Pensions Committee

Thursday, 25 March 2021 at 6.00 p.m.

Online 'Virtual' Meeting - https://towerhamlets.public-i.tv/core/portal/home

Agenda

Chair: Councillor Krysten Perry

Members

Vice-Chair: Councillor Rachel Blake

Councillor Ayas Miah, Councillor Helal Uddin, Councillor Puru Miah, Councillor David Edgar and Councillor Andrew Wood

Observers (Independent Persons):
Kehinde Akintunde ((GMB Union Representative)), Colin Robertson (Independent Investment Advisor (Pensions Committee)) and Steve Turner (Mercers - Senior Investment Consultant)

Substitutes:
Councillor Faroque Ahmed, Councillor Kevin Brady, Councillor Gabriela Salva Macallan and Councillor Peter Golds

[The quorum for the Pensions Committee is 3 Members]

Further Information

Reports for consideration, meeting contact details, public participation and more information is available on the following pages.

Public Information

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London Borough of Tower Hamlets

Pensions Committee

Thursday, 25 March 2021

6.00 p.m.

6. EXCLUSION OF THE PRESS AND PUBLIC

In view of the contents of the remaining items on the agenda the Committee is recommended to adopt the following motion:

"That, under the provisions of Section 100A of the Local Government Act 1972, as amended by the Local Government (Access to Information) Act 1985, the press and public be excluded from the remainder of the meeting for the consideration of the Section Two business on the grounds that it contains information defined as Exempt in Part 1 of Schedule 12A to the Local Government Act, 1972."

EXEMPT SECTION (Pink Papers)
The exempt committee papers in the agenda will contain information, which is commercially, legally or personally sensitive and should not be divulged to third parties. If you do not wish to retain these papers after the meeting, please post them to the Democratic Service Office, 1st Floor, Mulberry Place London E14 3BG or hold onto the papers until such time you can return to the Town Hall and dispose of the papers in the confidential bins.

7. TRAINING EVENTS

8. RESTRICTED MINUTE(S) OF THE PREVIOUS MEETING(S) 429 - 446

To confirm as a correct record the restricted minutes of the meetings of the Committee held on 19th November 2020 and 9th December 2020.

9. ANY OTHER BUSINESS CONSIDERED TO BE URGENT

Next Meeting of the Committee:
Date Not Specified at Time Not Specified to be held in the Online 'Virtual' Meeting - https://towerhamlets.public-i.tv/core/portal/home

DECLARATIONS OF INTERESTS AT MEETINGS– NOTE FROM THE MONITORING OFFICER

This note is for guidance only. For further details please consult the Code of Conduct for Members at Part C, Section 31 of the Council's Constitution

(i) Disclosable Pecuniary Interests (DPI)

You have a DPI in any item of business on the agenda where it relates to the categories listed in **Appendix A** to this guidance. Please note that a DPI includes: (i) Your own relevant interests; (ii)Those of your spouse or civil partner; (iii) A person with whom the Member is living as husband/wife/civil partners. Other individuals, e.g. Children, siblings and flatmates do not need to be considered. Failure to disclose or register a DPI (within 28 days) is a criminal offence.

Members with a DPI, (unless granted a dispensation) must not seek to improperly influence the decision, must declare the nature of the interest and leave the meeting room (including the public gallery) during the consideration and decision on the item – unless exercising their right to address the Committee.

DPI Dispensations and Sensitive Interests. In certain circumstances, Members may make a request to the Monitoring Officer for a dispensation or for an interest to be treated as sensitive.

(ii) Non - DPI Interests that the Council has decided should be registered – (Non - DPIs)

You will have 'Non DPI Interest' in any item on the agenda, where it relates to (i) the offer of gifts or hospitality, (with an estimated value of at least £25) (ii) Council Appointments or nominations to bodies (iii) Membership of any body exercising a function of a public nature, a charitable purpose or aimed at influencing public opinion.

Members must declare the nature of the interest, but may stay in the meeting room and participate in the consideration of the matter and vote on it **unless:**

- A reasonable person would think that your interest is so significant that it would be likely to impair your judgement of the public interest. **If so, you must withdraw and take no part in the consideration or discussion of the matter.**

(iii) Declarations of Interests not included in the Register of Members' Interest.

Occasions may arise where a matter under consideration would, or would be likely to, **affect the wellbeing of you, your family, or close associate(s) more than it would anyone else living in the local area** but which is not required to be included in the Register of Members' Interests. In such matters, Members must consider the information set out in paragraph (ii) above regarding Non DPI - interests and apply the test, set out in this paragraph.

Guidance on Predetermination and Bias

Member's attention is drawn to the guidance on predetermination and bias, particularly the need to consider the merits of the case with an open mind, as set out in the Planning and Licensing Codes of Conduct, (Part C, Section 34 and 35 of the Constitution). For further advice on the possibility of bias or predetermination, you are advised to seek advice prior to the meeting.

Section 106 of the Local Government Finance Act, 1992 - Declarations which restrict Members in Council Tax arrears, for at least a two months from voting

In such circumstances the member may not vote on any reports and motions with respect to the matter.

Further Advice contact: Janet Fasan, Director of Legal and Monitoring Officer, Tel: 0207 364 4800.

APPENDIX A: Definition of a Disclosable Pecuniary Interest

(Relevant Authorities (Disclosable Pecuniary Interests) Regulations 2012, Reg 2 and Schedule)

Subject	Prescribed description
Employment, office, trade, profession or vacation	Any employment, office, trade, profession or vocation carried on for profit or gain.
Sponsorship	Any payment or provision of any other financial benefit (other than from the relevant authority) made or provided within the relevant period in respect of any expenses incurred by the Member in carrying out duties as a member, or towards the election expenses of the Member. This includes any payment or financial benefit from a trade union within the meaning of the Trade Union and Labour Relations (Consolidation) Act 1992.
Contracts	Any contract which is made between the relevant person (or a body in which the relevant person has a beneficial interest) and the relevant authority— (a) under which goods or services are to be provided or works are to be executed; and (b) which has not been fully discharged.
Land	Any beneficial interest in land which is within the area of the relevant authority.
Licences	Any licence (alone or jointly with others) to occupy land in the area of the relevant authority for a month or longer.
Corporate tenancies	Any tenancy where (to the Member's knowledge)— (a) the landlord is the relevant authority; and (b) the tenant is a body in which the relevant person has a beneficial interest.
Securities	Any beneficial interest in securities of a body where— (a) that body (to the Member's knowledge) has a place of business or land in the area of the relevant authority; and (b) either— (i) the total nominal value of the securities exceeds £25,000 or one hundredth of the total issued share capital of that body; or (ii) if the share capital of that body is of more than one class, the total nominal value of the shares of any one class in which the relevant person has a beneficial interest exceeds one hundredth of the total issued share capital of that class.

LONDON BOROUGH OF TOWER HAMLETS

MINUTES OF THE PENSIONS COMMITTEE

HELD AT 6.00 P.M. ON THURSDAY, 19 NOVEMBER 2020

ONLINE 'VIRTUAL' MEETING - HTTPS://TOWERHAMLETS.PUBLIC-I.TV/CORE/PORTAL/HOME

Members Present:

Councillor Rachel Blake – Vice-Chair in the Chair
Councillor Helal Uddin
Councillor Abdal Ullah
Councillor Andrew Wood

Union and Admitted Bodies, Non-Voting Members Present:

Kehinde Akintunde	GMB Union Representative
Colin Robertson	Independent Advisor
Steve Turner	Mercer

Others Present:

John Jones	– Chair of Pensions Board
Sam Yeandle	– Mercer

Officers Present:

Miriam Adams	– Interim Pensions and Investment Manager
Ngozi Adedeji	– (Principal Lawyer Civil Litigation, Governance)
Kevin Bartle	– (Interim Divisional Director of Finance, Procurement and Audit)
Farhana Zia	– (Democratic Services Officer, Committees, Governance)

APOLOGIES FOR ABSENCE

Apologies for absence were received from the Chair of the Pensions Committee, Councillor Kyrsten Perry and Councillor Puru Miah.

1. DECLARATIONS OF INTERESTS

There were no declarations of pecuniary interests made by members of the meeting.

2. APPOINTMENT OF VICE-CHAIR

Councillor Rachel Blake put herself forward for the position of the Vice-Chair. This was seconded by Councillor Abdal Ullah and Councillor Helal Uddin.

No further nominations were made.

The Pensions Committee **RESOVLED** to:

1. Elect Councillor Rachel Blake as the Vice-Chair of the Pensions Committee for 2020-21.

The Vice-Chair was in the Chair for this meeting.

3. MINUTES OF THE PREVIOUS MEETING(S)

The public and restricted minutes of the meeting held on the 22nd September 2020 were agreed and approved be to an accurate record of the meeting.

4. PETITIONS

No Petitions relating to the matters for which the Committee is responsible had been received by Officers.

5. SUBMISSIONS / REFERRALS FROM PENSION BOARD

Mr John Jones, Chair of Pensions Board presented his report stating the Pensions Board had met on the 13th October 2020 and were due to meeting again on the 16th November 2020. However, the 16th November meeting had been cancelled. He said he hoped to ensure future meetings of the Board would follow the previous timetable, by meeting a few days before the Committee.

