Non-Executive Report of the: **Pensions Committee** 29 November 2018	
Report of: Neville Murton, Acting Corporate Director of Resources	**Classification:** Unrestricted
Section 13 Valuation Results based on 31st March 2016 Triennial Valuation of Pension Schemes	

Originating Officer(s)	Bola Tobun, Investment and Treasury Manager
Wards affected	All wards

REASONS FOR URGENCY

The report was not published five clear days in advance of the meeting. Therefore, before this report can be considered at this meeting, the Chair would need to be satisfied that it is necessary to consider the Section 13 analysis completed by the Government Actuary's Department (GAD) using the 2016 valuations without that consideration being delayed to a later meeting. The Committee may also take the view that it is important that there is no delay in member oversight of the Section 13 analysis

Summary
This report provides Members with information on the Section 13 analysis completed by the Government Actuary's Department (GAD) using the 2016 valuations.

This is the first formal section 13 report, a 'Dry Run' was produced in respect of the 2013 valuations and published in 2016	The Government Actuary has been appointed by the Department of Communities and Local Government (DCLG) to report under section 13 of the Public Service Pensions Act 2013 in connection with the Local Government Pension Scheme ("LGPS" or "the Scheme") in England and Wales.
This report is based on the actuarial valuations of the 91 LGPS funds	Section 13 requires the Government Actuary (GAD) to report on whether the following aims are achieved: • compliance • consistency • solvency • long term cost efficiency
Significant progress has been made by a number of funds that were highlighted in the 2013 valuation dry run.	In aggregate, the LGPS is in a strong financial position and funds have made significant progress since the 2013 valuation. On GAD best estimate basis, the LGPS was in surplus in aggregate at 2016 (funding level approximately 106%), and around 60 of the 91 individual funds were in surplus. This means that GAD expect on average, a greater than 50% chance that existing assets would be sufficient to cover benefits in respect of accrued service when they fall due.
For this review Tower Hamlets Fund improved significantly, no amber or red flags.	For the 2013 dry run, Tower Hamlets Fund had two amber flags on solvency measures; asset shock and liability shock which basically indicate inability of employers to pay the required future and past contributions into the Fund.

Recommendations:
The Pensions Committee is recommended to note the content of this report.

1. REASONS FOR THE DECISIONS

1.1 The LGPS is a funded scheme and periodic assessments are needed to ensure the fund has sufficient assets to meet its liabilities. Employer contribution rates may change depending on the results of valuations. Scheme regulations set out when valuations are to be carried out.

1.2 Each LGPS pension fund is required to appoint its own fund actuary, who carries out the fund's valuation. The fund actuary uses a number of assumptions to value the liabilities of the fund. Liabilities are split between those that relate to the past (the past service cost), and those that relate to the future (the future service cost). The results of the valuation may lead to changes in employer contribution rates for both future and past service costs.

1.3 The report is based on the actuarial valuations of the 91 funds, with data provided by the funds and their actuaries, and a significant engagement exercise with affected funds. GAD is committed to preparing a section 13

report that makes practical recommendations to advance the reporting aims. Also expecting that their approach to section 13 will continue to evolve to reflect ever-changing circumstances and feedback received.

2. ALTERNATIVE OPTIONS

2.1 There are no alternative options.

3. DETAILS OF REPORT

3.1 The Government Actuary (GAD) has been appointed by the Ministry of Housing, Communities and Local Government (MHCLG) to report under section 13 of the Public Service Pensions Act 2013 in connection with the actuarial valuations of the 91 funds in the Local Government Pension Scheme in England and Wales ('LGPS' or 'the Scheme').

3.2 This is the first formal section 13 report, a 'Dry Run' was produced in respect of the 2013 valuations and published in 2016. Section 13 applies for the first time to the valuations as at 31 March 2016 and requires the Government Actuary (GAD) as the person appointed by MHCLG to report on whether the following four main aims are achieved:

a. **compliance**: whether the fund's valuation is in accordance with the scheme regulations

b. **consistency**: whether the fund's valuation has been carried out in a way which is not inconsistent with the other fund valuations within LGPS

c. **solvency**: whether the rate of employer contributions is set at an appropriate level to ensure the solvency of the pension fund

d. **long term cost efficiency**: whether the rate of employer contributions is set at an appropriate level to ensure the long term cost efficiency of the scheme, so far as relating to the pension fund.

