in contribution requirements as a result of any benefit costs being insured with a third party or internally within the Fund. More detail on how the Fund is implementing the captive insurance for ill health costs is set out in **Appendix G**.

REGULATORY

The key regulatory risks are as follows:-

- Changes to Regulations, e.g. changes to the benefits package, retirement age, potential new entrants to scheme,
- Changes to national pension requirements and/or HMRC Rules
- Political risk that the guarantee from the Department for Education for academies is removed or modified along with the operational risks as a consequence of the potential for a large increase in the number of academies in the Fund due to Government policy.

Membership of the Local Government Pension Scheme is open to all local government staff and should be encouraged as a valuable part of the contract of employment. However, increasing membership does result in higher employer monetary costs.

GOVERNANCE

The Fund has done as much as it believes it reasonably can to enable employing bodies and scheme members (via their trades unions) to make their views known to the Fund and to participate in the decision-making process. So far as the revised Funding Strategy Statement is concerned, the Administering Authority circulated copies of the first draft to all employing bodies for their comments and placed a copy on the Fund’s website. The first draft was approved at the Committee’s meeting on 21st June 2019 and finalised on 27th September 2019 after the Fund received feedback from the employing bodies.

Governance risks are as follows:-

- The quality of membership data deteriorates materially due to breakdown in processes for updating the information resulting in liabilities being under or overstated
- Administering Authority unaware of structural changes in employer's membership (e.g. large fall in employee numbers, large number of retirements) with the result that contribution rates are set at too low a level
- Administering Authority not advised of an employer closing to new entrants, something which would normally require an increase in contribution rates
- An employer ceasing to exist with insufficient funding or a bond which is not adequate.

For these risks to be minimised much depends on information being supplied to the Administering Authority by the employing bodies. Arrangements are strictly controlled and monitored (e.g. the implementation of iConnect for transferring data from employers), but in most cases the employer, rather than the Fund as a whole, bears the risk.

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MONITORING AND REVIEW

The Administering Authority has taken advice from the actuary in preparing this Statement.

A full review of this Statement will occur no less frequently than every [4] years, to coincide with completion of a full statutory actuarial valuation and every review of employer rates or interim valuation. Any review will take account of the current economic conditions and will also reflect any legislative changes.

The Administering Authority will monitor the progress of the funding strategy between full actuarial valuations. If considered appropriate, the funding strategy will be reviewed (other than as part of the valuation process), for example, if there:

- has been a significant change in market conditions, and/or deviation in the progress of the funding strategy
- have been significant changes to the Scheme membership, or LGPS benefits
- have been changes to the circumstances of any of the employing authorities to such an extent that they impact on or warrant a change in the funding strategy
- have been any significant special contributions paid into the Fund.

When monitoring the funding strategy, if the Administering Authority considers that any action is required, the relevant employers will be contacted. In the case of an employer who may exit the Fund, there is statutory provision for rates to be amended between valuations but it is unlikely that this power will be invoked other than in exceptional circumstances.

REVIEW OF CONTRIBUTIONS

In line with the Regulations, the Administering Authority has the ability to review employer contributions or request a full interim valuation. If considered appropriate, the Fund will carry out an interim valuation or a review of contributions for a specific employer or employer(s), if there:

1. has been a significant change in market conditions so that the funding level has changed by [more than 10% over a period of [y] months / the whole Fund funding level drops below 90%],
2. has been a material change in an employer's covenant assessed in line with the policy in Appendix F.
3. the employer has notified the Fund of their intention to exit within the next [x] years. Employers must notify the Fund as soon as they become aware of their planned exit date.
4. has been a deviation in the progress of the funding strategy for the employer.
5. have been significant changes to the Scheme membership, or LGPS benefits.
6. has been a change in employer status.
7. have been any significant special contributions paid into the Fund.
8. have been significant statutory or regulatory changes.

In the normal course of events, contributions will only be reviewed for statutory or tax raising employers as part of a full actuarial valuation (statutory or interim valuation).

Consideration will be given to any cap and covenant arrangements when reviewing contribution rates.

In exceptional circumstances, not envisaged in the Funding Strategy Statement, the Fund can apply for a direction from the Secretary of State to carry out an interim valuation. The Secretary of State would also have a power to require interim valuations of the Fund either on representation from funds, scheme employers or of his own motion.

Where the contribution review is triggered by an employer request (e.g. points 2, 3, 4, 5, 6 and 7 above), the costs associated with the review will be included in the assessment of the contributions if deemed appropriate.

[Drafting Note – This has been added following the consultation published by the MHCLG on 8 May 2019 (found [here](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/800321/LGPS_valuation_cycle_reform_consultation.pdf): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/800321/LGPS_valuation_cycle_reform_consultation.pdf). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

THE M^CCLOUD JUDGMENT

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.

As part of this, it was agreed that employers should bear the costs/risks of external factors such as the discount rate, investment returns and inflation changes, whereas employees should bear the costs/risks of other factors such as wage growth, life expectancy changes, ill health retirement experience and commutation of pension.

The outcomes of the cost management process were expected to be implemented from 1 April 2019, based on data from the 2016 valuations for the LGPS. This has now been put on hold due to 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 Schemes).

The Government have confirmed that this judgment will result in a remedy being required for the LGPS. The Scheme Advisory Board issued guidance [here](#) which sets out how the McCloud case should be allowed for within the 2019 valuation. As a consequence, cost management is expected to remain paused until the remedy is known and therefore no allowance has been made in this valuation. This will be reconsidered once the final outcomes are known.

The potential impact of the McCloud judgment (based on the information available at the time) has been quantified and communicated to employers as part of the 2019 valuation. This has been assessed by removing the current age criteria applied to the underpin implemented in 2014 for the LGPS. This underpin therefore would apply to all active members as at 1 April 2012. Employers will be able to choose to pay these estimated costs over 2020/23 in their certified contributions. Alternatively, they will need to make provision within their budgets and backdated contributions would be paid once the remedy is known. The mechanism to achieve this has been set out in the Actuary's certificate.

APPENDIX A - ACTUARIAL METHOD AND ASSUMPTIONS

METHOD

The actuarial method to be used in the calculation of the solvency funding target is the Projected Unit method, under which the salary increases assumed for each member are projected until that member is assumed to leave active service by death, retirement or withdrawal from service. This method implicitly allows for new entrants to the scheme on the basis that the overall age profile of the active membership will remain stable. As a result, for those employers which are closed to new entrants, an alternative method is adopted, which makes advance allowance for the anticipated future ageing and decline of the current closed membership group potentially over the period of the rates and adjustments certificate.

FINANCIAL ASSUMPTIONS – SOLVENCY FUNDING TARGET

Investment return (discount rate)

The discount rate for the higher risk valuation funding basis has been derived from the expected return on the Fund assets based on the long term strategy set out in the Investment Strategy Statement (ISS). It includes appropriate margins for prudence. When assessing the appropriate discount rate consideration has been given to the returns in excess of CPI inflation (as derived below). The discount rate at the valuation has been derived based on an assumed return of [1.75]% per annum above CPI inflation i.e. a real return of [1.75]% per annum and a total discount rate of [4.15]% per annum. This real return will be reviewed from time to time based on the investment strategy, market outlook and the Fund's overall risk metrics. The discount rate will be reviewed as a matter of course at the time of a formal valuation.

For those employers who are funding on a lower risk funding basis, the discount rate used will be linked directly to the yields available for the assets within the lower risk investment strategy. The typical discount rate used at the valuation date is [2.60]% per annum.

Inflation (Consumer Prices Index)

The inflation assumption will be taken to be the investment market's expectation for RPI inflation as indicated by the difference between yields derived from market instruments, principally conventional and index-linked UK Government gilts as at the valuation date, reflecting the profile and duration of the Scheme's accrued liabilities, but subject to an adjustment due to retirement pensions being increased annually by the change in the Consumer Price Index rather than the Retail Price Index.

The overall average reduction to the assumption to long term RPI inflation to arrive at the CPI inflation assumption at the valuation date is [1.00]% per annum. The CPI inflation assumption at the valuation date is 2.40% per annum.

Salary increases

In relation to benefits earned prior to 1 April 2014, the assumption for real salary increases (salary increases in excess of price inflation) will be determined by an allowance of [1.50]% p.a. over the inflation assumption as described above. This includes allowance for promotional increases. In addition to the long term salary increase assumption allowance has been made for expected short

term pay restraint for some employers as budgeted in their financial plan. Depending on the circumstances of the employer, the variants on short term pay that have been applied are either no allowance or allowances based on evidence from the employer of [2]%, [2.5]% or [3]% per annum for each year from the valuation date up to 31 March 2023. The allowance made has been notified to each employer separately on their individual results schedule.

Application of bespoke salary increase assumptions as put forward by individual employers will be at the ultimate discretion of the Administering Authority but as a minimum must be reasonable and practical. To the extent that experience differs to the assumption adopted, the effects will emerge at the next actuarial valuation.

Pension Increases/Indexation of CARE benefits

Increases to pensions are assumed to be in line with the inflation (CPI) assumption described above. This is modified appropriately to reflect any benefits which are not fully indexed in line with the CPI (e.g. Guaranteed Minimum Pensions where the LGPS is not required to provide full indexation). For members in pensionable employment, their CARE benefits are also indexed by CPI although this can be less than zero i.e. a reduction in benefits, whereas for pension increases this cannot be negative, as pensions cannot be reduced.