Mr Jones said the Board at its October meeting had considered some of the same reports that had been presented to the Pensions Committee. Mr Jones said it had been updated on the current position with the Pensions Administration service and the progress being made to implement the new staffing structure. He said concern had been expressed that the new staffing structure was not being implemented as quickly as intended. He said the Board were advised the Council's internal procedures accounted for some of the delays in recruitment. He said the Board fully supported the new structure and action being taken but were concerned over the problems being encountered. Mr Jones requested the Committee to review and monitor progress in implementing the new staffing structure, and to support officers in ensuring that the new structure was implemented as quickly as possible.

Mr Jones stated the other areas of discussion had been the draft Pension Accounts for 2019/20 and questions around the management expense of the Fund. He said this had to be disclosed and this was a welcomed improvement to understanding the costs of investment managers and should be reviewed on a regular basis, in the future.

Mr Jones continued stating Board Members were concerned with the Voting and Engagement arrangements of the Fund's investment. He said this related to the practice of managers and London CIV voting in accordance with Tower Hamlets policy, as recommended by the LAPFF. Mr Jones said this was an issue the Pension Board would look at more closely in the future, to understand fully why the recommendations are not always followed through and if reasons are clearly stated when there is a divergence from the Tower Hamlets policy.

In response to questions from Members the following was noted:

- Mr Jones said when they discussed the Voting and Engagement paper, it was not clear from the columns and recommendations why the managers had departed from Tower Hamlets policy. Mr Jones said it was a case of understanding why this was, especially as London CIV would be playing a bigger role in the future of the Fund's investments. He said clearer policies and feedback was required.
- Ms Miriam Adams, Interim Pensions and Investments Manager added she had struggled to get information from the London CIV. She said they were the fund managers however behind them were investment managers which the Council no longer had direct access to. Ms Adams said previously they could ask for individual reports and as such this had been raised with the London CIV. Ms Adams said she was a member of the group looking at Responsible Investments and the issue of voter engagement as well as climate change was on the agenda. She said because the fund is a pooled fund, inevitably individual councils lose the ability to determine how votes are cast. She said the London CIV was hoping to develop critical mass in the future, on how council views are reflected in voting
  - **ACTION:** The Vice-Chair requested a report to be presented to the Pensions Board and Committee on this issue, with examples and reasons as to why and how issues are voted on.

The Vice-Chair thanked Mr Jones for his update.

6. REPORTS FOR CONSIDERATION

6.1 Pensions Committee Terms of Reference, Membership, Quorum and Dates of Meetings

The Vice-Chair referred members to the Pension Committee Terms of Reference, Membership, Quorum and Dates of meeting and said these were for noting following the Council AGM held on the 30th September 2020.

She said in the printed pack, Appendix 1 the terms of reference were missing however they were on the Council website. Councillor Blake said the terms of reference needed to be revised and refreshed before being bought back to the March 2021 meeting.

- **ACTION:** The Interim Pensions and Investments Manager, Ms Adams to bring the revised Terms of Reference to the March 2021 Committee meeting.

The Pensions Committee **RESOLVED** to:

1. Note the Terms of reference report and dates of meeting for the Pensions Committee and requested the updated terms of reference be presented at the March 2021 meeting.

6.2 Carbon Foot-Print Audit

Ms Miriam Adams, Interim Pensions and Investments Manager introduced the report and said it summarised the Fund's carbon footprint analysis, quantification of the Fund's decarbonisation progress of the listed equity portfolio of the Fund. She said the Fund had made strong decarbonisation progress since 2017 when it divested from GMO Global Equities and invested in LGIM Low Carbon Equities.

Ms Adams referred members to paragraph two of the report which detailed the reasons why investments needed to be climate friendly. In particular, she referred members to the diagram on page 35 of the agenda and said this illustrated the transition and pathways of the current policies and the direction of travel for climate change generally. Ms Adams highlighted the information at paragraph 2.2, which provided the Global and European Regulations and paragraph 2.3 which outlined the UK Government decision to declare a climate emergency and a commitment to become a carbon-neutral economy by 2050.

Reference was made to paragraph three and the next steps outlined. Ms Adams said the Committee needed to consider and agree a broad strategy in respect to a climate change strategy which was inclusive of the short-term decarbonisation targets to 2025 and 2030 and a commitment to net zero emissions by 2050.

The following comments were made by Members:

- Concern was expressed regarding the cost implication of commissioning such analysis and the impact on officer workload. Members stated this information was useful if it was to be used for decision making in the next twelve to eighteen months but feared the exercise would need to be repeated, if action was not taken in a timely way.
- The Vice-Chair, Councillor Blake said there were a few errors within the report which should be clarified for the record.
    - She referenced page 33 of the agenda (page 1 of the report) and the fourth paragraph of the summary. Councillor Blake said the sentence should read "Overall, carbon intensity (WACI) of the listed equity portfolio decreased **by** 29% …" and not "decreased is"
    - She also referenced page 34 of the agenda (page 2 of the report) and said under paragraph 1.1 the word should read **"exception"** and not "expectations".
- Further to the corrections, Councillor Blake suggested the 3rd recommendation on page 34 of the agenda be amended to state the driver for the change was due to the Council's fiduciary duty. She suggested the

recommendation be re-worded and said the decarbonisation targets should be at least 2025 and 2030 and the commitment to zero emissions should be 2040.

The Pensions Committee **RESOLVED** to:

1. Note the contents of this report;
2. Note the reduction in carbon footprint from 2017 to 31 March 2020;
3. **In order to meet the fiduciary duty of the Council,** agreed to put in place a climate change strategy, inclusive of short-term decarbonisation targets to **at least** 2025 and 2030, and a commitment to net zero emissions by **2040** to align thinking with the Climate Emergency declared by the Council and the UK Climate Change Act 2008;
4. Agreed the adoption of the recommendations of the Task Force on Climate – Related Financial Disclosures (TCFD), to further embed climate led investment thinking. Analysis in will help the Fund to adopt and disclose according to TCFD recommendations (Metrics & Targets);
5. Agreed conducting climate change scenario analysis as per the TCFD recommendations to help the Fund to better understand climate change risks and opportunities that arise, both from the transition to a low carbon economy and physical damages; and
6. Agreed to expanding the scope in measuring climate change investment risk across the entire portfolio.

The Vice-Chair summarised the Committee would receive a further paper at the next meeting on what these changes would look like. She also questioned why the appendix was a restricted item and was informed that all Mercer papers come with a disclaimer and therefore it was restricted.

6.3 Independent Investment Adviser Update - Q2

Mr Colin Robertson, Independent Adviser to the Pensions Committee presented his quarterly update. He said the report had been deferred at the last meeting and therefore he would be providing an update from March to date, including quarter 3.

Mr Robertson said there had been a consistent trend since the markets collapsed at the end of March. He said equity markets were performing strongly. While the prediction for economic growth had been horrendous, actual economic growth had not been typically worse than anticipated and was sometimes better. Mr Robertson said that with news of producing an effective vaccine for COVID, equity markets were more stable.

Mr Robertson said the real driver for equity market returns had continued to be technology and technology enabled growth stock such as Apple, Amazon and TESLA. He said this had led to ‘growth’ stocks outperforming ‘value’ stocks. He said the Council’s active equity portfolio was full of this type of stock and Ballie Gifford had outperformed their benchmark by 20% over the last year. However, Mr Robertson cautioned this would be more challenging in the future and some correction in performance might be expected, especially given this was a narrow group of stock.

Mr Robertson said there remained considerable uncertainty, because it was unclear how effective the vaccines developed would be and if individuals would take them. He said the economy was being supported by aggressive fiscal policies and these could not be sustained indefinitely. He questioned what would happen to consumer spending post government support.

With reference to bonds, Mr Robertson said these were being bought by Central Banks and therefore prices had been fairly stable. The Property market remained uncertain and therefore it was difficult to form a view on its performance from an unknown starting point.

In relation to managers, Mr Robertson said some had performed badly in the first quarter, but performance had improved. Mr Robertson expressed his concerns relating to the London CIV. He said it was positive that senior positions had been filled however more junior staff were still required. In addition, Mr Robertson said he had some reservation as to how much the London CIV could do themselves and questioned if they were being too ambitious.

In response to questions from members the following was noted:

- Mr Robertson said it was very hard to know what the true price for property was and it was difficult to sell when the price was unknown. Mr Robertson said normally property assets shouldn’t be sold when the price cannot be established. On the positive side, the property portfolio does offer some inflation protection and does produce income.

The Vice-Chair thanked Mr Robertson for this update.

6.4 McCloud Remedy Consultation Response

Ms Miriam Adams, Interim Pensions and Investments Manager presented this report stating this was a deferred report from the last Pensions meeting. She said it related to the key changes being proposed by Government following a recent consultation document in response to the McCloud judgement concerning age discrimination.

Ms Adams said the courts had determined that the protections afforded to some members of the LGPS and other public service pensions schemes were age discriminatory and unlawful. Ms Adams referred members to paragraphs 3.10 onwards which set out the implications for the Tower Hamlets Fund.

Members had no questions in relation to this item.

6.5 Administration and LGPS Recent Update

Ms Miriam Adams, Interim Pensions and Investments Manager stated the report provided an update on the administration and performance of the Fund since the July 2020 meeting and the key recent LGPS issues and initiatives which impact the Fund.

She referred members to paragraph 4.2 and said the Council had outsourced catering and cleaning services in schools and the Pensions Team had been working alongside new employers. Ms Adams said several tenders were in the pipeline and she hoped to provide an update at the March 2021 meeting.