3.2 Section 13 subsection (6) states that if any of the aims of subsection (4) are not achieved:

a) the report may recommend remedial steps

b) the scheme manager must:

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

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

c) the responsible authority may

iii) require the scheme manager to report on progress in taking remedial steps

iv) direct the scheme manager to take such remedial steps as the responsible authority considers appropriate

3.3 GAD looked at a range of metrics to identify potential issues in respect of solvency and long term cost efficiency. Each fund's score under each measure is colour coded or flagged, where:

a) **GREEN** - indicates that there are no material issues that may contribute to a recommendation for remedial action in order to ensure solvency or long term cost efficiency

b) **AMBER** - indicates a potential issue should be recognised, but in isolation would not usually contribute to a recommendation for remedial action in order to ensure solvency or long term cost efficiency

c) **RED** - indicates a potentially material issue that may contribute to a recommendation for remedial action in order to ensure solvency or long term cost efficiency

3.4 The trigger points for these flags are based on a combination of absolute measures and measures relative to the bulk of the funds in scope. Whereby GAD had regard to particular circumstances of some potential exceptions, following engagement with the administering authority and the fund actuary.

3.5 In total, 70 out of 89 funds tested had green flags on all solvency and long term cost efficiency metrics. This is a significant improvement compared with the previous dry run report (52 out of 90). There are a total of 20 amber and 2 red flags, which is again a significant improvement compared with the dry run (58 amber, 5 red).

3.6 The trigger points for these flags should not represent targets, these measures and flags helps GAD to determine whether a more detailed review is required, for example, we might have concern where multiple measures are triggered amber for a given fund.

3.7 In broad terms, amber flags are advisory signals that may indicate action and a need for further investigation through engagement with the relevant administering authority and their actuary. It should be noted that these flags are intended to highlight areas where risk may be present, or further investigation is required. Where an amber flag remains following that engagement, this then become an area of issue that administering authorities and pension boards should be mindful of. There is no implication that the administering authority was previously unaware of the issue.

3.8 A green flag (i.e. the absence of a red or amber flag) does not necessarily indicate that no risk is present and similarly the fact that the GAD are not specifically suggesting remedial action does not mean that scheme managers should not consider actions.

GAD findings on each of the four aims and their recommendations.

3.9 **Compliance** - GAD selected one Fund as a representative example from each of the firms of actuarial advisors. The review indicated that fund valuations were compliant with relevant regulations.

3.10 **Consistency** – GAD interpreted 'not inconsistent' to mean that methodologies and assumptions used, in conjunction with adequate disclosure in the report, should facilitate comparison by a reader of the reports. It is noted that readers

of the actuarial valuations face two difficulties in making meaningful comparisons between the reports:

a) presentational: information is presented in different ways in different reports (e.g. funding levels), and sometimes information is contained in some reports but not others (e.g. life expectancies), so readers may have some difficulties in locating the information they wish to compare. This is called presentational inconsistency

b) evidential: even when the reader has located the relevant information (e.g. funding levels), differences in the underlying methodology and assumptions mean that it is not possible to make a like-for-like comparison. This is called evidential inconsistency. GAD believe that local circumstances may merit different assumptions (e.g. financial assumptions are affected by the current and future planned investment strategy, different financial circumstances leading to different levels of prudence adopted). However, in some areas, it appears that the choice of assumptions is more dependent on the house view of the particular firm of actuaries advising the fund, than on the local circumstances of the fund.

3.11 There has been an improvement in consistency of presentation of contribution rates emerging from the 2016 valuations. However, despite this welcome improvement, inconsistencies remain, both presentational and evidential.

3.12 The recommendations are designed to:

a) encourage the presentation of results in a consistent way which is easy to understand and compare across the whole LGPS

b) move towards an assumption set that differs from one fund to another only where local conditions justify it, rather than being dependent on the house view of a particular actuarial advisor

3.13 **Solvency** – under this element, GAD tested the following five metrics:

- SAB funding level
- Open fund
- Non Statutory members
- Asset Shock
- Employer default

3.14 For open funds, solvency is dependent on employers being able to pay contributions as required, knowing that these contributions may increase or decrease significantly in future. Considering the LGPS as a whole, our long term expectation is that contributions will fall below their current levels as remaining deficits are paid off. However there is a significant chance that contributions remain at their current levels or even increase further in the long term, and in the short term there is always the risk that contributions need to increase or decrease following actuarial valuations.