DEMOGRAPHIC ASSUMPTIONS

Mortality/Life Expectancy

The mortality in retirement assumptions will be based on the most up-to-date information in relation to self-administered pension schemes published by the Continuous Mortality Investigation (CMI), making allowance for future improvements in longevity and the experience of the scheme. The mortality base tables used are set out below, with a loading reflecting Fund specific experience. The derivation of the mortality assumption is set out in a separate advice as supplied by the Actuary. A specific mortality assumption has also been adopted for current members who retire on the grounds of ill health. For all members, it is assumed that the trend in longevity seen over recent time periods (as evidenced in the 2018 CMI analysis) will continue in the longer term and as such, the assumptions build in a level of longevity 'improvement' year on year in the future in line with the CMI 2018 projections and a long term improvement trend of 1.75% per annum.

As an indication of impact, we have set out the life expectancies at age 65 based on the 2016 and 2019 assumptions:

	Male Life Expectancy at 65		Female Life Expectancy at 65	
	2016	2019	2016	2019
Pensioners	23.7	23.1	26.2	25.7
Actives aged 45 now	26.3	24.6	29.0	27.6
Deferreds aged 45 now	24.2	23.2	27.8	26.4

For example, a male pensioner, currently aged 65, would be expected to live to age 88.1. Whereas a male active member aged 45 would be expected to live until age 89.6. This is a reflection of the expected improvement in life expectancy over the next 20 years in the assumptions above.

The mortality before retirement has also been reviewed based on LGPS wide experience.

Commutation

It has been assumed that, on average, [50]% of retiring members will take the maximum tax-free cash available at retirement and [50]% will take the standard 3/80ths cash sum. The option which members have to commute part of their pension at retirement in return for a lump sum is a rate of £12 cash for each £1 p.a. of pension given up.

[Drafting note: This assumption will be considered in more detail once the full data has been analysed. It may therefore change although any impact is unlikely to be significant.]

Other Demographics

Following an analysis of Fund experience carried out by the Actuary, the incidence of ill health retirements, withdrawal rates and the proportions married/civil partnership assumption remain in line with the assumptions adopted for the last valuation. In addition, no allowance will be made for the future take-up of the 50:50 option. Where any member has actually opted for the 50:50 scheme, this will be allowed for in the assessment of the rate for the next 3 years. Other assumptions are as per the last valuation.

Expenses

Expenses are met out of the Fund, in accordance with the Regulations. This is allowed for by adding [0.6]% of pensionable pay to the contributions as required from participating employers. This addition is reassessed at each valuation. Investment expenses have been allowed for implicitly in determining the discount rates.

Discretionary Benefits

The costs of any discretion exercised by an employer in order to enhance benefits for a member through the Fund will be subject to additional contributions from the employer as required by the Regulations as and when the event occurs. As a result, no allowance for such discretionary benefits has been made in the valuation

METHOD AND ASSUMPTIONS USED IN CALCULATING THE COST OF FUTURE ACCRUAL (OR PRIMARY RATE)

The future service liabilities are calculated using the same assumptions as the funding target except that a different financial assumption for the discount rate is used. A critical aspect here is that the Regulations state the desirability of keeping the “Primary rate” (which is the future service rate) as stable as possible so this needs to be taken into account when setting the assumptions.

As future service contributions are paid in respect of benefits built up in the future, the Primary rate should take account of the market conditions applying at future dates, not just the date of the valuation, thus it is justifiable to use a slightly higher expected return from the investment strategy. In addition, the future liabilities for which these contributions will be paid have a longer average duration than the past service liabilities as they relate to active members only.

The financial assumptions in relation to future service (i.e. the Primary rate) are based on an overall assumed real discount rate of [2.25]% per annum above the long term average assumption for consumer price inflation of 2.40% per annum. This leads to a discount rate of [4.65]% per annum.

EMPLOYER ASSET SHARES

The Fund is a multi-employer pension scheme that is not formally unitised and so individual employer asset shares are calculated at each actuarial valuation. This means it is necessary to

make some approximations in the timing of cashflows and allocation of investment returns when deriving the employer asset share.

In attributing the overall investment performance obtained on the assets of the Fund to each employer a pro-rata principle is adopted. This approach is effectively one of applying a notional individual employer investment strategy identical to that adopted for the Scheme as a whole unless agreed otherwise between the employer and the Fund at the sole discretion of the Administering Authority.

At each review, cashflows into and out of the Fund relating to each employer, any movement of members between employers within the Fund, along with investment return earned on the asset share, are allowed for when calculating asset shares at each valuation.

Other adjustments are also made on account of the funding positions of orphan bodies which fall to be met by all other active employers in the Fund.

SUMMARY OF KEY WHOLE FUND ASSUMPTIONS USED FOR CALCULATING FUNDING TARGET AND COST OF FUTURE ACCRUAL (THE “PRIMARY RATE”) FOR THE 2019 ACTUARIAL VALUATION

Long-term yields		
	Market implied RPI inflation	[3.40]% p.a.
Solvency Funding Target financial assumptions		
	Investment return/Discount Rate	[4.15]% p.a.
	CPI price inflation	[2.40]% p.a.
	Short Term Salary Increases	Varies by employer - 4 year period to 31 March 2023 as noted above
	Long Term Salary increases	[3.90]% p.a.
	Pension increases/indexation of CARE benefits	[2.40]% p.a.
Future service accrual financial assumptions		
	Investment return/Discount Rate	[4.65]% p.a.
	CPI price inflation	[2.40]% p.a.
	Short Term Salary Increases	Varies by employer - 4 year period to 31 March 2023 as noted above
	Long Term Salary increases	[3.90]% p.a.
	Pension increases/indexation of CARE benefits	[2.40]% p.a.

Life expectancy assumptions

The post retirement mortality tables adopted for this valuation are set out below:

Current Status	Retirement Type	Mortality Table
Annuitant	Normal Health	92% S3PMA_CMI_2018 [1.75%] 87% S3PFA_M_CMI_2018 [1.75%]
	Dependant	119% S3PMA_CMI_2018 [1.75%] 87% S3DFA_CMI_2018 [1.75%]
	Ill Health	113% S2IMA_CMI_2018 [1.75%] 127% S2IFA_CMI_2018 [1.75%]
	Future Dependant	117% S3PMA_CMI_2018 [1.75%] 106% S3DFA_CMI_2018 [1.75%]
Active	Normal Health	98% S3PMA_CMI_2018 [1.75%] 88% S3PFA_M_CMI_2018 [1.75%]
	Ill Health	115% S2IMA_CMI_2018 [1.75%] 138% S2IFA_CMI_2018 [1.75%]
Deferred	All	118% S3PMA_CMI_2018 [1.75%] 105% S3PFA_M_CMI_2018 [1.75%]
Future Dependant	Dependant	124% S3PMA_CMI_2018 [1.75%] 113% S3DFA_CMI_2018 [1.75%]

Other demographic assumptions are set out in the Actuary's formal report.

APPENDIX B - ADMISSION POLICY

ENTRY TO THE FUND

MANDATORY SCHEME EMPLOYERS

Certain employing bodies are required to join the scheme under the Regulations. These bodies include tax raising bodies, those funded by central government (academies and colleges) and universities (reliant on non-government income). Academies also fall under this category.

DESIGNATING BODIES

Designating bodies are permitted to join the scheme if they pass a resolution to this effect. Designating bodies including connected entities are not required under the Regulations to provide a guarantee. These bodies usually have tax raising powers.

ADMISSION BODIES

An admitted body is an employer which, if it satisfies certain regulatory criteria, can apply to participate in the Fund. If its application is accepted by the administering authority, it will then have an “admission agreement”. In accordance with the Regulations, the admission agreement sets out the conditions of participation of the admitted body including which employees (or categories of employees) are eligible to be members of the Fund.

Admitted bodies can join the Fund if

1. They provide a service for a scheme employer as a result of an outsourcing (formerly known as Transferee Admission Bodies)
2. They provide some form of public service and their funding in most cases derives primarily from local or central government. In reality they take many different forms but the one common element is that they are “not for profit” organisations (formerly known as Community Admission Bodies).

Admitted bodies may only join the Fund if they are guaranteed by a scheme employer. When the agreement or service provision ceases, the Fund’s policy is that the assets and liabilities of the admission body will in all cases revert to the outsourcing scheme employer or guaranteeing employer. If the outsourcing scheme employer or guaranteeing employer wishes to recover any deficit from the admission body, it is a matter between themselves and the admission body. The Fund will require appropriate instruction from the guarantor regarding any outstanding deficit to be recovered from the outgoing body.

Where an admission agreement involves multiple guarantors (typically under 2 above), who may not all be employers in the Fund, it may not be practical for any deficit on closure to be transferred to another employer in the Fund. Where this is the case, the lower risk funding basis would apply for valuing the liabilities from the outset.

[JOINING THE FUND VIA THE ‘DEEMED EMPLOYER’ ROUTE

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.

It will be the outsourcing Scheme Employer's choice, when initially putting the contract out to tender, whether the Admission Agreement or Deemed Employer approach will be used. The outsourcing scheme employer will be also known as the deemed employer with regard to this admitted body.