Ms Adams referred members to paragraph 6.1 and said the £95K cap came in effect as of 4th November 2020. She said the LGPS regulations needed to be updated. Ms Adams said this would affect high earners but also those with long service. She said ill health was not affected by the cap. Ms Adams said there were several grey areas that needed to be resolved. Ms Adams continued saying guidance was required on how to deal with this, however she had a meeting with the Actuary, to help understand the complexity of the cap.

Ms Adams then provided updates in relation to paragraph seven onwards.

Mr Kevin Bartle, Interim Divisional Director for Finance, Procurement and Audit provided an update regarding the issue with staffing, that had been highlighted by Mr John Jones, the Chair of the Pensions Board. Mr Bartle informed members the recruitment of staff had been slow and time consuming however additional members of staff had been recruited. Mr Bartle said they would share with the Committee the update that had been provided to the Pensions Board. He said he'd like to provide some comparative data looking at the progress made over the last twelve months.

- **ACTION:** Ms Adams to circulate the information relating to staffing, with members of the Pensions Committee by end of next week. i.e. 27th November 2020.

In response to questions from members the following was noted:

- Ms Kehinde Akintunde, Trade Union Representative stated the £95K cap was causing considerable anxiety amongst staff and members of the trade union, especially given the backdrop of ongoing restructuring and reviews. Ms Akintunde asked if local guidance could be provided in respect to the deferment of pensions and its impact. Ms Akintunde said the trade unions had instigated a Judicial Review against the £95k cap.
- In response, Ms Adams stated there was a distinction to be drawn between the Fund and the Council as an employer. She said from a Fund perspective it was dealing with the administration of members' pensions after the employer had made a decision whereas from an employer perspective, there was a duty to manage the impact this cap

would have on employees. She said she was aware the issue was subject to a judicial review and would be taking legal advice on the matter. Mr Bartle added the Fund and the Committee's role related to the administration side of the pension fund and whilst this would have a big impact on employees there were a whole series of questions that remained unanswered.

- o **ACTION:** Ms Adams was requested to provide information and guidance on how locally the £95K cap is being administered, regardless of the role of the Pension Committee and the General Purposes Committee.

- In response to staff being TUPE to new employers, Ms Akintunde said this would be occurring in January 2021.
- Ms Adams clarified performance figures were reported at the July 2020 meeting however she would circulate again, as requested.

- o **ACTION:** Ms Miriam Adams, Interim Pensions and Investments Manager to provide committee members with the performance data relating to quarter two.

The Pensions Committee **RESOLVED** to:

1. Note the report contents; and
2. Note that three employers are in the process of joining the scheme – Taylor Shaw Cleaning, Ridgecrest Cleaning and Atlantic Cleaning following successful joint tender process involving a number of primary and secondary schools include Ian Mikado Academy.

6.6 Real Estate Investment Manager Presentation

Mr Jack Bladon and Mr Patrick Bone from Schroders gave a presentation on the Real Estate Portfolio.

The presentation covered how the Real Estate markets were performing and the effect the pandemic has had on the market. In addition to this the presentation provided members with an update on the Real Estate portfolio managed by Schroders on behalf of Tower Hamlets, which is valued at £158M and is invested in various property funds; and Environmental Social and Governance (ESG) factors.

- The impact of COVID has been unprecedented. Businesses have ceased trading for the lockdown period and Landlords have had to deal with this in a pragmatic way, working with the tenants by deferring rent until next year or offering rent free periods for longer leases. Retail and Leisure sectors have been hit hard.
- The valuation of property had been difficult, with valuers adding 'material uncertainty clauses' as they could not rely on the market evidence to accurately value property. Funds were suspended and redemptions deferred in the initial months of the pandemic. However, the good news is that the 'material uncertainty' clauses have now been removed on the underlying Funds in which Tower Hamlets invests.

- The forecast for the total returns from Real Estate will be minus five to eight percent this year although there is expected to be a bounce back next year.
- The portfolio is valued at £158m based on £15bn of underlying real estate assets. Referring to the pie charts, the fund has a lot of diversification by style and manager and this is considered a benefit.
- Statistical information was shared with members regarding the performance of the underlying Real Estate funds.
- The property markets have had a turbulent year, with performance especially bad in the Retail sector. However there has been a better performance from industrials where the fund is well positioned and where the fund is looking to invest going forward.
- ESG has been incorporated into the investment process. As an investment desk they had received an internal accreditation from Schroders stating they had fully incorporated ESG into their investment process. This is achieved by meeting with their underlying managers every quarter and bi-annually asking the managers to complete a sustainability survey. An example was given of ESG in practice.

In response to questions from Members the following was noted:

- Alternatives referred to non-retail, industrials or office and included areas such as student accommodation and healthcare. These were preferred areas for investment because demand is driven by long-term demographic changes as opposed to the economic cycle.
- The distinction between warehouses and retail warehouses is that warehouses have seen strong growth especially with online shopping whereas retail warehouses, those on the outskirts of towns, whilst faring better than the High Street, have seen values fall quite aggressively.
- In terms of income return, Schroders expected this to be down by 15 to 30% this year. They said there had been a fall in income returns because of the difficulties in collecting rent in some sectors. Some areas had been resilient such as industrials and office whereas retail and hospitality had really struggled.
- In reference to performance, Schroders acknowledged they were mandated to achieve 0.75% above the benchmark and this had not been achieved in recent years. Mr Bone said that to achieve the target return they would need to take more risk and invest more in specialist and less in core funds.
- o **ACTION:** Schroders to liaise with Ms Miriam Adams about their ESG plans going forward.

The Vice-Chair thanked Mr Bladon and Mr Bone for their presentation.

7. EXCLUSION OF THE PRESS AND PUBLIC - RESTRICTED SESSION 1 (MEMBERS, COOPTEES & OFFICERS)

The Vice-Chair **MOVED** and it was:

RESOLVED:

"That, under the provisions of Section 100A of the Local Government Act 1972, as amended by the Local Government (Access to Information) Act 1985, the press and public be excluded from the remainder of the meeting for the consideration of the Section Two business on the grounds that it contains information defined as Exempt in Part 1 of Schedule 12A to the Local Government Act, 1972."

7.1 Real Estate Mandate Review

The minute to this item is restricted.

7.2 Carbon Foot-Print Audit (appendix A restricted)

The minute for this item is restricted.

7.3 Responsible Investment (RI) and RI Accreditations

The minute for this item is restricted.

7.4 Sustainable Equity Investment Follow Up

The minute for this item is restricted.

8. TRAINING EVENTS

Councillor Blake expressed her thanks to officers for arranging the training session held in October 2020.

Ms Adams said she had emailed new members of the Committee, offering one to one training on Pension matters and was still waiting to hear back from them.

9. ANY OTHER BUSINESS CONSIDERED TO BE URGENT - LCIV MAC FUND VERBAL UPDATE

The minute for this item is restricted.

10. EXCLUSION OF THE PRESS AND PUBLIC - RESTRICTED SESSION 2 (MEMBERS & OFFICERS)

The Vice-Chair **MOVED** and it was:

RESOLVED:

"That, under the provisions of Section 100A of the Local Government Act 1972, as amended by the Local Government (Access to Information) Act 1985, the press and public be excluded from the remainder of the meeting for the consideration of the Section Two business on the grounds that it contains information defined as Exempt in Part 1 of Schedule 12A to the Local Government Act, 1972."

10.1 Contract Arrangement Review

The minute for this item is restricted.

The meeting ended at 8.59 p.m.

Vice-Chair in the Chair, Councillor Rachel Blake
Pensions Committee

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Non-Executive Report of the: **Pensions Committee** 25 March 2021	TOWER HAMLETS
Report of Kevin Bartle, Interim Corporate Director, Resources	**Classification:** Unrestricted
Action from Previous meeting - Review of Terms of Reference	

Originating Officer(s)	Miriam Adams, Head of Pensions & Treasury
Wards affected	All wards

SUMMARY

At the November 2020 meeting, the Committee requested a review of the Terms of Refence for the Committee. This report sets out the revised Terms of Reference for the information of Pensions Committee.

RECOMMENDATIONS

The Pensions Committee is recommended to:

- Note and comment on the revised Terms of reference (Appendix A);
- Approve the revised Terms of Reference;
- Recommend that the revised Terms of Reference is presented at the earliest possible Council meeting; and
- Note that the relevant sections of the Council's Constitution will be updated.

1. REASONS FOR NTHE DECISION

1.1 It is good practice to periodically review the terms of reference for the Committee to ensure it is fit for purpose. The terms of reference inform the Committee of its framework and is set out in the Council's Constitution.

2. DETAILS OF REPORT

2.1 At the meeting of the Pensions Committee held in November 2020, the Committee requested a review of its terms of reference to ensure it is fit for purpose.

2.2 As a statutory public service scheme, the Fund has a different legal status compared with trust-based schemes in the private sector. Although those making decisions relating to the Fund are required, in many ways, to act as if they were Trustees in terms of their duty of care, they are subject to a different legal framework and are not Trustees in the strict legal sense.

2.3 The revised terms of reference are appended to this report and shows changes in track. Changes include addition of ESG and risk management roles of the Committee.

