Bath & North East Somerset Council

MEETING:	**AVON PENSION FUND COMMITTEE**	
MEETING DATE:	**13 DECEMBER 2013**	**AGENDA ITEM NUMBER**
TITLE:	**ACTUARIAL VALUATION 2013**	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
List of attachments to this report: Nil		

1 THE ISSUE

1.1 The Actuary has calculated the contribution rates effective 1 April 2014 for the majority of the employing bodies within the Fund. Those outstanding are for bodies where special circumstances apply.

1.2 In due course (before 31 March 2014) the Actuary will prepare the actuarial valuation report which will be circulated to all employing bodies. In the meantime, the employing bodies have been notified of their revised rates.

1.3 The aim of the 2013 valuation was to maintain stable employer contribution rates where possible, and the Funding Strategy Statement (FSS), which was approved by the Committee in September 2013, set out the parameters as to how this objective would be met.

1.4 By utilising the flexibility allowed within the FSS, deficit recovery payments have been kept relatively stable. The basis for calculating the future service rate has been adjusted to take account of market yields; this has led to an increase in contribution rate for most employers.

1.5 The valuation has taken account of the new scheme (LGPS 2014). At the overall Fund level this has resulted in savings of c. 1.7% of pensionable payroll. However the impact is dependent on the membership profile (especially age) and therefore the results across the employers varies significantly with some employers experiencing *higher costs,* not savings.

1.6 This report examines the outcome of the valuation process for the whole fund and highlights the principal changes which have occurred since the 2010 valuation.

1.7 The Actuary will give a presentation on the outcome at the Committee meeting.

2 RECOMMENDATION

The Committee notes:

2.1 The outcome of the actuarial valuation 2013

3 FINANCIAL IMPLICATIONS

3.1 The actuarial valuation sets the contribution rates for all employers for the 3 years commencing 1 April 2014. The costs for completing the valuation are provided for in the 2013/14 budget.

4 BACKGROUND

4.1 The Local Government Pension Scheme (LGPS) Regulations require LGPS funds to have an actuarial valuation every three years. The 2013 valuation has a base date of 31 March 2013 with new employer rates effective from 1 April 2014.

4.2 This valuation is taking place amid significant funding pressures within the public sector. The valuation also incorporates the LGPS 2014 benefit structure. The LGPS 2014 does not affect the value of accrued service (or the past service deficit) as all accrued rights are protected. The new benefits structure will reduce the cost of future accruals; however the impact of this at the individual employer level will vary significantly. This is because there are protections in place for members aged 55 or over at 1 April 2012 and therefore the level of savings will depend on the age profile of the membership.

4.3 The actuary has structured the valuation having regard to the FSS and has used the flexibility within the FSS to accommodate the budgetary pressures facing all scheme employers.

5 ACTUARIAL VALUATION 2013 OUTCOME

5.1 The aim of the 2013 valuation is to maintain stable contribution rates where possible. The funding level has fallen from 82% in 2010 to 76%.

5.2 The initial outcome of the valuation is as follows:

	2010	2013
Deficit	£552m	£1,005m
Funding Level	82%	76%
Value of assets	£2,459m	£3,147m
Value of Liabilities	£3,011m	£4,152m
Average employee contribution rate	6.4%	6.4%
Average future service rate (employer)	11.8%	14.3%
Annual past service deficit payments	£33m *	£56m
Past service recovery period (years)	23	20

** 2010 payment is the annual payment for 2014/15, based on 23 year recovery period at 2010 and indexed at 4.5% p.a.*

In light of discussions with employers and the Fund, the Actuary will declare results allowing for short-term pay restraint (1% per annum for three years) in his formal actuarial valuation report. Incorporating this adjustment has the effect of increasing the funding level at 31 March 2013 to 78% and reducing the deficit to £876m (liabilities fall to £4,023m from £4,152m).

5.3 The FSS provides flexibility for the Actuary to take affordability into account when setting contribution rates and deficit recovery payments. In this regard the Actuary has

(1) Phased in increases in deficit recovery payment increases over 3 years

(2) Phased in increases in future service rates over a maximum of 4 years

(3) Applied yield reversion where appropriate. This does not alter the deficit values but adjusts the repayment plan by taking forward an element of higher yields.