If the Deemed Employer route is chosen, the admitted body will not join the Fund and will instead be grouped / pooled with the original scheme employer. This may be used when a pass through arrangement has been agreed.

The Fund's policy will be dependent on the deemed employer's policy and approach to dealing with these outsourcings. This makes it imperative that each outsourcing scheme employer has a clear policy on the treatment of each type of admitted body. The Fund also requires an agreement (similar to the admission agreement) with the admitted body to ensure their duties are fulfilled e.g. payment of contributions.]

[Drafting Note – This has been added following the consultation published by the MHCLG on 10 January 2019 (found here: <https://www.gov.uk/government/consultations/local-government-pension-scheme-fair-deal-strengthening-pension-protection>). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

CONNECTED ENTITIES

Connected entities by definition have close ties to a scheme employer given that a connected entity is included in the financial statements of the scheme employer.

Although connected entities are “Designating Bodies” under the Regulations, they have similar characteristics to admitted bodies (in that there is an “outsourcing employer”). However, the Regulations do not strictly require such bodies to have a guarantee from a scheme employer.

To limit the risk to the Fund, the lower risk funding basis for calculating the liabilities will apply to all new connected entities. In the event that a scheme employer provides a guarantee for their connected entity, the higher risk valuation funding basis will be applied to value the liabilities.

CHILDREN'S CENTRE TRANSFER TO ACADEMY TRUSTS

Local education authorities have an obligation to provide Children's Centres under the Childcare Act 2006. The Act places duties on these authorities in relation to establishing and running Children's Centres and therefore the financial obligation to cover the LGPS costs of eligible staff remains a responsibility of the local education authority regardless of service delivery vehicle. The local education authority is liable for all the LGPS liabilities of the Children's Centre.

As the staff cannot be employed directly by an Academy or Academy Trust, the Fund will permit admission of a separate participating employer (with its own contribution rate requirements based on the transferring staff), through a tri-partite admission agreement between the Fund, the Local Education Authority of the ceding Council and the body responsible for managing the Children's Centre (this could be an Academy Trust or private sector employer).

SECOND GENERATION OUTSOURCINGS FOR STAFF NOT EMPLOYED BY THE SCHEME EMPLOYER CONTRACTING THE SERVICES TO AN ADMITTED BODY

A 2nd generation outsourcing is one where a service is being outsourced for the second time, usually after the previous contract has come to an end. Best Value Authorities, principally the unitary authorities, are bound by The Best Value Authorities Staff Transfers (Pensions) Direction 2007 so far as 2nd generation outsourcings are concerned. In the case of most other employing bodies, they must have regard to Fair Deal Guidance issued by the Government.

It is usually the case that where services have previously been outsourced, the transferees are employees of the contractor as opposed to the original scheme employer and as such will transfer from one contractor to another without being re-employed by the original scheme employer. There are even instances where staff can be transferred from one contractor to another without ever being employed by the outsourcing scheme employer that is party to the Admission Agreement. This can occur when one employing body takes over the responsibilities of another, such as a maintained school (run by the local education authority) becoming an academy. In this instance the contracting body is termed a 'Related Employer' for the purposes of the Local Government Pension Scheme Regulations and is obliged to guarantee the pension liabilities incurred by the contractor.

"Related employer" is defined as "any Scheme employer or other such contracting body which is a party to the admission agreement (other than an administering authority in its role as an administering authority)".

[Drafting Note – This section will potentially need amending when the outcome of the consultation published by the MHCLG on 10 January 2019 is known (found here: <https://www.gov.uk/government/consultations/local-government-pension-scheme-fair-deal-strengthening-pension-protection>).]

LGPS REGULATIONS 2013: SCHEDULE 2 PART 3, PARAGRAPH 8

Where, for any reason, it is not desirable for an admission body to enter into an indemnity or bond, the admission agreement must provide that the admission body secures a guarantee in a form satisfactory to the administering authority from—

- (a) a person who funds the admission body in whole or in part;
- (b) in the case of an admission body falling within the description in paragraph 1(d), the Scheme employer referred to in that paragraph;

(d) a body that is providing or will provide a service or assets in connection with the exercise of a function of a Scheme employer as a result of—

- (i) the transfer of the service or assets by means of a contract or other arrangement,*
- (ii) a direction made under section 15 of the Local Government Act 1999 (115) (Secretary of State's powers),*
- (iii) directions made under section 497A of the Education Act 1996 (116) ;*

- (c) a person who—

- (i) owns, or
- (ii) controls the exercise of the functions of, the admission body; or

In accordance with the above Regulations, the Fund requires a guarantee from the related employer. The related employer may seek a bond from the admitted body taking into account the risk assessment carried out by the Fund actuary.

APPENDIX C - TERMINATION POLICY

EXITING THE FUND

TERMINATION POLICY

[Unless agreed otherwise via an employer deferred debt arrangement], an employer ceases to participate within the Fund when the last active member leaves the Fund. This includes where the employer ceases to be eligible for membership e.g. a contract with a local authority comes to an end or the employer chooses to voluntarily cease participation. The employer becomes an exiting employer under the Regulations and the Fund is then required to obtain an actuarial valuation of that employer's liabilities in respect of benefits of the exiting employer's current and former employees along with a termination contribution certificate.

When an employer exits the Fund the Regulations give power to the Fund to set a repayment plan to recover the outstanding debt over a period at its sole discretion and this will depend on the affordability of the repayments and financial strength of the exiting employer. Once this repayment plan is set the payments would not be reviewed for changes in the funding position due to market or demographic factors.]

[Drafting Note – “Unless agreed otherwise “ has been added following the consultation published by the MHCLG on 8 May 2019 as it is possible employers could continue to participate in the Fund with no active members which is commonly referred to as an deferred debt arrangement (found here:

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/800321/LGPS_valuation_cycle_reform_consultation.pdf). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed. This is distinct from an employer exiting the Fund and agreeing a repayment plan.]

The Fund's policy for termination payment plans is as follows:

1. The default position is for exit payments and exit credits to be paid immediately in full.
2. At the discretion of the administering authority, instalment plans over a defined period will only be agreed when there are issues of affordability that risk the financial viability of the organisation and the ability of the Fund to recover the debt.
3. Any costs associated with the exit valuation will be paid by the employer by either increasing the exit payment or reducing the exit credit by the appropriate amount. In the case of an employer where the exit debt / credit is the responsibility of the original employer through a risk sharing agreement the costs will be charged directly to the employer unless the original employer directs otherwise.

EMPLOYERS WITHOUT A GUARANTOR

The lower risk funding basis is used for assessing liabilities on termination unless the Administering Authority agrees otherwise based on the advice of the Actuary. This basis mitigates against financial market risks as an investment strategy to run off these liabilities could be constructed to minimise fluctuations due to market shifts. In the event that the lower risk basis

produces a higher discount rate than the higher risk valuation funding basis, the higher risk valuation funding basis will be used.

The assumptions used will be consistent with the previous valuation assumptions, updated for market yields and inflation applying at the cessation date except that the discount rate will be based on the investment returns of the lower risk investment strategy and allowing for any further margins the Administering Authority deems appropriate based on the advice of the Actuary. At the valuation date the discount rate used would have been [x.xx]% per annum.

However, this does not provide against future adverse demographic experience relative to the assumptions which could emerge at future valuations. This risk is managed by including a higher level of prudence in the demographic assumptions on termination to further protect the remaining employers.

The termination basis for an outgoing employer currently includes an adjustment to the assumption for longevity improvements over time by increasing the rate of improvement in mortality rates to [2.25]% p.a. from those used in the 2019 valuation for ongoing funding and contribution purposes.

The policy for such employers will be:

- In the case of a surplus, the Fund pays the exit credit to the exiting employer following completion of the termination process (within 3 months of completion of the cessation assessment by the Actuary).
- In the case of a deficit, the Fund would require the exiting employer to pay the termination deficit to the Fund as a lump sum cash payment (unless agreed otherwise by the Administering Authority at their sole discretion) following completion of the termination process.

The Administering Authority can vary the treatment on a case by case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary.

[Subject to sufficient financial covenant and at the sole discretion of the Administering Authority an employer may continue to participate in the Fund with no contributing members under the Deferred Debt arrangement.]

[Drafting Note – Wording has been added following the consultation published by the MHCLG on 8 May 2019 (found here: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/800321/LGPS_valuation_cycle_reform_consultation.pdf). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

EMPLOYERS WITH A GUARANTOR

If, instead, the employing body has a guarantor within the Fund or a successor body exists to take over the employing body's liabilities, the Fund's policy is that the higher risk valuation funding basis will be used for the termination assessment unless the guarantor informs the Fund otherwise.

The guarantor or successor body will then, following any termination payment made by the exiting employer, subsume the assets and liabilities (and any surplus or deficit) of the employing body within the Fund. This is subject to the agreement of all parties involved (i.e. the Fund, the exiting employer and the guarantor) who will need to consider any separate agreements that have been put in place between the exiting employer and the guarantor.

In the event of a surplus, the default position is that, the surplus will be paid directly to the exiting employer within 3 months of completion of the cessation assessment by the Actuary (despite any

other agreements that may be in place). However, in some instances, the outgoing employer may only be responsible for part of the residual deficit or surplus as per the separate agreement and, if the parties are in agreement, the surplus would be retained by the Fund in favour of the outsourcing employer/guarantor. This would only occur if the Administering Authority is made aware of any such arrangement.