3. COMMENTS OF THE CHIEF FINANCE OFFICER

3.1 There are no direct financial implications from this report.

4. LEGAL COMMENTS

4.1 The terms of reference are consistent with the legal framework and Part A, Section 10 of the Council's Constitution. Once approved by the Committee, it will be adopted by Council in accordance with Part A, Sections 7(a) and 7(d)

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5. OTHER STATUTORY IMPLICATIONS

5.1 This section of the report is used to highlight further specific statutory implications that are either not covered in the main body of the report or are required to be highlighted to ensure decision makers give proper consideration. Examples of other implications may be:

- Best Value Implications
- Consultations
- Crime Reduction
- Safeguarding
- Data Protection / Privacy Impact Assessment

5.2 Not applicable to this report.

6. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

6.1 The terms of reference of the Committee includes Environment Sustainable Governance which will have a positive and direct impact on Sustainable Action for a Greener Environment implication.

8. RISK MANAGEMENT IMPLICATIONS

8.1 There are no direct risk management impact arising from this report. However, by including risk management in its terms of reference the Committee ensures that risks inherence in the Pension Fund is delt with.

Linked Reports, Appendices and Background Documents

Linked Report

- None

Appendices

Appendix A – Revised Pensions Committee Terms of Reference.

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

Officer contact details for documents:

Miriam Adams, Interim Head of Pensions & Treasury
Tel: 0207 3644248
Email: Miriam.adams@towerhamlets.gov.uk

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Pensions Committee

Summary Description To consider pension matters and meet the obligations and the duties of the Council under the Superannuation Act 1972 and the various statutory requirements in respect of investment matters.	
Membership 7 Councillors, 1 representative of the Admitted Bodies and 1 Trade Union representative. The Admitted Body and Trade Union representatives will be non-voting members of the Committee. **Declaration of Interests:** Members of the Pensions Committee including co-opted members, are required to declare any interests that they have in relation to the Pension Fund or items on the agenda at the commencement of the meeting	
Functions	**Delegation of Functions**
1. To act as Trustees of the Council's Pension Fund, consider pension matters and meet the obligations and the duties of the Council under the Superannuation Act 1972, the Public Service Pensions Act 2013, and the various pensions' legislation. **2.** To make arrangements for the appointment of and to appoint suitably qualified pension fund administrators, actuaries, advisers, investment managers and global custodians and periodically to review those arrangements. **3.** To formulate and publish an Investment Strategy Statement. **4.** To set the overall strategic objectives for the Pension Fund, having taken appropriate expert advice, and to develop a medium term plan to deliver the objectives. **5.** To determine the strategic asset allocation policy, the mandates to be given to the investment managers and the performance measures to be set for them. **6.** To make arrangements for the triennial actuarial valuation, to monitor liabilities and to undertake any asset/liability and other relevant studies as	None

required. **7.** To monitor the performance and effectiveness of the investment managers and their compliance with the Investment Strategy Statement. **8.** To set an annual budget for the operation of the Pension Fund and to monitor income and expenditure against budget. **9.** To receive and approve an Annual Report and accounts on the activities of the Fund prior to publication. **10.** To make arrangements to keep members of the Pension Fund informed of performance and developments relating to the Pension Fund on an annual basis. **11.** To keep the terms of reference under review. **12.** To determine all matters relating to admission body issues. **13.** To review the Pension Fund's policy and strategy documents on a regular basis and review performance against the Fund's objectives within the business plan **14.** To maintain an overview of pensions training for Members. **15.** To ensure compliance with the LGPS Regulations, Codes of Practice or guidance issued by the Pensions Regulator and the National Scheme advisory Board as they apply to pension benefits and the payment of pensions and their day to day administration and to be responsible for any policy decisions relating to the administration of the scheme. **16.** Selection, appointment and termination of external Additional Voluntary Contribution (AVC) providers and reviewing performance. **17.** Approve policy on environmental, social and governance considerations and on the exercise of share voting rights.	

18. To review the risks inherent in the management of the Pension Fund. **19.** To consider any recommendations made or views expressed by the London Borough of Tower Hamlets Pensions Board.	
Quorum: 3 Members of the Committee	
Meetings: At least four times a year in the ordinary course of business and additional meetings may be arranged as required to facilitate work. Work for the year will be agreed with the Committee to include dedicated training sessions for Committee members.	
Additional Information: • Constitution Part D, Section 53 (Pensions Committee Meeting Procedure Rules)	

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PENSIONS COMMITTEE

Work Plan

March 2020/21 and Draft 2021/22

Date of Meeting	Items	Title of Report / Presentation
25 March 2021		
	1	Member Training – FSS and new changes
	2	Revised Funding Strategy Statement (FSS)
	3	Actuarial Funding Update December 20
	4	Report on Corporate Governance, Stewardship, Engagement & Share Voting
	5	Fund liquidity 2020/21 to 2022/23
	6	Quarterly Administrative Update and Key Performance Indicators and LGPS Update Report
	7	Quarterly Investment Performance Reporting and update on emerging /current issues • Report of Independent Adviser market and manager update • Whole Fund and manager quarterly performance • LIBOR Transition update
	8	Portfolio Update and LCIV Renewable Energy Suitability Advice • LCIV Renewable Energy fund suitability • UNPRI Paris Aligned Global Equities fund update • Sustainable Equities fund update
	9	Investment Strategy Statement (ISS) 2021
	10	TCFD implementation and Road Map
	11	Review of Pensions Committee Terms of Reference and work plan

DRAFT 2021/22 WORK PLAN

Date of Meeting	Items	Title of Report / Presentation
24 June 2021		
	1	Member Training – Governance
	2	Quarterly Administrative Update and Key Performance Indicators and LGPS Update Report
	3	2020/21 draft pension fund accounts, audit plan and annual report
	4	Report on Corporate Governance, Stewardship, Engagement & Share Voting
	5	Quarterly Investment Performance Reporting and update on emerging /current issues • Report of Independent Adviser market and manager update • Whole Fund and manager quarterly performance • LCIV updates
	6	Review of Fund Manager and Custodian Internal Controls
	7	Responsible Investment Policy Review
	8	Review of Additional Voluntary Contribution (AVC)
	9	Portfolio Update and Strategic Asset Allocation Changes
	10	Knowledge Assessment and training plan
23 September 2021		

	1	Member Training
	2	Pension Fund Accounts and Annual Report and Audit Plan
	3	Report on Corporate Governance, Stewardship, Engagement & Share Voting
	4	Quarterly Administrative Performance and LGPS Update Report
	5	Quarterly Investment Performance Reporting and update on emerging /current issues • Report of Independent Adviser market and manager update • Whole Fund and manager quarterly performance • Equity Protection Update • LCIV Updates
	6	Annual Carbon Footprint Audit
	7	Review of Governance Compliance
	8	Portfolio Update and Strategic Asset Allocation Changes
	9	Knowledge Assessment and training plan
25 November 2021		
	1	Member Training
	2	Pension Fund Accounts and Annual Report
	3	Report on Corporate Governance, Stewardship, Engagement & Share Voting
	4	Quarterly Administrative Performance and LGPS Update Report
	5	Quarterly Investment Performance Reporting and update on emerging /current issues

		• Report of Independent Adviser market and manager update • Whole Fund and manager quarterly performance • LCIV Updates
	6	LCIV Update and Development
	7	Annual Carbon Footprint Audit
	8	Review of Governance Compliance
	9	Quarterly Performance Reporting of Fund Managers and update on emerging /current issues
	10	Knowledge Assessment and training plan
24 March 2022		
	1	Member Training – triennial valuation
	2	Quarterly Investment Performance Reporting and update on emerging /current issues • Report of Independent Adviser market and manager update Whole Fund and manager quarterly performance
	3	Quarterly Administrative Update and Key Performance Indicators Report
	4	Review of Pension Fund Policy Statements
	5	Asset Liability Modelling
		Investment Strategy Statement
	6	Report on Corporate Governance, Stewardship, Engagement & Share Voting
	7	Pension Fund Audit Plan 2021/22

	8	Fund liquidity and Cash Flow 2022/23
	9	GMP Progress Report
	10	McCloud Progress
	11	Knowledge Assessment and training plan

Non-Executive Report of the: **PENSIONS COMMITTEE** **25 March 2021**	TOWER HAMLETS
Report of: Kevin Bartle, Interim Corporate Director, Resources	**Classification:** Unrestricted
Pension Fund Updated Funding Strategy Statement	

Originating Officer(s)	Miriam Adams, Interim Head of Pensions & Treasury
Wards affected	All

Summary

This report covers updates to the Funding Strategy Statement's termination policy and a new contributions flexibilities policy in light of the new Regulations that came into force on 23 September 2020. The Regulations require these policies to be included in the Funding Strategy Statement. The Committee received the draft Funding Strategy Statement (FSS) in September 2019 and final in June 2020 post employer consultation following completion of the triennial valuation. This draft updated FSS (Appendix 1) will be circulated to employers in the Fund and comments fed back to the Committee verbally during the meeting.

Recommendations:

Pensions Committee is recommended to:

1. Note the content of this report; and
2. Approve the revised Funding Strategy Statement as set out in Appendix A which includes the draft policy for 'Flexibility in Contribution Rates' and 'Deferred Debt Agreements.

1. REASONS FOR THE DECISIONS

1.1 Regulation 58 of the Local Government Pension Scheme (Administration) Regulations 2013 (as amended) together with the guidance issued by CIPFA provides the statutory framework from which the Administering Authority is required to prepare a Funding Strategy Statement (FSS).

1.2 Following consultation with such persons as it considers appropriate, prepare, maintain and publish a written statement setting out its funding strategy with all relevant interested parties involved with the fund – for example, local authority employers, admitted bodies, scheduled/resolution bodies.