5.4 The main drivers of the valuation outcome are:

(1) The investment return over the 3 years to 31 March 2013 was 8.3% per annum compared to an expected return in the 2010 valuation of 6.1% p.a. This excess investment return reduced the deficit by c. £189m.

(2) The discount rate used to value the liabilities is based on real yields derived from the market. Compared to 2010 the nominal yield on long term UK gilts has fallen from 4.5% to 3.2% in 2013. This has been offset slightly by a fall in the inflation assumption from 3% in 2010 to 2.6% in 2013. The Asset Outperformance Assumption has remained unchanged at 1.6% which means the discount rate used to value liabilities has fallen from 6.1% in 2010 to 4.8% in 2013. Overall these changes in the financial assumptions have increased the liabilities by £635m.

(3) The fall in long term interest rates has also affected the future service rate (FSR). The Actuary uses a “smoothed” discount rate to value future accruals, in order to keep the FSR as stable as possible in line with the Regulations. This has been achieved over recent valuations. However, the significant fall in long term interest rates means the basis used by the Actuary does not sufficiently reflect market rates and thus the cost of on-going accrual. Therefore, the discount rate used to value future service has fallen from 6.75% in 2010 to 5.6% in 2013.

(4) At each valuation the actuary uses an analysis of the life expectancy experienced by the Fund, other LGPS funds and the improvement trend models from the Continuous Mortality Investigation to assess the adequacy of the 2010 longevity assumptions.

The longevity assumption is made up of two elements, the current life expectancy (or baseline assumption) and an assumption of future improvement / deterioration around the baseline assumption. The Actuary has altered the baseline assumption marginally for the 2013 valuation reflecting the updated membership information to include the Fund’s experience since 2010. In 2010 the assumption for the long term improvement rate was increased to 1.5% p.a. for valuing past service liabilities. The future accrual improvement assumption was maintained at 1% p.a. ahead of a new scheme being introduced and the expected cost control mechanism. However, LGPS experience has confirmed this is too low and the assumption has been increased to 1.5% for valuing future accruals in line with past service.

(5) In addition the Actuary has looked at life expectancy prior to retirement, ill health rates, retirement rates and the rate of dependants pensions coming into payment. Overall the demographic analysis decreased the past service liabilities by 0.8% and increased the future service rate by 0.6% of pay per annum. This includes the impact of changes made to the life expectancy assumptions (which in isolation were c.0.1% increase to past service liabilities and c.0.4% increase to the future service cost).

(6) Overall the changes in the financial and demographic assumptions have increased the FSR by 4.2%. This has been offset by savings from the new scheme of 1.7% at the Fund level, giving an overall average increase in the FSR of 2.5% of pensionable pay. This is before any allowance for the 50:50 option for members.

5.5 The changes are summarised in the following tables:

Changes to past service position since 2010 valuation

	£m
Deficit at 31 March 2010	**(552)**
Interest on deficit	(108)
Investment returns versus assumptions	189
Contribution paid versus benefits accruing	91
Salary gain (i.e. salary increases less than assumption)	52
Change in demographic assumptions	34
Change in financial assumptions	(635)
Member movement and other factors	(76)
Deficit at 31 March 2013	**(1,005)**

Changes to future service rate

Average Employer Rate at 31 March 2010	**11.8% of pay**
Change in membership profile	Neutral
Change in assumptions	+4.2% of pay
Impact of 2014 LGPS	-1.7% of pay
Average Employer Rate at 31 March 2013	**14.3% of pay**

6 COMMUNICATION WITH EMPLOYING BODIES

6.1 The 2013 actuarial report will be published by 31 March 2014. In the meantime, the employing bodies have been notified of their revised rates and officers are holding meetings with employers where required.

6.2 An Investments Forum was held on 22 November where the Actuary explained the results in greater detail.

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 EQUALITIES

8.1 An equalities impact assessment is not necessary.

9 CONSULTATION

9.1 This is reporting the outcome of a consultation process.

10 ISSUES TO CONSIDER IN REACHING THE DECISION

10.1 Are contained in the report.

11 ADVICE SOUGHT

11.1 The Council's Monitoring Officer (Divisional Director – Legal & Democratic Services) and Section 151 Officer (Divisional Director - Business Support) 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	Actuary reports and presentations
Please contact the report author if you need to access this report in an alternative format	