In maintaining a consistent approach, if all parties do not agree, the Fund will seek to recover any deficit from the exiting employer in the first instance although, if this is not possible, then the deficit will be recovered from the guarantor either as a further contribution collection or at the next valuation.

If a guarantor unjustifiably deviates from the Fund's policy (e.g. to subsume the residual assets, liabilities and any surplus or deficit of an exiting employer), any future termination events will, unless the situation is remedied, be treated in line with the approach adopted for employers without a guarantor in the Fund (e.g. the guarantor will be required to pay the termination deficit as a lump sum cash payment at the time of exit, any surplus would also be paid by the Fund to the guarantor at this point). The higher risk valuation funding basis will still be adopted in this case.

Again, the Administering Authority can vary the treatment on a case by case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary [and, for example, may adjust any exit payment or exit credit to take into account any risk sharing arrangements which exist between the exiting employer and other Fund employers].

[Drafting Note – Wording has been added following the LGPS (Amendment) Regulations 2018, which amended the LGPS 2013 Regulations to provide for the payment of an exit credit to an existing employer where, at the exit date, that employer's assets in the fund exceed its liabilities. In the case where the employer has a guarantor, the above clarifies who the recipient of the exit credit should be.]

DESIGNATING BODIES

In the event of cessation, the designating body will be required to meet any outstanding liabilities valued in line with the "employers without a guarantor" approach outlined above. Upon exit, if there is a shortfall, the assets and liabilities will revert to the Fund as a whole.

[EMPLOYERS THAT JOINED VIA THE 'DEEMED EMPLOYER' ROUTE]

In the event of cessation, the assets and liabilities will remain with the outsourcing scheme employer and no termination assessment or payment will be required.]

[Drafting Note – This has been added following the consultation published by the MHCLG on 10 January 2019 (found here: <https://www.gov.uk/government/consultations/local-government-pension-scheme-fair-deal-strengthening-pension-protection>). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

CONNECTED ENTITIES

In the event of cessation, the connected entity will be required to meet any outstanding liabilities valued in line with the approach outlined above. In the event there is a shortfall, the assets and liabilities will revert to the Fund as a whole (i.e. all current active employers).

In the event that a scheme employer provides a guarantee for their connected entity, the assets and liabilities will revert in totality to that scheme employer on termination, including any unrecovered deficit.

[EMPLOYERS WITH NO CONTRIBUTING MEMBERS]

An employer may participate in the Fund with no contributing members and utilise the “Deferred Debt” Arrangements at the sole discretion of the Administering Authority which will be subject to a satisfactory covenant review on an ongoing basis. In this circumstance they will be treated as per any other participating employer in relation to overall funding strategy (including potentially requiring a final exit payment at some point) allowing for the covenant.]

[Drafting Note – This has been added following the consultation published by the MHCLG on 8 May 2019 (found here: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/800321/LGPS_valuation_cycle_reform_consultation.pdf). The Funding Strategy Statement and Fund policies may need further adaptation once the consultation process has been completed.]

APPENDIX D - ACADEMIES / MULTI-ACADEMY TRUST POLICY

ACADEMY CONVERSIONS AND DEFICIT TRANSFERS

The Fund's policy regarding the treatment of schools when converting to academy status is for the new academy to inherit the school's share of the historic local authority deficit prior to its conversion. This is in accordance with the Department for Education (DfE) guidance issued when the Academy conversion programme was extended to cover all schools.

Therefore, the transferring deficit is calculated as the capitalised amount of deficit funding contributions (based on the local authority deficit recovery period) the school would have made to the Fund had it not converted to academy status. This deficit amount is subject to a limit to ensure that the minimum asset share of the new academy is nil.

MULTI ACADEMY TRUSTS

Multi-Academy Trusts (MATs) are groups of academies managed and operated by one proprietor. The employer of non-teaching staff in academies is the proprietor of the Academy Trust and not the individual academy within the Trust. It is therefore the proprietor who is the employer for LGPS purposes making the MAT legally responsible for staff across all schools in the pool.

Within a MAT all academies are governed by one Trust and a Board of Directors. The MAT holds ultimate responsibility for all decisions regarding the running of the individual academies, however, the governing bodies of the individual academies remain in place and the MAT will need to decide the extent to which it delegates functions to these governing bodies to enable more focused local control.

Multi-Academy Trusts are set up to cover a number of academies across England. The employees of the former schools can be employed directly by the Trust so they can be deployed across different academy schools in the Trust if necessary.

In cases where numerous academies are operated by the same managing Trust, the Fund is willing to allow a combined funding position and average contribution requirements to apply to all constituent academies. Notwithstanding this, the Fund will continue to track the constituent academies separately, in the interests of transparency and clarity around entry and exit events.

APPROACH TO SETTING CONTRIBUTION RATES

The Fund must have a separate employer number for each academy for transparency of cashflows, managing risks should an academy need to leave one Trust for another and for FRS reporting where disaggregated disclosure reports are required. It should also be noted that the Department for Education (DfE) have confirmed that the guarantee relates to individual academies and MATs.

The Fund will provide the MATs with the option of having a common Primary contribution rate for all the academies within the trust if the MAT is willing to settle for that approach bearing in mind that the risks of under and over payments will be shared by all academies in the MAT pool.

The past service deficit will still be assessed at an individual academy level so that it only relates to the staff of the respective academy. However, the MAT can opt to have the deficits for all the academies within the trust aggregated for the purposes of the actuarial valuation report.

Any new academies joining an existing MAT pool in the Fund can contribute at the employer contribution rate already established for the MAT but an actuarial assessment will still need to be carried out to determine the deficit applicable to the transferring staff.

OUTSOURCINGS BY MULTI ACADEMY TRUSTS

The Fund's current policy is in accordance with the Regulations requiring a separate admission agreement in respect of separate contracts.

Under **Schedule 2, Part 3, paragraph 5. of the 2013 Regulations**, if the admission body is exercising the functions of the Scheme employer in connection with more than one contract or other arrangement under paragraph 1(d)(i), the administering authority and the admission body shall enter into a separate admission agreement in respect of each contract or arrangement.

With the development of MATs, there is a case for the Fund to allow a MAT to enter into a single admission agreement with the contractor providing similar services at various sites provided the outsourcing is covered by a single commercial contract. The Fund has now developed a mechanism whereby this can be done, subject to certain conditions which must be agreed by the MAT.

The Fund will need to have sight of the contract in order to satisfy the regulatory requirement that the Admission Agreement covers one contract. The Admission Agreement will need to have provision for adding future employees should any academies join the MAT subsequent to the commencement date.

The Scheme employer, the Multi Academy Trust in this instance, needs to be a party to any admission agreement and, as such, is the ultimate guarantor. In the event of contractor failure, the LGPS regulations provide that the outstanding liabilities assessed by the Fund's actuary can be called from the Scheme employer i.e. the Multi Academy Trust.

If academies are to comply with "new" Fair Deal guidance, employees carrying out a service on behalf of the Academies must be allowed continued access to the LGPS. This can be achieved by entering into an Admission Agreement with the Administering Authority, Multi Academy Trust and the contractor (admitted body).

At every triennial valuation the actuary reviews the funding level of the admitted body and adjusts its employer contribution rate as required. Once either the service contract comes to an end or all the LGPS members have left, the admission agreement terminates and, in accordance with Fund policy, the Trust becomes responsible for the assets and liabilities standing to the account of the admitted body. A cessation valuation can be provided by the Fund actuary should the Trust request it. In accordance with Fund policy, the Trust becomes responsible for the assets and liabilities of and liabilities standing to the account of the admitted body when the admission agreement ceases.

APPENDIX E - RISK MANAGEMENT POLICY FOR NON-SCHEDULED BODIES

ADMISSION BODIES AS A RESULT OF OUTSOURCINGS

The Regulations provide that bodies admitted to the Fund as a result of an outsourcing of services (formerly transferee admission bodies) are guaranteed by the outsourcing Scheme employer. Therefore, these employers pose less financial risk to the Fund.

The Fund's policy is that the liabilities of such an admission body will in all cases revert to the outsourcing Scheme employer when the agreement ceases.

The administering authority will discuss the appropriate deficit recovery period for the admission body with the outsourcing Scheme employer. If the Scheme employer is retaining the financial risk, the deficit recovery period applied can be the same as the Scheme employer's. Otherwise the deficit recovery period will be the length of the commercial contract left to expiry (or the average remaining working lifetime of the membership if this is shorter).

ADMISSION BODIES PROVIDING A SERVICE TO THE COMMUNITY

These admission bodies are a diverse group. Some are financially very secure in that they receive funding from either the government or local authorities on a quasi-permanent basis. Others either have short-term funding contracts with local authorities, which may not be renewed when they expire, or depend heavily on various forms of fund raising.

The Fund's policy in recent years has been to require a guarantee from the Scheme employer which has financial links with the bodies and for this reason they are treated in the same way as those bodies admitted due to an outsourcing.

For historical reasons those which were admitted prior to 2004 have no guarantee and, as such, constitute a potential risk to the Fund. This is because they may cease operations with insufficient residual assets to meet their pension liabilities.

The risks associated with admitted bodies have always existed but these risks have assumed a higher profile recently because most of these bodies have a deficit of assets relative to liabilities.