1.3 The administering authority will prepare and publish its funding strategy by having have regard to:-

a. the guidance issued by CIPFA for this purpose; and

b. the Statement of Investment Principles (SIP) or investment strategy statement (ISS), whichever is appropriate.

1.4 The FSS will 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 or investment strategy statement.

1.5 The revised FSS should be completed and approved by the Pension Committee (or equivalent) prior to the completion of each valuation.

1.6 The Fund actuary must have regard to the FSS as part of the fund valuation process.

2. ALTERNATIVE OPTIONS

2.1 There is no alternative because there is a requirement for Members of the Pensions Committee to approve any significant changes to the Funding Strategy Statement and associated policies.

3. DETAILS OF REPORT

BACKGROUND INFORMATION

3.1 A number of regulatory changes came into force on 23 September 2020 (LGPS (Amendment No.2) Regulations 2020). These allow for more flexibilities with contributions both on exit from the Fund (via spreading of exit payments and allowing employers to remain in the Fund with no active members) and via interim contribution reviews between actuarial valuations in line with these Regulations, the Fund is required to include policies within its Funding Strategy Statement (FSS) which sets out how the flexibilities will apply in practice to employers. The Fund has therefore updated its Funding Strategy Statement to incorporate the new Regulations (the changes are set out on pages 9, 17 and 20 -24X in the attached FSS). These policies aim to provide much needed flexibilities to manage employer liabilities.

3.2 To assist with drafting the policies and applying the Regulations, the Scheme Advisory Board (SAB) produced a practical guide in draft form for Funds and the MHCLG issued draft statutory guidance on the amendments to the FSS.

3.3 At the time of writing this report, the draft revised FSS was issued to employers in the scheme on 1 March 2021 for consultation on the updated termination policy and new contributions flexibilities. The Committee will be updated of any employer comments verbally during the meeting.

3.4 Further cosmetic updates to the FSS which include approach taken by the Fund to dealing with uncertainty arising from the Goodwin court case and its potential impact on the LGPS benefit structure.

The Goodwin tribunal (details are set out on page 9 in the FSS) was raised in the Teachers' scheme. It claimed members, or their survivors, were discriminated against due to their sexual orientation. The claim was because the Teachers' scheme provides a survivor's pension which is less favourable for a widower or surviving male partner, than for a widow or surviving female partner of a female scheme member. On 30 June 2020, the Tribunal found in favour of the claimant and agreed there was discrimination. The finding and remedy is expected to apply across all public service pension schemes, including the LGPS, however this is not certain and the details are not yet known. The impact, if any, of the Goodwin case on Fund liabilities is expected to be small and will largely be an administrative issue. In the absence of a resolution or any guidance to this case, no allowance has been made for this within the 2019 formal valuation.

Payment of cessation debt and Deferred Debt Agreement Policy

3.5 The new Regulations permit LGPS funds to develop policies that provide alternative options to employers when the last active member leaves the employer (subject to a covenant assessment and consideration of security) (page 21 of Appendix A).

3.6 The default position for exit payments is that they are paid in full at the point of exit. The termination policy in the FSS has therefore been updated to allow for the new Regulations which allow exiting employers (subject to a suitable review of the unaffordability of an immediate exist debt payment) to spread their exit debt over a set period or to enter into a Deferred Debt Arrangement allowing them to remain in the Fund with no active members. The policy sets out the process that must be followed by the Fund when an employer exits the Fund (usually triggered when the last active contributing member leaves pensionable service).

The Fund can only enter into one of the above arrangements if the FSS includes a policy setting out how the employer will be treated.

New Contributions Flexibilities Policy

3.7 The new Regulations (details are set out on page 17 of the FSS) also permit contribution rates to be adjusted between valuations. Currently the contribution rates set out in the valuation report stay in place until the next valuation (except in limited circumstances or where an employer exists the Fund). These Regulations allow changes to contributions to be made before the next valuation if an employer's circumstances meet the specified criteria. The policy sets out the situations where contributions may be reviewed between actuarial valuations and the conditions that must be met.

4. Consultation and publication

4.1 Regulation 58(3) of the LGPS Regulations 2013 states that following a material change in its policy the Administering Authority should consult such persons it considers appropriate. The FSS is being updated to meet regulatory changes and adopted policies are in line with regulations but given the potential impact on Fund employers resulting from the use of the new powers to manage and mitigate employer risk it is expected that all Fund employers would be considered as ‘appropriate’ for consultation.

4.2 This DRAFT version of the FSS was distributed to all participating employers in the Fund on 1 March 2021 for comments. Deadline for responses is the 31 March 2021. The Committee will be updated verbally of any comments received. If after consideration of responses received after 25 March and no changes are made, then the draft as submitted will be accepted as the final version and published accordingly. Should there be comments which will impact the Administering Authority will finalise and a revised version will be presented in the June 2021 meeting.

5. COMMENTS OF THE CHIEF FINANCE OFFICER

5.1 The FSS sets out the funding basis and related policies through which the Fund manages the scheme liabilities and payment of contributions by scheme employers (including on exit from the Fund).

5.2 Actuarial and covenant advice regarding the FSS and related policies is met by the pension fund.

5.3 Allowing exiting employers to have the flexibility to have contributions reviewed, spreads costs or enter into DDAs may provide a greater likelihood of the Fund receiving full payment of the exit costs.

6. LEGAL COMMENTS

6.1 The Constitution delegates to the Pensions Committee the function of setting the overall strategic objectives for the Pension Fund.

6.2 Regulation 58 of the Local Government Pension Scheme Regulations 2013 requires the Council as an administering authority to publish and maintain a funding strategy statement.

6.3 The changes made to the FSS ensure that it is updated and reflects the two sets of amending regulations. The “Local Government Scheme (Amendment) Regulations 2020/179” permits Funds to determine the amount of exit credit payable to a employer leaving the Local Government Pension Scheme (LGPS). Whilst the legislation has retrospective effect, this does not apply to any cases where an exit payment has already been made.

6.4 When performing its functions as administrator of the LBTH pension fund, the Council 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 don’t (the public sector duty).

7. ONE TOWER HAMLETS CONSIDERATIONS

7.1 The London Borough of Tower Hamlets Pension Fund represents an asset to the Council in terms of its ability for attracting and retaining staff who deliver services to residents. The adoption of a Work Plan should lead to more effective management of the Fund.

7.2 A significant element of the Council's budget is the employer's contribution to the Fund. Therefore, any improvement in the efficiency of the Fund that leads to improvement in investment performance or cost savings will likely reduce contributions from the Council and release funds for other corporate priorities.

8. BEST VALUE (BV) IMPLICATIONS

8.1 The preparation and production of a Funding Strategy Statement ought to result in a more efficient process of managing the Pension Fund.

8.2 Without sound financial management of the Pension Fund, the Council and other employers in the Pension Fund could see increased volatility in their contribution rates and increases in the cost of providing for the benefits of scheme members.

9. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

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

10. RISK MANAGEMENT IMPLICATIONS

10.1 All material, financial and business issues and possibility of risks have been considered and addressed within the report and its appendices, and that the actuarial report and funding strategy statement will provide the Pension Fund with a solid framework in which to achieve a full funding status over the long term.

10.2 The Funding Strategy Statement forms part of the broader framework for funding and management of the London Borough of Tower Hamlets Pension Fund. It sets out how the Fund will approach the future funding of its liabilities and the recovery periods for recovering any deficit.

11. CRIME AND DISORDER REDUCTION IMPLICATIONS

11.1 There are no any crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report - NONE

Appendices
Appendix A – Revised Funding Strategy Statement March 2021

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report - NONE

Officer contact details for documents:

- Miriam Adams – Interim Head of Pensions & Treasury x4248

- Mulberry House, 5 Clove Crescent E14 2BG

TOWER HAMLETS

The London Borough of Tower Hamlets Pension Fund

Funding Strategy Statement

1 Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the London Borough of Tower Hamlets Pension Fund ("the Fund"), which is administered by London Borough of Tower Hamlets Council, ("the Administering Authority").

It has been prepared by the Administering Authority in collaboration with the Fund's actuary, Hymans Robertson LLP, and after consultation with the Fund's employers and investment adviser. It is effective from 1 April 2021.

1.2 What is the London Borough of Tower Hamlets Pension Fund?

The Fund is part of the national Local Government Pension Scheme (LGPS). The LGPS was set up by the UK Government to provide retirement and death benefits for local government employees, and those employed in similar or related bodies, across the whole of the UK. The Administering Authority runs the London Borough of Tower Hamlets Pension Fund, in effect the LGPS for the London Borough of Tower Hamlets area, to make sure it:

- receives the proper amount of contributions from employees and employers, and any transfer payments;
- invests the contributions appropriately, with the aim that the Fund's assets grow over time with investment income and capital growth; and
- uses the assets to pay Fund benefits to the members (as and when they retire, for the rest of their lives), and to their dependants (as and when members die), as defined in the LGPS Regulations. Assets are also used to pay transfer values and administration costs.

The roles and responsibilities of the key parties involved in the management of the Fund are summarised in Appendix B.

1.3 Why does the Fund need a Funding Strategy Statement?

Employees' benefits are determined in accordance with the LGPS Regulations, and do not change with market values or employer contributions. Investment returns will help pay for some of the benefits, but probably not all, and with no certainty. Employees' contributions are fixed in those Regulations also, at a level which covers only part of the cost of the benefits.

Therefore, employers need to pay the balance of the cost of delivering the benefits to members and their dependants.