3.15 At a fund level, GAD has expressed their stress tests in terms of the relative effects of an adverse stress to asset values on core spending power for English local authorities, and financing data for Welsh local authorities. They find that if asset values were to fall by 15%, then there is a range of impacts

on different funds and, on the basis of their assumptions, three funds could face increases in contribution over 3% of their core spending. Funds should be aware of this risk, and consider if any action should be taken to manage it. For the avoidance of doubt, GAD does not consider that this risk implies that the aims of section 13 are not achieved.

3.16 **Long term cost efficiency** – a series of relative and absolute considerations were developed to help assess whether the contributions met the aims of section 13 under long term cost efficiency. The below listed measures were used:

- Deficit Period
- Required Return
- Repayment Shortfall
- Return Scope
- Deficit Reconciliation

3.17 As set out in CIPFA's Funding Strategy Statement Guidance, GAD consider that the rate of employer contributions has been set at an appropriate level to ensure long term cost efficiency if it is sufficient to make provision for the cost of current benefit accrual, with an appropriate adjustment to that rate for any surplus or deficit in the fund.

3.18 It was evident that a number of funds highlighted in the Dry Run have made progress, with their employers increasing contributions following the 2016 valuation.

3.19 CIPFA's Funding Strategy Statement Guidance states "Administering authorities should avoid continually extending deficit recovery periods at each and subsequent actuarial valuations. Over time and given stable market conditions, administering authorities should aim to reduce deficit recovery periods." In the dry run, GAD established the deficit reconciliation measure so that funds could confirm that the deficit recovery plan can be demonstrated to be a continuation of the previous plan, after allowing for actual fund experience.

3.20 GAD considers that reconciliation of the deficit recovery plan is an important component of section 13 for all funds. Through this exercise, they identified and engaged with a number of funds that have extended their deficit recovery end points, but have not concluded that this implies the aims of section 13 are not achieved, however they do recommend that all funds review their funding strategy and consider whether this is in accordance with the CIPFA guidance referred to above.

Conclusion

3.21 In total, 70 out of 89 funds tested had green flags on all solvency and long term cost efficiency metrics. This is a significant improvement compared with the previous dry run report (52 out of 90). There are a total of 20 amber and 2 red flags, which is again a significant improvement compared with the dry run (58 amber, 5 red).

3.22 So good news for Tower Hamlets Fund no amber or red flags from this review, signifying significant improvement for our fund when compared to the 2013 dry run whereby Tower Hamlets Fund had two amber flags on solvency measures; asset shock and liability shock which basically underpinned inability of employers to pay the required future and past contributions into the Fund.

3.23 The Committee has to be mindful of this information when making decision on employer contributions. The valuation process for 31st March 2019 commences soon and the Committee would be required to make decisions and approve new contribution rates for Fund employers which would be effective from 1st April 2020 for the next three years up to 31st March 2023.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 There are no immediate finance implications arising from this report.

4.2 The employers' contribution rate for the London Borough of Tower Hamlets was set at 15.8% for 2013 valuation. This was increase to 19.9% as a result of the 2016 triennial review. The Council will still continue to pay this rate up until 31 March 2020. However the next valuation exercise will occur in March 2019 with the results taking effect from 1 April 2020, for the next three years. The outcome of this process could then have a positive or a negative impact on the general fund depending if there is a reduction or a rise to the level of contribution the Council has to pay to the Fund.

5. LEGAL COMMENTS

5.1 The Local Government Pension Scheme Regulations 2013, Regulation 62, requires an Administering Authority to obtain an actuarial valuation of its fund as at 31st March 2016, and as at 31st March every third year thereafter. The documents obtained by the administering authority must include a report by an actuary in respect of the valuation, and a rates and adjustments certificate provided by the actuary. The report must contain a statement of the demographic assumptions used in producing the valuation, and how these assumptions relate to events which have actually occurred in relation to the scheme membership. These documents must be received before the first anniversary of the valuation date.