The tools available to manage these risks are limited to using a more prudent valuation basis (such as the lower risk valuation basis) which minimises the deficit on exit; obtaining charges on assets in favour of the Fund; setting up escrow accounts or obtaining other security. The approach to agreeing the funding plans of these bodies will have regard to the financial strength of each individual body. The aim will be to achieve a balance between securing the solvency of the Fund and the sustainability of the organisation. For those with less secure income streams, the Fund will consider how it can manage contributions into the Fund in the short to medium term without compromising the financial stability of the organisation. Where there are assets or reserves, the administering authority will explore how these contingent assets could be used to assist in funding the liabilities or providing security to the Fund and its employing bodies.

Where there are no contingent assets the policy is to move over time to the lower risk funding basis and to shorten the deficit recovery period. However, this will need to be weighed against the ability of that body to pay higher contribution rates.

CONTROLLED/CONNECTED ENTITIES

These are employers that were “controlled entities” under the previous regulations. Under the current regulations those entities which were controlled by **local authorities** can only remain as Scheme employers if they become “connected entities”. The Fund is currently investigating the implications of this change so far as the three employers who originally joined the Fund as “controlled entities” are concerned. In these cases the parent Scheme employer is not obliged to provide a guarantee although with one exception the parent Scheme employers have elected to do so in order to allow the entities to use the Higher Risk Valuation Funding Basis. In the third case discussions will take place with the interested parties to see how the situation can best managed.

APPENDIX F – COVENANT ASSESSMENT AND MONITORING POLICY

An employer's covenant (including those with no active members who are operating under a deferred debt arrangement) underpins its legal obligation and ability to meet its financial responsibilities now and in the future. The strength of covenant depends upon the robustness of the legal agreements in place and the likelihood that the employer can meet them. The covenant effectively underwrites the risks to which the Fund is exposed, including underfunding, longevity, investment and market forces.

An assessment of employer covenant focuses on determining the following:

- > Type of body and its origins
- > Nature and enforceability of legal agreements
- > Whether there is a bond in place and the level of the bond
- > Whether a more accelerated recovery plan should be enforced
- > Whether there is an option to call in contingent assets
- > Whether there is a need for monitoring of ongoing and termination funding ahead of the next actuarial valuation

The strength of employer covenant can be subject to substantial variation over relatively short periods of time and, as such, regular monitoring and assessment is vital.

RISK CRITERIA

The assessment criteria upon which an employer should be reviewed could include:

- Nature and prospects of the employer's industry
- Employer's competitive position and relative size
- Management ability and track record
- Financial policy of the employer
- Profitability, cashflow and financial flexibility
- Employer's credit rating
- Position of the economy as a whole

Not all of the above would be applicable to assessing employer risk within the Fund; rather a proportionate approach to consideration of the above criteria would be made, with further consideration given to the following:

- The scale of obligations to the pension scheme relative to the size of the employer's operating cashflow
- The relative priority placed on the pension scheme compared to corporate finances

- An estimate of the amount which might be available to the scheme on insolvency of the employer as well as the likelihood of that eventuality.

ASSESSING EMPLOYER COVENANT

The employer covenant will be assessed objectively and the ability of the employer to meet its obligations will be viewed in the context of the Fund's exposure to risk and volatility based on publically available information and/or information provided by the employer. The monitoring of covenant strength along with the funding position (including on the termination basis) enables the Fund to anticipate and pre-empt employer funding issues and thus adopt a proactive approach. In order to objectively monitor the strength of an employer's covenant, adjacent to the risk posed to the Fund, a number of fundamental financial metrics will be reviewed to develop an overview of the employer's stability and a rating score will be applied using a Red/Amber/Green (RAG) rating structure.

In order to accurately monitor employer covenant, it will be necessary for research to be carried out into employers' backgrounds and, in addition, for those employers to be contacted to gather as much information as possible. Focus will be placed on the regular monitoring of employers with a proactive rather than reactive view to mitigating risk.

The covenant assessment will be combined with the funding position to derive an overall risk score. Action will be taken if these metrics meet certain triggers based on funding level, covenant rating and the overall risk score

FREQUENCY OF MONITORING

The funding position and contribution rate for each employer participating in the Fund will be reviewed as a matter of course with each triennial actuarial valuation. However, it is important that the relative financial strength of employers is reviewed regularly to allow for a thorough assessment of the financial metrics. The funding position will be monitored (including on the termination basis) using an online system provided to officers by the Fund Actuary.

Employers subject to a more detailed review, where a risk criterion is triggered, will be reviewed at least every six months, but more realistically with a quarterly focus.

COVENANT RISK MANAGEMENT

The focus of the Fund's risk management is the identification and treatment of the risks and it will be a continuous and evolving process which runs throughout the Fund's strategy. Mechanisms that will be explored with certain employers, as necessary, will include but are not limited to the following:

1. Parental Guarantee and/or Indemnifying Bond
2. Transfer to a more prudent actuarial basis (e.g. the termination basis)
3. Shortened recovery periods and increased cash contributions
4. Managed exit strategies
5. Contingent assets and/or other security such as escrow accounts.

APPENDIX G – INSURANCE ARRANGEMENTS

OVERVIEW OF ARRANGEMENT

For certain employers in the Fund, following discussions with the Fund Actuary and after considering potential alternative insurance arrangements, a captive insurance arrangement was established by the Administering Authority to cover ill-health retirement costs. This has applied to all ill-health retirements since 1 April 2017.

The captive arrangement operates as follows:

- “Premiums” are paid by the eligible employers into the captive arrangement which is tracked separately by the Fund Actuary in the valuation calculations. The premiums are included in the employer’s primary rate. The premium for 2020/23 is [x.xx]% of pay per annum
- The captive arrangement is then used to meet strain costs (over and above the premium paid) emerging from ill-health retirements in respect of active members i.e. there is no initial impact on the deficit position for employers within the captive.
- The premiums are set with the expectation that they will be sufficient to cover the costs in the 3 years following the valuation date. If any excess premiums over costs are built up in the Captive, these will be used to offset future adverse experience and/or result in lower premiums at the discretion of the Administering Authority based on the advice of the Actuary.
- In the event of poor experience over a valuation period any shortfall in the captive fund is effectively underwritten by the other employers within the Fund. However, the future premiums will be adjusted to recover any shortfall over a reasonable period with a view to keeping premiums as stable as possible for employers. Over time the captive arrangement should therefore be self-funding and smooth out fluctuations in the contribution requirements for those employers in the captive arrangement.
- Premiums payable are subject to review from valuation to valuation depending on experience and the expected ill health trends. They will also be adjusted for any changes in the LGPS benefits. They will be included in employer rates at each valuation or on commencement of participation for new employers.

EMPLOYERS COVERED BY THE ARRANGEMENT

Those employers (both existing and new) that will generally be included in the captive are:

- Academies
- Community related Admitted Bodies
- Contract related Admitted Bodies
- Town and Parish Councils
- Designating Bodies.

These employers will be notified of their participation. New employers entering the Fund who fall into the categories above will also be included at the discretion of the Administering Authority and

where it is felt to be beneficial to the long term covenant and financial health of an employer, specific employers (outside of the categories listed above) may be included within the captive arrangement. In addition, the Administering Authority has the ability to exclude any employer in order to manage employer risk within the Fund.

The Fund and the Actuary will monitor the number of retirements that each captive employer is granting over time. If any employer has an unusually high incidence of ill health retirements, consideration will be given to the governance around the eligibility criteria applied by the employer and it is possible that some or all of the costs would fall on that employer if the governance was not deemed strong enough.

For all other employers who do not form part of the captive arrangement, the current treatment of ill-health retirements will still apply. The Fund therefore continues to monitor ill-health retirement strain costs incurred in line with the allowance made in the actuarial assumptions. Once the allowance is exceeded, any excess costs are recovered from the employer, either at the next valuation or at an earlier review of the contributions due, including on termination of participation.

APPENDIX H - GLOSSARY OF TERMS

ACTUARIAL VALUATION: an investigation by an actuary into the ability of the Fund to meet its liabilities. For the LGPS the Fund Actuary will assess the funding level of each participating employer and agree contribution rates with the administering authority to fund the cost of new benefits and make good any existing deficits as set out in the separate Funding Strategy Statement. The asset value is based on market values at the valuation date.

ADMINISTERING AUTHORITY: the council with a statutory responsibility for running the Fund and that is responsible for all aspects of its management and operation.

ADMISSION BODIES: A specific type of employer under the Local Government Pension Scheme (LGPS) who do not automatically qualify for participation in the Fund but are allowed to join if they satisfy the relevant criteria set out in the Regulations.

BENCHMARK: a measure against which fund performance is to be judged.

BEST ESTIMATE ASSUMPTION: an assumption where the outcome has a 50/50 chance of being achieved.

BONDS: loans made to an issuer (often a government or a company) which undertakes to repay the loan at an agreed later date. The term refers generically to corporate bonds or government bonds (gilts).

CAREER AVERAGE REVALUED EARNINGS SCHEME (CARE): with effect from 1 April 2014, benefits accrued by members in the LGPS take the form of CARE benefits. Every year members will accrue a pension benefit equivalent to 1/49th of their pensionable pay in that year. Each annual pension accrued receives inflationary increases (in line with the annual change in the Consumer Prices Index) over the period to retirement.