The FSS focuses on how employer liabilities are measured, the pace at which these liabilities are funded, and how employers or pools of employers pay for their own liabilities. This statement sets out how the Administering Authority has balanced the conflicting aims of:

- Long term solvency of the Fund,
- transparency of processes,
- stability of employers' contributions, and
- prudence in the funding basis

There are also regulatory requirements for an FSS, as given in Appendix A.

The FSS is a summary of the Fund's approach to funding its liabilities, and this includes reference to the Fund's other policies; it is not an exhaustive statement of policy on all issues. The FSS forms part of a framework which includes:

- the LGPS Regulations;
- the Rates and Adjustments Certificate (confirming employer contribution rates for the next three years) which can be found in an appendix to the formal valuation report;
- all Fund's policies (including admissions, cessations and bulk transfers); which can be found on the Fund's website when this is available;
- actuarial factors for valuing individual transfers, early retirement costs and the costs of buying added service; and
- the Fund's Statement of Investment Principles / Investment Strategy Statement (see Section 4)

1.4 How does the Fund and this FSS affect me?

This depends on who you are:

- a member of the Fund, i.e. a current or former employee, or a dependant: the Fund needs to be sure it is collecting and holding enough money so that your benefits are always paid in full;
- an employer in the Fund (or which is considering joining the Fund): you will want to know how your contributions are calculated from time to time, that these are fair by comparison to other employers in the Fund, and in what circumstances you might need to pay more and what happens if you cease to be an employer in the Fund. Note that the FSS applies to all employers participating in the Fund;
- an Elected Member whose council participates in the Fund: you will want to be sure that the council balances the need to hold prudent reserves for members' retirement and death benefits, with the other competing demands for council money;
- a Council Tax payer: your council seeks to strike the balance above, and also to minimise cross-subsidies between different generations of taxpayers.

1.5 What does the FSS aim to do?

The FSS sets out the objectives of the Fund's funding strategy, such as:

- to ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable where appropriate;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return (**NB** this will also minimise the costs to be borne by Council Tax payers);
- to reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and
- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

1.6 How do I find my way around this document?

In Section 2 there is a brief introduction to some of the main principles behind funding, i.e. deciding how much an employer should contribute to the Fund from time to time.

In Section 3 we outline how the Fund calculates the contributions payable by different employers in different situations.

In Section 4 we show how the funding strategy is linked with the Fund's investment strategy.

In the Appendices we cover various issues in more detail if you are interested:

A. the regulatory background, including how and when the FSS is reviewed,

B. who is responsible for what,

C. what issues the Fund needs to monitor, and how it manages its risks,

D. some more details about the actuarial calculations required,

E. the assumptions which the Fund actuary currently makes about the future,

F. a glossary explaining the technical terms occasionally used here.

If you have any other queries please contact the Pensions & Investments Manager email: pensionsLBTH@towerhamlets.gov.uk or call telephone number 020 7364 4248.

2 Basic Funding issues

(More detailed and extensive descriptions are given in Appendix D).

2.1 How does the actuary calculate the required contribution rate?

In essence this is a three-step process:

- Calculate the funding target for that employer, i.e. the estimated amount of assets it should hold in order to be able to pay all its members' benefits. See Appendix E for more details of what assumptions we make to determine that funding target;
- Determine the time horizon over which the employer should aim to achieve that funding target. See the table in 3.3 and Note (c) for more details;
- Calculate the employer contribution rate such that it has at least a given likelihood of achieving that funding target over that time horizon, allowing for various possible economic outcomes over that time horizon. See 2.3 below, and the table in 3.3 Note (e) for more details.

2.2 What is each employer's contribution rate?

This is described in more detail in Appendix D. Employer contributions are normally made up of two elements:

a) the estimated cost of benefits being built up each year, after deducting the members' own contributions and including an allowance for administration expenses. This is referred to as the "Primary rate", and is expressed as a percentage of members' pensionable pay; plus

b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the "*Secondary rate*". In broad terms, payment of the Secondary rate is in respect of benefits already accrued at the valuation date. The Secondary rate may be expressed as a percentage of pay and/or a monetary amount in each year.

The rates for all employers are shown in the Fund's Rates and Adjustments Certificate, which forms part of the formal Actuarial Valuation Report. Employers' contributions are expressed as minima, with employers able to pay contributions at a higher rate. Account of any higher rate will be taken by the Fund actuary at subsequent valuations, i.e. will be reflected as a credit when next calculating the employer's contributions.

2.3 What different types of employer participate in the Fund?

Historically the LGPS was intended for local authority employees only. However over the years, with the diversification and changes to delivery of local services, many more types and numbers of employers now participate. There are currently more employers in the Fund than ever before, a large part of this being due to new academies.

In essence, participation in the LGPS is open to public sector employers providing some form of service to the local community. Whilst the majority of members will be local authority employees (and ex-employees), the majority of participating employers are those providing services in place of (or alongside) local authority services: academy schools, contractors, housing associations, charities, etc.

The LGPS Regulations define various types of employer as follows:

Scheduled bodies - councils, and other specified employers such as academies and further education establishments. These must provide access to the LGPS in respect of their employees who are not eligible to join another public sector scheme (such as the Teachers Scheme). These employers are so-called because they are specified in a schedule to the LGPS Regulations.

It is now possible for Local Education Authority schools to convert to academy status, and for other forms of school (such as Free Schools) to be established under the academies legislation. All such **academies (or Multi Academy Trusts)**, as employers of non-teaching staff, become separate new employers in the Fund. As academies are defined in the LGPS Regulations as "Scheduled Bodies", the Administering Authority has no discretion over whether to admit them to the Fund, and the academy has no discretion whether to continue to allow its non-teaching staff to join the Fund. There has also been guidance issued by the MHCLG regarding the terms of academies' membership in LGPS Funds.

Designating employers - employers such as town and parish councils are able to participate in the LGPS via resolution (and the Fund cannot refuse them entry where the resolution is passed). These employers can designate which of their employees are eligible to join the scheme.

Other employers are able to participate in the Fund via an admission agreement, and are referred to as 'admission bodies'. These employers are generally those with a "community of interest" with another scheme employer – **community admission bodies** ("CAB") or those providing a service on behalf of a scheme employer – **transferee admission bodies** ("TAB"). CABs will include housing associations and charities, TABs will generally be contractors. The Fund is able to set its criteria for participation by these employers and can refuse entry if the requirements as set out in the Fund's admissions policy are not met. (NB The terminology CAB and TAB has been dropped from recent LGPS Regulations, which instead combine both under the single term 'admission bodies'; however, we have retained the old terminology here as we consider it to be helpful in setting funding strategies for these different employers).

2.4 How does the calculated contribution rate vary for different employers?

All three steps above are considered when setting contributions (more details are given in Section 3 and Appendix D).

1. The **funding target** is based on a set of assumptions about the future, (e.g. investment returns, inflation, pensioners' life expectancies). If an employer is approaching the end of its participation in the Fund then its funding target may be set on a more prudent basis, so that its liabilities are less likely to be spread among other employers after its cessation;

2. The **time horizon** required is, the period over which the funding target is achieved. Employers may be given a lower time horizon if they have a less permanent anticipated membership, or do not have tax-raising powers to increase contributions if investment returns under-perform; and

3. The likelihood of achieving the funding target over that time horizon will be dependent on the Fund's view of the strength of employer covenant and its funding profile. Where an employer is considered to be weaker then the required likelihood will be set higher, which in turn will increase the required contributions (and vice versa).

For some employers it may be agreed to pool contributions, see 3.4.

Any costs of non ill-health early retirements must be paid by the employer, see 3.6.

Costs of ill-health early retirements are covered in 3.7 and 3.8.

2.5 How is a funding level calculated?

An employer's "funding level" is defined as the ratio of:

- the market value of the employer's share of assets (see Appendix D, section D5, for further details of how this is calculated), to
- the value placed by the actuary on the benefits built up to date for the employer's employees and ex-employees (the "liabilities"). The Fund actuary agrees with the Administering Authority the assumptions to be used in calculating this value.

If this is less than 100% then it means the employer has a shortfall, which is the employer's deficit; if it is more than 100% then the employer is said to be in surplus. The amount of deficit or shortfall is the difference between the asset value and the liabilities value.

It is important to note that the funding level and deficit/surplus are only measurements at a particular point in time, on a particular set of assumptions about the future. Whilst we recognise that various parties will take an interest in these measures, for most employers the key issue is how likely it is that their contributions will be sufficient to pay for their members' benefits (when added to their existing asset share and anticipated investment returns).

In short, funding levels and deficits are short term, high level risk measures, whereas contribution-setting is a longer term issue.

2.6 How does the Fund recognise that contribution levels can affect council and employer service provision, and council tax?

The Administering Authority and the Fund actuary are acutely aware that, all other things being equal, a higher contribution required to be paid to the Fund will mean less cash available for the employer to spend on the provision of services. For instance:

- Higher Pension Fund contributions may result in reduced council spending, which in turn could affect the resources available for council services, and/or greater pressure on council tax levels;
- Contributions which Academies pay to the Fund will therefore not be available to pay for providing education; and
- Other employers will provide various services to the local community, perhaps through housing associations, charitable work, or contracting council services. If they are required to pay more in pension contributions to the LGPS then this may affect their ability to provide the local services at a reasonable cost.