5.2 Regulation 66 also requires the Administering Authority to supply copies of any valuation report, rates and contributions certificates to the Secretary of State, employing authorities participating in the Fund and any other bodies liable to make payments to it.

5.3 When exercising its functions, the Pensions Committee, must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who do not (the public sector duty).

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The Pension Fund Accounts demonstrate financial stewardship of the fund's assets. A financially viable and stable pension fund is a valuable recruitment and retention incentive for the Council.

7. BEST VALUE (BV) IMPLICATIONS

7.1 The level of funding for the Pension Fund and the requirement to fund employee pension benefits, both past and current can directly impact on the level of resources available for other Council services. The valuation outcome is sensitive to both the actuarial and financial assumptions made within the valuation and any significant variations to those assumptions could impact upon Fund's financial position.

7.2 The understanding of the Pension Fund in terms of its investments, the Fund's liabilities both short and long term and the profile of its members between actuarial valuations determines the financial status of the pension fund, its funding level and the contributions that employers need to make into the Fund for the following three years.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 The valuation outcome is sensitive to both the actuarial and financial assumptions made within the valuation and any significant variations to those assumptions could impact upon Fund's financial position. Therefore a prudent approach is crucial in minimising the key risks involved in managing the Pension Fund.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no any Crime and Disorder Reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- NONE

Appendices

- Appendix 1 – Standardising Local Valuation Results
- Appendix 2 – Section 13 Review of the Actuarial Valuations of Funds as at 31 March 2016

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report

- As shown in appendices above.

Officer contact details for documents:
Bola Tobun(Investment & Treasury Manager) x4733