CPI: acronym standing for "Consumer Prices Index". CPI is a measure of inflation with a basket of goods that is assessed on an annual basis. The reference goods and services differ from those of RPI and the method of calculation is different. The CPI is expected to provide lower, less volatile inflation increases. Pension increases in the LGPS are linked to the annual change in CPI.

CONTINGENT ASSETS: assets held by employers in the Fund that can be called upon by the Fund in the event of the employer not being able to cover the debt due upon termination. The terms will be set out in a separate agreement between the Fund and employer.

CORPORATE BOND EMPLOYER: an employer in the Fund, under previous Fund policies, whose asset share is invested in corporate bond assets and for whom the discount rate used to assess the liabilities is determined based on the market yields of high quality corporate bond investments (usually at least AA rated) based on the appropriate duration of the liabilities being assessed. These employers will now be moved onto the lower risk funding basis.

COVENANT: the assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant

means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term or affordability constraints in the short term.

DEFICIT: the extent to which the value of the Fund's past service liabilities exceeds the value of the Fund's assets. This relates to assets and liabilities built up to date, and ignores the future build-up of pension (which in effect is assumed to be met by future contributions).

DEFICIT RECOVERY PERIOD: the target length of time over which the current deficit is intended to be paid off. A shorter period will give rise to a higher annual contribution, and vice versa.

DISCOUNT RATE: the rate of interest used to convert a cash amount e.g. future benefit payments occurring in the future to a present value i.e. the liabilities. A higher discount rate means lower liabilities and vice versa.

EMPLOYER'S FUTURE SERVICE CONTRIBUTION RATE ("PRIMARY RATE"): the contribution rate payable by an employer, expressed as a % of pensionable pay, as being sufficient to meet the cost of new benefits being accrued by active members in the future. The cost will be net of employee contributions and will include an allowance for the expected level of administrative expenses.

EMPLOYING BODIES: Scheme employers that participate in the LGPS

EQUITIES: shares in a company which are bought and sold on a stock exchange.

EQUITY PROTECTION: an insurance contract which provides protection against falls in equity markets. Depending on the pricing structure, this may be financed by giving up some of the upside potential in equity market gains.

EXIT CREDIT: the amount payable from the Fund to an exiting employer where the exiting employer is determined to be in surplus at the point of cessation based on a termination assessment by the Fund Actuary.

FUNDING OR SOLVENCY LEVEL: the ratio of the value of the Fund's assets and the value of the Fund's liabilities expressed as a percentage.

FUNDING STRATEGY STATEMENT: This is a key governance document which the Administering Authority is obliged to prepare and publish that outlines how the administering authority will manage employer's contributions and risks to the Fund.

GOVERNMENT ACTUARY'S DEPARTMENT (GAD): the GAD is responsible for providing actuarial advice to public sector clients. GAD is a non-ministerial department of HM Treasury.

GUARANTEE / GUARANTOR: a formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's covenant to be as strong as its guarantor's

HIGHER RISK VALUATION FUNDING BASIS: the financial and demographic assumptions used to determine the employer's contribution requirements. The relevant discount rate used for valuing the present value of liabilities is determined based on the expected long term return achieved on the Fund's investments. This is expressed as an expected return over CPI.

ILL HEALTH CAPTIVE: this is a notional fund designed to protect certain employers against excessive ill health costs in return for an agreed insurance premium.

INVESTMENT STRATEGY: the long-term distribution of assets among various asset classes that takes into account the Funds objectives and attitude to risk.

LETTING EMPLOYER: an employer that outsources part of its services or workforce to another employer, usually a contractor. The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer.

LGPS: the Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate those employing bodies which are eligible to participate, members' contribution rates, benefit calculations and certain governance requirements.

LIABILITIES: the actuarially calculated present value of all benefit entitlements i.e. scheme cashflows of all members of the Fund, accumulated to date or in the future. The liabilities in relation to the benefit entitlements earned up to the valuation date are compared with the present market value of Fund assets to derive the deficit and funding/solvency level. Liabilities can be assessed on different set of actuarial assumptions depending on the purpose of the valuation.

LOWER RISK FUNDING BASIS: an approach where the discount rate used to assess the liabilities is determined based on the expected long term return achieved on the Fund's lower risk investment strategy. This is usually adopted for employers who are deemed to have a weaker covenant than others in the Fund, are planning to exit the Fund or would like to target a lower risk strategy. This basis is adopted for ongoing contribution rate purposes as the employers' asset share is invested in the lower risk investment strategy.

LOWER RISK INVESTMENT STRATEGY: an investment strategy which is predominately linked to corporate bond investment assets that match the liabilities of the employers within it (as a minimum this will be reviewed following each actuarial valuation). In addition, the strategy has exposure to the Liability Driven Investment ("LDI") portfolio to provide protection against changes in market inflation expectations.

MANDATORY SCHEME EMPLOYERS: employers that have the statutory right to participate in the LGPS. These organisations (set out in Part 1 of Schedule 2 of the 2013 Regulations) would not need to designate eligibility, unlike the Part 2 Scheme Employers. For example, these include councils, colleges, universities and academies.

MATURITY: a general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.

MEMBERS: The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired and dependants of deceased ex-employees).

MINIMUM RISK FUNDING BASIS: an approach where the discount rate used to assess the liabilities is determined based on the market yields of Government bond investments based on the appropriate duration of the liabilities being assessed. This can be used as a benchmark to assess

the level of reliance on future investment returns in the funding strategy and therefore the level of risk appetite in a Funds choice of investment strategy.

ORPHAN LIABILITIES: liabilities in the Fund for which there is no sponsoring employer within the Fund. Ultimately orphan liabilities must be underwritten by all other employers in the Fund.

PERCENTILES: relative ranking (in hundredths) of a particular range. For example, in terms of expected returns a percentile ranking of 75 indicates that in 25% of cases, the return achieved would be greater than the figure, and in 75% cases the return would be lower.

PHASING/STEPPING OF CONTRIBUTIONS: when there is an increase/decrease in an employer's long term contribution requirements, the increase in contributions can be gradually "stepped" or phased in over an agreed period. The phasing/stepping can be in equal steps or on a bespoke basis for each employer.

POOLING: employers may be grouped together for the purpose of calculating contribution rates, (i.e. a single contribution rate applicable to all employers in the pool). A pool may still require each individual employer to ultimately pay for its own share of deficit, or (if formally agreed) it may allow deficits to be passed from one employer to another.

PREPAYMENT: the payment by employers of contributions to the Fund earlier than that certified by the Actuary. The amount paid will be reduced in monetary terms compared to the certified amount to reflect the early payment.

PRESENT VALUE: the value of projected benefit payments, discounted back to the valuation date.

PRIMARY RATE OF THE EMPLOYERS' CONTRIBUTION: the contribution rate required to meet the cost of the future accrual of benefits including ancillary, death in service and ill health benefits together with administration costs. It is expressed as a percentage of pensionable pay, ignoring any past service surplus or deficit, but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer's covenant. The Primary rate for the whole fund is the weighted average (by payroll) of the individual employers' Primary rates.

PROFILE: the profile of an employer's membership or liability reflects various measurements of that employer's members, i.e. current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members compared to their salary levels, etc.

PRUDENT ASSUMPTION: an assumption where the outcome has a greater than 50/50 chance of being achieved i.e. the outcome is more likely to be overstated than understated. Legislation and Guidance requires the assumptions adopted for an actuarial valuation to be sufficiently prudent.

RATES AND ADJUSTMENTS CERTIFICATE: a formal document required by the LGPS Regulations, which must be updated at least every three years at the conclusion of the formal valuation. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three year period until the next valuation is completed.

REAL RETURN OR REAL DISCOUNT RATE: a rate of return or discount rate net of (CPI) inflation.

RECOVERY PLAN: a strategy by which an employer will make up a funding deficit over a specified period of time (“the recovery period”), as set out in the Funding Strategy Statement.

SCHEME EMPLOYERS: organisations that participate in the Avon Pension Fund

SECTION 13 VALUATION: in accordance with Section 13 of the Public Service Pensions Act 2014, the Government Actuary’s Department (GAD) has been commissioned to advise the Department for Communities and Local Government (DCLG) in connection with reviewing the 2019 LGPS actuarial valuations. All LGPS Funds therefore will be assessed on a standardised set of assumptions as part of this process.

SECONDARY RATE OF THE EMPLOYERS’ CONTRIBUTION: an adjustment to the Primary rate to reflect any past service deficit or surplus, to arrive at the rate each employer is required to pay. The Secondary rate may be expressed as a percentage adjustment to the Primary rate, and/or a cash adjustment in each of the three years beginning 1 April in the year following that in which the valuation date falls. The Secondary rate is specified in the rates and adjustments certificate. For any employer, the rate they are actually required to pay is the sum of the Primary and Secondary rates. Secondary rates for the whole fund in each of the three years shall also be disclosed. These will be calculated as the weighted average based on the whole fund payroll in respect of percentage rates and as a total amount in respect of cash adjustments.

SOLVENCY FUNDING TARGET: an assessment of the present value of benefits to be paid in the future. The desired funding target is to achieve a solvency level of a 100% i.e. assets equal to the accrued liabilities at the valuation date assessed on the ongoing concern basis.

50/50 SCHEME: in the LGPS, active members are given the option of accruing a lower personal benefit in the 50/50 Scheme, in return for paying a lower level of contribution.