Whilst all this is true, it should also be borne in mind that:

- The Fund provides invaluable financial security to local families, whether to those who formerly worked in the service of the local community who have now retired, or to their families after their death;
- The Fund must have the assets available to meet these retirement and death benefits, which in turn means that the various employers must each pay their own way. Lower contributions today will mean higher contributions tomorrow: deferring payments does not alter the employer's ultimate obligation to the Fund in respect of its current and former employees;

- Each employer will generally only pay for its own employees and ex-employees (and their dependants), not for those of other employers in the Fund;
- The Fund will seek to moderate short term increases in contribution rates where appropriate and possible. However, a recent shift in regulatory focus means that solvency within each generation is considered by the Government to be a higher priority than stability of contribution rates;
- The Fund wishes to avoid the situation where an employer falls so far behind in managing its funding shortfall that its deficit becomes unmanageable in practice: such a situation may lead to employer insolvency and the resulting deficit falling on the other Fund employers. In that situation, those employers' services would in turn suffer as a result;
- Council contributions to the Fund should be at a suitable level, to protect the interests of different generations of council tax payers. For instance, underpayment of contributions for some years will need to be balanced by overpayment in other years; the council will wish to minimise the extent to which council tax payers in one period are in effect benefitting at the expense of those paying in a different period.

Overall, therefore, there is clearly a balance to be struck between the Fund's need for maintaining prudent funding levels, and the employers' need to allocate their resources appropriately. The Fund achieves this through various techniques which affect contribution increases to various degrees (see 3.1). In deciding which of these techniques to apply to any given employer, the Administering Authority takes a view on the financial standing of the employer, i.e. its ability to meet its funding commitments and the relevant time horizon.

The Administering Authority will consider a risk assessment of that employer using a knowledge base which is regularly monitored and kept up-to-date. This database will include such information as the type of employer, its membership profile and funding position, any guarantors or security provision, material changes anticipated, etc.

For instance, where the Administering Authority has reasonable confidence that an employer will be able to meet its funding commitments, then the Fund will permit options such as stabilisation (see 3.3 Note (b)), a longer time horizon relative to other employers, and/or a lower likelihood of achieving their funding target. Such options will temporarily produce lower contribution levels than would otherwise have applied. This is permitted in the expectation that the employer will still be able to meet its obligations for many years to come.

On the other hand, where there is doubt that an employer will be able to meet its funding commitments or withstand a significant change in its commitments, then a higher funding target, and/or a shorter time horizon relative to other employers, and/or a higher likelihood of achieving the target may be required.

The Fund actively seeks employer input, including to its funding arrangements, through various means: see Appendix A.

2.7 What approach has the Fund taken to dealing with uncertainty arising from the McCloud court case and its potential impact on the LGPS benefit structure?

The LGPS benefit structure from 1 April 2014 is currently under review following the Government's loss of the right to appeal the McCloud and other similar court cases. The courts have ruled that the 'transitional protections' awarded to some members of public service pension schemes when the schemes were reformed (on 1 April 2014 in the case of the LGPS) were unlawful on the grounds of age discrimination. At the time of carrying out the 31 March 2019 formal actuarial valuation, the Ministry of Housing, Communities and Local Government (MHCLG) had not provided any details of changes as a result of the case. However it was expected that benefits changes will be required and they would likely increase the value of liabilities. At that time, the scale and nature of any increase in liabilities were unknown, which limited the ability of the Fund to make an accurate allowance.

The LGPS Scheme Advisory Board (SAB) issued advice to LGPS funds in May 2019. As there was no finalised outcome of the McCloud case by 31 August 2019, the Fund Actuary acted in line with SAB's advice and valued all member benefits in line with the current LGPS Regulations.

The Fund, in line with the advice in the SAB's note, considered how to allow for this risk in the setting of employer contribution rates. As the benefit structure changes that would arise from the McCloud judgement were uncertain, the Fund elected to allow for the potential impact in the assessment of employer contribution rates at the 2019 valuation by increasing the required likelihood of reaching the funding target.

The Fund will include the impact of the McCloud case when reviewing the contribution rates at the 31 March 2022 formal actuarial valuation.

The Fund also considered the McCloud judgement in its approach to cessation valuations. Please see note (j) to table 3.3 for further information.

2.8 What approach has the Fund taken to dealing with uncertainty arising from the Goodwin court case and its potential impact on the LGPS benefit structure?

The Goodwin tribunal was raised in the Teachers' scheme. It claimed members, or their survivors, were discriminated against due to their sexual orientation. The claim was because the Teachers' scheme provides a survivor's pension which is less favourable for a widower or surviving male partner, than for a widow or surviving female partner of a female scheme member. On 30 June 2020, the Tribunal found in favour of the claimant and agreed there was discrimination. This finding and remedy is expected to apply across all public service pension schemes, including the LGPS, however this is not certain and the details are not yet known.

The impact, if any, of the Goodwin case on Fund liabilities is expected to be small and will largely be an administrative issue. In the absence of a resolution or any guidance to this case, no allowance has been made for this within the 2019 formal valuation.

2.9 When will the next actuarial valuation be?

On 8 May 2019 MHCLG issued a consultation seeking views on (among other things) proposals to amend the LGPS valuation cycle in England and Wales from a three year (triennial) valuation cycle to a four year (quadrennial) valuation cycle.

The Fund intends to carry out its next actuarial valuation in 2022 (3 years after the 2019 valuation date) in line with MHCLG's desired approach in the consultation. The Fund has therefore instructed the Fund Actuary to certify contribution rates for employers for the period 1 April 2020 to 31 March 2023 as part of the 2019 valuation of the Fund.

3 Calculating contributions for individual Employers

3.1 General comments

A key challenge for the Administering Authority is to balance the need for stable, affordable employer contributions with the requirement to take a prudent, longer-term view of funding and ensure the solvency of the Fund. With this in mind, the Fund's three-step process identifies the key issues:

1. What is a suitably (but not overly) prudent funding target?
2. How long should the employer be permitted to reach that target? This should be realistic but not so long that the funding target is in danger of never actually being achieved.
3. What likelihood is required to reach that funding target? This will always be less than 100% as we cannot be certain of the future market movements. Higher likelihood "bars" can be used for employers where the Fund wishes to reduce the risk that the employer ceases leaving a deficit to be picked up by other employers.

These and associated issues are covered in this Section.

The Administering Authority recognises that there may occasionally be particular circumstances affecting individual employers that are not easily managed within the rules and policies set out in the Funding Strategy Statement. Therefore the Administering Authority may, at its sole discretion, direct the actuary to adopt alternative funding approaches on a case by case basis for specific employers.

3.2 The effect of paying lower contributions

In limited circumstances the Administering Authority may permit employers to pay contributions at a lower level than is assessed for the employer using the three step process above. At their absolute discretion the Administering Authority may:

- extend the time horizon for targeting full funding;
- adjust the required likelihood of meeting the funding target;
- permit an employer to participate in the Fund's stabilisation mechanisms;
- permit extended phasing in of contribution rises or reductions;
- pool contributions amongst employers with similar characteristics; and/or
- accept some form of security or guarantee in lieu of a higher contribution rate than would otherwise be the case.

Employers which are permitted to use one or more of the above methods will often be paying, for a time, contributions less than required to meet their funding target, over the appropriate time horizon with the required likelihood of success. Such employers should appreciate that:

- their true long term liability (i.e. the actual eventual cost of benefits payable to their employees and ex-employees) is not affected by the pace of paying contributions;
- lower contributions in the short term will result in a lower level of future investment returns on the deficit. Thus, deferring a certain amount of contribution is likely to lead to higher contributions in the long-term; and
- it is likely to take longer to reach their funding target, all other things being equal.

Overleaf (3.3) is a summary of how the main funding policies differ for different types of employer, followed by more detailed notes where necessary.

Section 3.4 onwards deals with various other funding issues which apply to all employers.

3.3 The different approaches used for different employers

Type of employer	**Scheduled Bodies**			**Community Admission Bodies and Designating Employers**		**Transferee Admission Bodies**
Sub-type	**Council**	**Colleges**	**Academies**	**Open to new entrants**	**Closed to new entrants**	**(all)**
Funding Target Basis used	Ongoing participation basis, assumes long-term Fund participation (see Appendix E)			Ongoing participation basis, but may move to "gilts basis" - see Note (a)		Contractor exit basis, assumes fixed contract term in the Fund (see Appendix E)
Primary rate approach	(see Appendix D – D.2)					
Stabilised contribution rate?	Yes - see Note (b)	No	No	No	No	No
Maximum time horizon – Note (c)	20 years	20 years	20 years	Future working lifetime	Future working lifetime	Outstanding contract term
Secondary rate – Note (d)	% of payroll or monetary amount	Monetary amount	% of payroll	% of payroll or monetary amount	% of payroll or monetary amount	% of payroll or monetary amount
Treatment of surplus	Covered by stabilisation arrangement	Preferred approach: contributions kept at Primary rate. However, reductions may be permitted by the Administering Authority				Preferred approach: contributions kept at future service rate. However, contractors may be permitted to reduce contributions by spreading the surplus over the remaining contract term
Likelihood of achieving target – Note (e)	70%	75%	75%	70% if guaranteed, 80% otherwise	70% if guaranteed, 80% otherwise	70% if guaranteed, 80% otherwise
Phasing of contribution changes	Covered by stabilisation arrangement	At the discretion of the Administering Authority		None	None	None
Review of rates – Note (f)	Review of rates will be carried out in line with the Regulations and as set out in Note (f)					Particularly reviewed in last 3 years of contract
New employer	n/a	n/a	Note (g)	Note (h)		Notes (h) & (i)
Cessation of participation: debt/credit payable	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (machinery of Government changes for example), the cessation calculation principles applied would be as per Note (j).			Can be ceased subject to terms of admission agreement. debt/credit will be calculated on a basis appropriate to the circumstances of cessation – see Note (j).		Participation is assumed to expire at the end of the contract. Cessation debt/credit calculated on the contractor exit basis, unless the admission agreement is terminated early by the contractor in which case the low risk exit basis would apply. -Letting employer will be liable for future deficits and contributions arising. See Note (j) for further details

* Where the Administering Authority recognises a fixed contribution rate agreement between a letting authority and a contractor, the certified employer contribution rate will be derived in line with the methodology specified in the risk sharing agreement. Additionally, in these cases, upon cessation the contractor's assets and liabilities will transfer back to the letting employer with no crystallisation of any deficit or surplus. Further detail on fixed contribution rate agreements is set out in note (i).