Appendix 1

Chart B1: Standardising Local Valuation Results

2016 LOCAL BASES		SAB STANDARD BASIS	
103.4%	ENVIRONMENT AGENCY ACTIVE	BARKING AND DAGENHAM	N/A
103.0%	KENSINGTON AND CHELSEA	ENVIRONMENT AGENCY ACTIVE	122.6%
101.0%	WANDSWORTH	SOUTH YORKSHIRE TRANSPORT	121.0%
100.4%	TEESSIDE	WEST SUSSEX	120.3%
96.7%	DYFED	KENSINGTON AND CHELSEA	116.0%
96.0%	LDN PENSIONS FUND AUTHORITY	WANDSWORTH	116.0%
95.0%	WEST SUSSEX	WEST MIDLANDS TRANSPORT	111.0%
94.0%	MERTON	CHESHIRE	110.0%
93.8%	WEST YORKSHIRE	GWYNEDD	109.9%
93.8%	BEXLEY	ISLE OF WIGHT	109.3%
92.7%	GREATER MANCHESTER	EAST SUSSEX	108.8%
92.0%	EAST SUSSEX	SUFFOLK	108.7%
91.5%	ISLE OF WIGHT	HERTFORDSHIRE	107.3%
91.4%	BROMLEY	DYFED	106.8%
91.4%	HERTFORDSHIRE	BROMLEY	106.3%
91.3%	GWYNEDD	TEESSIDE	105.9%
91.1%	SUFFOLK	GREATER MANCHESTER	105.5%
91.0%	RICHMOND	RICHMOND	105.0%
91.0%	GREENWICH	CUMBRIA	104.9%
90.7%	CUMBRIA	EAST RIDING	104.6%
90.0%	NORTH YORKSHIRE	BEXLEY	103.0%
90.0%	OXFORDSHIRE	DERBYSHIRE	103.0%
89.9%	CHESHIRE	WARWICKSHIRE	101.7%
89.7%	LANCASHIRE	WEST YORKSHIRE	101.7%
89.0%	ESSEX	NORTH YORKSHIRE	100.7%
89.0%	KENT	LANCASHIRE	99.3%
89.0%	SOUTH YORKSHIRE TRANSPORT	ENFIELD	98.7%
88.0%	HAMMERSMITH AND FULHAM	NORFOLK	98.6%
87.9%	EAST RIDING	LAMBETH	98.6%
87.8%	SOUTHWARK	SOUTH YORKSHIRE	98.5%
87.4%	ENFIELD	MERSEYSIDE	97.8%
87.0%	BUCKINGHAMSHIRE	ESSEX	97.0%
87.0%	NOTTINGHAMSHIRE	TYNE AND WEAR	96.7%
86.7%	DERBYSHIRE	KINGSTON UPON THAMES	96.7%
85.9%	SOUTH YORKSHIRE	WILTSHIRE	96.6%
85.8%	AVON	STAFFORDSHIRE	96.3%
85.5%	TYNE AND WEAR	MERTON	96.0%
84.8%	MERSEYSIDE	LDN PENSIONS FUND AUTHORITY	96.0%
84.6%	CARDIFF AND GLAMORGAN	AVON	95.9%
84.5%	SHROPSHIRE	NORTHUMBERLAND	95.8%
84.0%	CITY OF LONDON	SOUTHWARK	95.5%
84.0%	DEVON	SURREY	95.1%
84.0%	HOUNSLOW	WEST MIDLANDS	95.0%
84.0%	NEWHAM	HACKNEY	94.9%
83.6%	NORTHUMBERLAND	GLOUCESTERSHIRE	94.7%
83.0%	DORSET	CAMBRIDGESHIRE	94.3%
82.8%	TOWER HAMLETS	WESTMINSTER	94.0%
82.6%	SURREY	OXFORDSHIRE	94.0%
82.3%	WARWICKSHIRE	LEWISHAM	94.0%
82.0%	WEST MIDLANDS TRANSPORT	CAMDEN	93.8%
81.7%	KINGSTON UPON THAMES	HARINGEY	93.5%
81.5%	WILTSHIRE	TOWER HAMLETS	93.4%
81.4%	DURHAM	NORTHAMPTONSHIRE	93.1%
81.1%	RHONDDA CYNON TAF	KENT	93.0%
81.0%	WEST MIDLANDS	LINCOLNSHIRE	92.8%
80.8%	HAMPSHIRE	CARDIFF AND GLAMORGAN	92.8%
80.4%	REDBRIDGE	RHONDDA CYNON TAF	92.3%
80.3%	NORFOLK	LEICESTERSHIRE	92.1%
80.0%	EALING	HAMMERSMITH AND FULHAM	92.0%
80.0%	WESTMINSTER	GREENWICH	92.0%
80.0%	SUTTON	SHROPSHIRE	91.4%
79.9%	LAMBETH	HAMPSHIRE	91.2%
79.8%	SWANSEA	REDBRIDGE	91.0%
79.7%	GLOUCESTERSHIRE	HARROW	91.0%
79.6%	POWYS	CORNWALL	90.9%
79.1%	HARINGEY	POWYS	90.2%
78.5%	CAMBRIDGESHIRE	DURHAM	90.1%
78.4%	ISLINGTON	NOTTINGHAMSHIRE	90.0%
78.4%	NORTHAMPTONSHIRE	BUCKINGHAMSHIRE	89.0%
78.4%	LEWISHAM	EALING	88.2%
78.0%	STAFFORDSHIRE	NEWHAM	88.0%
77.2%	BARKING AND DAGENHAM	HILLINGDON	87.8%
77.0%	HACKNEY	GWENT	86.8%
77.0%	SOMERSET	CLWYD	86.0%
76.9%	LINCOLNSHIRE	DEVON	86.0%
76.2%	CAMDEN	DORSET	86.0%
76.2%	LEICESTERSHIRE	SUTTON	86.0%
76.0%	CLWYD	SWANSEA	85.8%
75.2%	CORNWALL	ISLINGTON	85.4%
75.1%	HILLINGDON	HOUNSLOW	85.0%
74.9%	WORCESTERSHIRE	WORCESTERSHIRE	84.4%
74.3%	HARROW	CITY OF LONDON	84.0%
73.0%	BERKSHIRE	BEDFORDSHIRE	82.5%
73.0%	BARNET	BARNET	82.0%
72.9%	CROYDON	CROYDON	80.6%
72.2%	GWENT	SOMERSET	80.0%
70.8%	BEDFORDSHIRE	HAVERING	78.3%
69.8%	WALTHAM FOREST	WALTHAM FOREST	76.8%
68.8%	HAVERING	BERKSHIRE	72.0%
54.6%	BRENT	BRENT	66.3%
30.8%	ENVIRONMENT AGENCY CLOSED	ENVIRONMENT AGENCY CLOSED	37.7%