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Responses to Funding Strategy Statement (FSS)

(The views expressed are those of the employers themselves; in some cases they have been paraphrased. The intention has been to represent the comments concisely and as accurately as possible. Inevitably some of the detailed supporting material has had to be omitted.)

Employer	Comments
Bristol City Council	<ul style="list-style-type: none"> • Sets out context of BCC's experiences during the period of austerity since 2010 and highlights the difficulty of providing services in this environment. • Salary increase assumption of 3.9% is excessive, 2-3% p.a. would be more appropriate in medium to long term. • Long term projections for CPI and RPI are higher than Bank of England assumptions. • Questions the need to reduce the deficit recovery period by 3 years to 13 years, a deficit recovery period of 16 years is reasonable. • Local Authorities are under significant cost pressures due to increased demand for services and uncertain funding. • What consideration has been given to affordability and how will covenant information be utilised? • Disagree that the deficit contributions should remain at monetary levels from the preceding valuation. • Employers in surplus should have greater flexibility to withdraw funds or accelerate the runoff below 12 years. • McCloud issues remain a significant uncertainty. When the outcome is known APF should revisit employer contributions at that time. • What Brexit assumptions have been made? Are APF forecasting a financial downturn? • The FSS should explain the reasons for using different assumptions to other Funds. • Are there other similar contingent liabilities? • The FSS is not yet complete; more detail on the impact of legislative changes, and demographic assumptions is needed. • Is APF being too prudent in view of improvement in Funding levels, slowdown in longevity, low pay growth and low ill health retirements? This should allow for contribution reductions. • What are the benefits, if any, at this stage from the Brunel partnership?
Bath and North East Somerset Council	<ul style="list-style-type: none"> • Salary increase assumption of 3.9% is at the higher end of expectations. The Council's medium term pay strategy is 2% for the next 5 years. • Request DRP is reviewed and a planned reduction is suspended for further review at the next valuation. This is to help with affordability issues in the light of continued financial pressures. • Welcome prepayment options and phasing in of contributions. • Welcome an update on McCloud and further work the actuary is undertaking. • Welcome further discussions to reflect in 2020/21 budgets.
South Gloucestershire Council	<ul style="list-style-type: none"> • Salary increase assumption of 3.9% seems high, salary increases of 2-3% would be more appropriate given current pay restraint and affordability in the public sector. • Dispute that the Fund needs to be solvent in 12-13 years. Suggest resetting the DRP to 16 years is a reasonable time period. • There needs to be reality around the Government's financial position with

	<p>increased social care costs and reduced funding.</p> <ul style="list-style-type: none"> • It is likely the Local Government Spending Review will be for 2020/21 only leaving uncertainty about long term funding streams and as much flexibility as possible is needed to reduce funding pressures. • Much information is outstanding and no expenses met by the Fund are available. • Understand the funds' performance has been strong with income greater than anticipated and subsequently 'locked in' through secure investments. As a result the current funding level is high supporting our view. • Note that the McCloud judgement is likely to increase deficits and contributions and a compensating adjustment to the deficit recovery period is necessary to mitigate the impact.
West of England Combined Authority	<ul style="list-style-type: none"> • WECA is assuming salary increases of 2-3% over the next 3 years. • Disputes that the Fund needs to be fully solvent in 12-13 years. The Fund is seeking to reduce the deficit recovery period by a further 3 years when salaries are increasing and government funding is reducing. • Returns have outperformed targets and have been locked into more secure longer term investments. Difficult to understand how local authorities can be expected to make further cuts in order to achieve a quicker recovery period. • The DRP should remain at 16 years with employer contributions over the next 3 years either frozen or reduced. This is a 'reasonable time period' and complies with the long term plan for the region. • It is likely the Local Government Spending Review will be for 2020/21 only, leaving uncertainty about long term funding streams and as much flexibility as possible is needed to reduce pressures. • Much information is outstanding, importantly the current funding level and the progress made over the last couple of triennial valuations. No expenses of the fund are given to comment on the appropriateness.
University of Bath	<ul style="list-style-type: none"> • The University has estimated short-term salary increases of 2.4%. Longer term scheme wide salary projections in the FSS are forecast at 3.9%. The university believes this is a reasonable forecast. • The HE sector has been subject to recent funding review (Augar). The implementation is currently uncertain but the headline recommendation to reduce tuition fees will have a significant financial impact on the University if any shortfall cannot be made up from another income source (grants).
Weston College	<ul style="list-style-type: none"> • Disagrees that deficit contributions need to be maintained at monetary levels from the preceding valuation, in conflict with competing cost pressures. • An automatic 3 year reduction in DRP is too rigid. It does not allow for a deficit emerging to be funded over a reasonable timescale. This rigid approach hinders prudent financial planning for employers. Allowing APF discretion is uncertain. • Support alignment of average deficit recovery periods at 12 years. Strongly support recovery periods set on a consistent basis across employer categories. The consistency principle should be applied ahead of maintaining monetary levels and reducing recovery periods. • The college has a deficit recovery period of 5 years and proposes this is reset to 12 years as a consistent starting point for future valuations. • The GAD section 13 dry run report showed APF 78% funded but this increased to 92% on a standardised basis suggesting APF is more prudent than the average and a less severe approach is needed particularly for the

	<p>future service rate.</p> <ul style="list-style-type: none"> Weston College consider that they have a strong covenant in the sector and an increase in contributions is a very important cost factor for the College to consider. Operating within statutory financial constraints which limit the capacity to pick up extra costs. Weston College is keen to engage with the Fund.
University of the West of England	<ul style="list-style-type: none"> The salary assumption of 1.5% over inflation is on the high side but acceptable, despite the controls on pay awards. It is uncertain if the Augar Report recommendations to cut University fees will be implemented and fees are fixed to 2020/21. It will be a challenge for the institution to deal with increasing costs. McCloud could significantly affect the funding level of the scheme and University and would welcome the opportunity to explore the impact and mitigation in the final agreement of contribution rates. Sessions provided to HE/FE employers are very helpful.
Sirona	<ul style="list-style-type: none"> Does not agree that public sector pay will increase 1.5% above inflation having regard to current experience. Rationale for shortening the deficit recovery period is unclear. Questions whether the proposed 3 year shortening of the deficit recovery period is reasonable in the context of public services that are severely challenged by austerity. Any increase in employer pension costs will exacerbate financial and service pressures, particularly in the context of a contract let to Sirona on a "flat cash basis". Any increase in the already high employer's contribution rate will challenge a service where the majority of costs are pay related. Cannot support the assumptions behind the consultation and any increase will create considerable financial challenges.
Alliance Homes	<ul style="list-style-type: none"> The salary assumption of 3.9% is more prudent than we might expect when looking at Alliance's long term pay expectations and we believe a lower rate would be more appropriate. The recovery period we would have expected to be more consistent with the 2016 valuation in order to remain reasonable. The discount rate is reducing from CPI plus 2.2% to CPI plus 1.75% for past service and the rate for future service is also reduced. Is this reflecting changes in market expectations, or has additional prudence been assumed? Inflation expectations; long term projections for CPI and RPI are higher than we expect when considering the 2016 assumptions and out turn over the following three years. Is additional prudence allowed for? Notes a number of areas such as how the McCloud judgement will be allowed for are not yet proposed. Would welcome the opportunity to discuss employer specific assumptions used for Alliance Homes participation.
Downend and Bromley Heath Parish Council	<ul style="list-style-type: none"> Have considered the FSS and have no additional comments to make.
Oldland Parish Council	<ul style="list-style-type: none"> Supports the FSS and requests that a commitment to move away from investment in fossil fuel related businesses is made.
Whitchurch	<ul style="list-style-type: none"> It is difficult for the employer to make comments on the questions raised in

Village Parish Council	the FSS given its technical nature.
Clevedon Learning Trust	<ul style="list-style-type: none"> • The salary assumption appears very generous. The academy trust follows the national picture and over the past 5 years pay increments have barely been at inflation let alone 1.5% above inflation. • There is no reason why the deficit recovery period needs to be reduced by 3 years. The liabilities will not become due for a large number of years. The Fund is able to function in terms of cash flow. The rationale for reducing the repayment period should be explicitly a cash flow issue as opposed to an accounting exercise. It is not fair to have a plan which could lead to people leaving the profession and ultimately costing you future contributions which you are relying on in the assumptions. • What is the cash flow impact of a recovery plan of differing lengths? This is how it should be addressed. • Affordability of contributions is a really big issue. Educational funding is tight and an increase in contributions that is not funded will make it extremely difficult to meet payments over 2020-2023. • Keen to understand how they can phase in contribution increases from 1st September 2020 as there is no capability to cope with increased contributions from 1st April 2020. • Need sufficient time to make savings to pay for contribution increases.
Extend learning Academy Trust	<ul style="list-style-type: none"> • ELAN have budgeted 2%p.a. from 2020-2023 for support staff salary increases in addition to incremental increases. This is lower than inflation plus 1.5%. • ELAN schools are all facing ever smaller budgets in line with the regional and national picture. Spending reductions and cuts to staffing have been made and are anticipated to continue from 2020-2023 as budgets are reducing.
Russell Educational Trust	<ul style="list-style-type: none"> • Pay rises for the next few years depend on funding from DfE and are not known until treasury budgets are drawn up. • See no reason to bring forward the deficit recovery period by 3 years, this would not achieve anything positive. • As a new Free School ideally any increase in contributions would be moved into future years as the School has not had the opportunity to accrue reserves yet.
Learn @ Multi Academy Trust	<ul style="list-style-type: none"> • Have budgeted for pay increases of 2%p.a. • Budgets are already tight and do not want contributions to go up.

If anyone would like to see any of these responses in full please contact Liz Woodyard.

Avon Pension Fund (APF) Statutory Funding Strategy Statement (FSS)

Response by independent Chair of Local Pension Board (LPB)

Introduction

- 1) Thank you for email of 12th July providing members of the LPB the opportunity to comment on the Avon Pension Fund (APF) updated FSS. I understand our comments will be included in papers or tabled at the Pension Committee (PC) meeting on 27 September.

Locus

- 2) The statutory locus of the APF LPB is to assist the APF Administering Authority comply with Public Service Pensions Act, LGPS regulations, and TPR requirements; and to ensure the governance and management of the APF is efficient and effective.
- 3) In respect of the updated FSS the LPB role is to consider a) does the APF FSS comply with LGPS Regulation 58, b) does the APF FSS comply with MHCLG statutory guidance on preparing and maintaining FSS issued in 2016, c) does the FSS comply with the LGPS regulations and TPR Code 14 in respect of consultation and disclosure to employers and fund member communication requirements, and d) does the FSS assist BANES in improving the efficiency and effectiveness of the APF
- 4) The Pensions Committee should note that under LGPS regulation 8 the LPB would be consulted by Secretary of State for DCLG prior to his/her intervention if he/she considers the Administering Authority is failing to act in accordance with the FSS statutory guidance.

Comments and recommendations to the Administering Authority

Statutory compliance

- 5) It is my view the preparation, consultation with fund stakeholders, and contents of the FSS appears robust and to cover the regulatory requirements. However the LPB recommends that this should be confirmed by the funds actuaries and senior officers at the time when the PC are asked to approve the final FSS.
- 6) The LPB recommend this would best be done on a factual basis by the use of compliance table/tick sheet against the 2016 FSS statutory guidance (as was done by APF officers for the statutory Investment Strategy Statement (ISS) against its statutory guidance) and any MHCLG or national LGPS scheme advisory board (SAB) supplementary guidance.

Solvency

- 7) The FSS refers to an objective to achieve 100% solvency level. The PC should note that the actual market value of the funds assets needed to maintain this on an ongoing basis will undoubtedly fluctuate (possibly markedly) by a varying % over different market and economic cycles and geo-political changes during inter-valuation years.
- 8) Consequently it might be prudent for the FSS to actually target slightly >100% solvency in order to reduce and smooth out this risk in order to consistently maintaining an average solvency of 100% for say 95% of the time or some other % or statistical probability recommended by the funds actuary. This approach is used

by some public sector funds in the EU to ensure they are continually 100% funded with no risk of falling below 100% in inter-valuation periods. As the LGPS is moving from triennial to quadrennial valuations this becomes more important consideration.

Actuarial assumption comparatives

- 9) In various places the covering paper and draft FSS refer to changing the 2016 assumptions for the 2019 valuation. However for absolute clarity for the FSS users it would be helpful throughout the covering paper and in the FSS for the following convention to be adopted. Where the 2019 assumption/figure to be used is presented then immediately behind/next to it in brackets the 2016 assumption figure that was used in the 2016 valuation should be provided for comparison. By doing so the reader can more easily tell to what extent the 2019 assumption/figure is reducing or increasing from the 2016. This is especially important for key financial assumptions like “real expected asset return above CPI”, “discount rate”, “future service rates”, “deficit recovery period” etc.

Deficit recovery

- 10) Seeking to reduce historic funding deficit is very laudable and is consistent with best practice and supported by the Pensions Regulator. However the proposal to reduce the deficit recovery period from 16 to 13 years could impact on employer contributions and may well cause a negative reaction from the funds key stakeholders. This might benefit from further consideration by the PC who may wish to understand the actual quantum of the additional cash needed from large employers (who have other financial pressures). The PC might wish to consider a range of mitigation measures or seek further actuarial advice on other options to reduce the fund past service deficit - be this in respect of other actuarial assumptions and or to adjust the investment strategy risk profile and asset allocation to deliver a higher investment return.

Future regulatory changes

- 11) In addition to the McCloud judgement there are a number of other known and likely potential regulatory changes being put forward by the MHCLG and or national LGPS SAB. Most are likely to further increase the funds future liabilities and cash flows above and beyond what has currently been modelled in the valuation process so far. It is recommended that the PC seek advice from the funds actuary on whether and how to incorporate an allowance for them in the current or new actuarial assumptions or if alternatively to adjust the investment strategy risk profile and asset allocation to deliver a higher investment return.

Climate change

- 12) The covering paper (section 7) refers to climate change and reducing financial risk via the investment strategy and asset allocation. This is welcomed and important given the current predictions about the impact of climate change on mankind.
- 13) However the draft FSS document is actually silent on climate change. As well as possibly negatively affecting the value of some of the funds assets, the Committee must be aware climate change may also impact on the fund and its members in other ways – such as mortality and longevity, as well as population migration into BANES and political change.

- 14) The Bank of England, Financial Conduct Authority, Financial Reporting Council, the Pensions Regulator, Association of British Insurers, and Government Actuaries Department are all actively now taking climate change into account in their funding strategy policy work, albeit in different ways and different extents. The Avon Pension Fund FSS should do so to.
- 15) Specifically the Institute and Faculty of Actuaries has issued specific guidance on climate change <https://www.actuaries.org.uk/practice-areas/resource-and-environment/research-working-parties/practical-guide-climate-change-life-actuaries>
The Committee is recommended to ask the fund actuaries to include a statement in the 2019 FSS how the impact of climate change has been and will be integrated into the 2019 and future fund valuations (in addition to statements in the fund Investment Strategy Statement (ISS)).

Efficacy

- 16) In general terms the updated FSS should help improve the effectiveness and efficiency of the APF future funding level. However because of the strategic importance of the on-going transfer of APF asset management to BBP, it is recommended the FSS would strongly benefit by the inclusion of a policy statements on how the financial savings from APF asset pooling into BPP will affect future employers contributions from 2019 onwards.

Howard Pearce

Chair of the Local Pension Board

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Funding Strategy Statement Checklist 2019

Regulation 58 of LGPS Regulations 2013 provides statutory framework for preparing and maintaining an FSS. In addition CIPFA has produced guidance for administering authorities.

Requirements of regulation 58	Confirmation of Compliance	Comments
1) An administering authority must, after consultation with such persons as it considers appropriate, prepare, maintain and publish a written statement setting out its funding strategy.	✓	The draft FSS was circulated to all employers and Pension Board.
2) The authority must keep the statement under review and, after consultation with such persons as it considers appropriate, make such revisions as are appropriate following a material change in its policy set out in the statement, and if revisions are made, publish the statement as revised.	✓	The FSS is reviewed at each valuation.
3) In preparing, maintaining and reviewing the statement, the administering authority must have regard to: <ul style="list-style-type: none"> a) the guidance set out in the document published in October 2012 by CIPFA, the Chartered Institute of Public Finance and Accountancy and called "Preparing and Maintaining a Funding Strategy Statement in the Local Government Pension Scheme 2012 b) the current version of the investment strategy under regulation 7 (investment strategy statement) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016. 	✓	A checklist against the CIPFA guidance is set out below. Section 7 of the FSS references the current Investment Strategy Statement.

CIPFA Guidance	Confirmation of Compliance	Reference to FSS section
CIPFA states that the FSS should be prepared having regard to the guidance given on the following matters:		
<p>1) The purpose of the FSS in policy terms including the processes by which the admin authority:</p> <ul style="list-style-type: none"> a) Establishes a clear and transparent fund-specific strategy that will identify how employers' pension liabilities are best met going forward b) Supports the desirability of maintaining as nearly constant a primary contribution rate as possible as defined in Reg 62(5) of the LGPS Regulations 2013 c) Ensures that the regulatory requirements to set contributions so as to ensure the solvency and long-term cost efficiency of the fund are met d) Takes a prudent longer-term view of funding those liabilities 	✓	Section 2
2) The aims and purpose of the pension fund	✓	Section 3
3) The responsibility of the key parties including the administering authority, individual employers and fund actuary	✓	Section 4
<p>4) Solvency issues, target funding levels and long-term cost efficiency. The funding plan must be prudently appropriate, relevant to local circumstances, balanced with the short-term and long-term funding requirements of the pension fund, including the ability to meet pension obligations as they fall due.</p> <p>Securing solvency and long-term cost efficiency is a regulatory requirement whereas as constant as possible primary contribution rate remains a desirable outcome</p> <p>Long-term cost efficiency will be met if the rate of employer contributions is sufficient to for the cost of current benefit accrual with and appropriate adjustment for any surplus/deficit.</p>	✓	Section 5
<p>5) Links to the investment policy set out in the Investment Strategy Statement</p> <p>The required investment returns to meet the aspirations set out in the FSS must be compatible with the investment policy set out in the ISS and this should be confirmed and explained in the FSS</p>	✓	Section 7
6) Identifications of risk and countermeasures including investment, employer, liquidity/maturity, liability, regulatory and compliance risks	✓	Section 8