** Includes Community Benefit Societies

Note (a) (Gilts exit basis for CABs and Designating Employers closed to new entrants)

In the circumstances where:

- the employer is a Designating Employer, or an Admission Body but not a Transferee Admission Body, and
- the employer has no guarantor, and
- the admission agreement is likely to terminate, or the employer is likely to lose its last active member, within a timeframe considered appropriate by the Administering Authority to prompt a change in funding,

the Administering Authority may set a higher funding target (e.g. based on the return from long-term gilt yields. by the time the agreement terminates or the last active member leaves, in order to protect other employers in the Fund. This policy will increase regular contributions and reduce, but not entirely eliminate, the possibility of a final deficit payment being required from the employer when a cessation valuation is carried out.

The Administering Authority also reserves the right to adopt the above approach in respect of those Designating Employers and Admission Bodies with no guarantor, where the strength of covenant is considered to be weak but there is no immediate expectation that the admission agreement will cease or the Designating Employer alters its designation.

Note (b) (Stabilisation)

Stabilisation is a mechanism where employer contribution rate variations from year to year are kept within a pre-determined range, thus allowing those employers' rates to be relatively stable. In the interests of stability and affordability of employer contributions, the Administering Authority, on the advice of the Fund Actuary, believes that stabilising contributions can still be viewed as a prudent longer-term approach. However, employers whose contribution rates have been "stabilised" (and may therefore be paying less than their theoretical contribution rate) should be aware of the risks of this approach and should consider making additional payments to the Fund if possible.

This stabilisation mechanism allows short term investment market volatility to be managed so as not to cause volatility in employer contribution rates, on the basis that a long term view can be taken on net cash inflow, investment returns and strength of employer covenant.

The current stabilisation mechanism applies to London Borough of Tower Hamlets Council as a tax raising body:

On the basis of extensive modelling carried out for the 2019 valuation exercise (see Section 4), total contributions have been set to ensure that stabilised employers have at least a 70% chance of being fully funded in 20 years under the 2019 formal valuation assumptions.

The stabilisation criteria and limits will be reviewed at the next formal valuation. However the Administering Authority reserves the right to review the stabilisation criteria and limits at any time before then, on the basis of membership and/or employer changes as described above.

Note (c) (Maximum time horizon)

The maximum time horizon starts at the commencement of the revised contribution rate (1 April 2020 for the 2019 valuation). The Administering Authority would normally expect the same period to be used at successive triennial valuations, but would reserve the right to propose alternative time horizons, for example where there were no new entrants.

Note (d) (Secondary rate)

The maximum time horizon starts at the commencement of the revised contribution rate (1 April 2020 for the 2019 valuation). The Administering Authority would normally expect the same period to be used at successive triennial valuations, but would reserve the right to propose alternative time horizons, for example where there were no new entrants.

- the employer is relatively mature, i.e. has a large Secondary contribution rate (e.g. above 15% of payroll), or
- there has been a significant reduction in payroll due to outsourcing or redundancy exercises, or
- the employer has closed the Fund to new entrants.

Note (e) (Likelihood of achieving funding target)

Each employer has its funding target calculated, and a relevant time horizon over which to reach that target. Contributions are set such that, combined with the employer's current asset share and anticipated market movements over the time horizon, the funding target is achieved with a given minimum *likelihood* . A higher required likelihood bar will give rise to higher required contributions, and vice versa.

The way in which contributions are set using these three steps, and relevant economic projections, is described in further detail in Appendix D.

Different likelihoods are set for different employers depending on their nature and circumstances: in broad terms, a higher likelihood will apply due to one or more of the following:

- the Fund believes the employer poses a greater funding risk than other employers,
- the employer does not have tax-raising powers;
- the employer does not have a guarantor or other sufficient security backing its funding position; and/or
- the employer is likely to cease participation in the Fund in the short or medium term.

Note (f) (Regular Reviews)

Under the Local Government Pension Scheme (Amendment) (No. 2) Regulations 2020 the Fund may amend contribution rates between valuations for "significant change" to the liabilities or covenant of an employer: this may result in a material increase or decrease in contributions, depending on the circumstances. The Fund would consider the following circumstances as a potential trigger for review:

- in the opinion of an Administering Authority there are circumstances which make it likely that an employer (including an admission body) will become an exiting employer sooner than anticipated at the last valuation;
- an employer is approaching exit from the scheme within the next two years and before completion of the next valuation;
- an employer agrees to pay increased contributions to meet the cost of an award of additional pension, under Regulation 31(3) of the Regulations;
- there are changes to the benefit structure set out in the LGPS Regulations including the outcomes of the McCloud case and cost sharing mechanisms (if permitted in Regulation at that time) which have not been allowed for at the last valuation;
- it appears likely to the Administering Authority that the amount of the liabilities arising or likely to arise for an employer or employers has changed significantly since the last valuation;
- it appears likely to the Administering Authority that there has been a significant change in the ability of an employer or employers to meet their obligations (i.e. a material change in employer covenant);
- it appears to the Administering Authority that the membership of the employer has changed materially such as bulk transfers, significant reductions to payroll or large-scale restructuring; or
- where an employer has failed to pay contributions or has not arranged appropriate security as required by the Administering Authority.

The Administering Authority will also consider a request from any employer to review contributions where the employer has undertaken to meet the costs of that review and sets out the reasoning for the review (which would be expected to fall into one of the above categories, such as a belief that their covenant has changed materially or they are going through a significant restructuring impacting their membership).

Except in circumstances such as an employer nearing cessation, the Administering Authority will not consider market volatility or changes to asset values as a basis for a change in contributions outside a formal valuation.

The Rates & Adjustments Certificate will be updated as necessary, following such a review.

The Administering Authority will also consider guidance in such matters from the Scheme Advisory Board as issued from time to time.

Note (g) (New Academy conversions)

At the time of writing, the Fund's policies on academies' funding issues are as follows:

i. The new academy will be regarded as a separate employer in its own right and will not be pooled with other employers in the Fund. The only exception is where the academy is part of a Multi Academy Trust (MAT) in which case the academy's figures will be calculated as below but can be combined with, for the purpose of setting contribution rates, those of the other academies in the MAT;

ii. The new academy's past service liabilities on conversion will be calculated based on its active Fund members on the day before conversion. For the avoidance of doubt, these liabilities will include all past service of those members, but will exclude the liabilities relating to any ex-employees of the school who have deferred or pensioner status;

iii. The new academy will be allocated an initial asset share from the ceding council's assets in the Fund. This asset share will be calculated using the estimated funding position of the ceding council at the date of academy conversion. The share will be based on the active members' funding level, having first allocated assets in the council's share to fully fund deferred and pensioner members. The assets allocated to the academy will be limited if necessary so that its initial funding level is subject to a maximum of 100%. The asset allocation will be based on market conditions and the academy's active Fund membership on the day prior to conversion;

iv. The new academy's calculated contribution rate will be based on the time horizon and likelihood of achieving funding target outlined for Academies in the table in Section 3.3 above;

v. It is possible for an academy to leave one MAT and join another. If this occurs, all active, deferred and pensioner members of the academy transfer to the new MAT.

The Fund's policies on academies are subject to change in the light of any amendments to MHCLG guidance (or removal of the formal guarantee currently provided to academies by the DfE). Any changes will be notified to academies, and will be reflected in a subsequent version of this FSS. In particular, policy (iv) above will be reconsidered at each valuation.

Note (h) (New Admission Bodies)

With effect from 1 October 2012, the LGPS 2012 Miscellaneous Regulations introduced mandatory new requirements for all Admission Bodies brought into the Fund from that date. Under these Regulations, all new Admission Bodies will be required to provide some form of security, agreed in conjunction with the Administering Authority, such as a guarantee from the letting employer, an indemnity or a bond. The security is required to cover some or all of the following:

- the strain cost of any redundancy early retirements resulting from the premature termination of the contract;
- allowance for the risk of asset underperformance;

- allowance for the risk of a greater than expected rise in liabilities;;
- allowance for the possible non-payment of employer and member contributions to the Fund; and/or
- the current deficit.

Transferee Admission Bodies: For all TABs, the security must be to the satisfaction of the Administering Authority as well as the letting employer, and will be reassessed on an annual basis. See also Note (i) below.

Community Admission Bodies (including Community Benefit Societies): The Administering Authority will only consider requests from CABs (or other similar bodies, such as section 75 NHS partnerships) to join the Fund if they are sponsored by a Scheduled Body with tax raising powers, guaranteeing their liabilities and also providing a form of security as above.

The above approaches reduce the risk, to other employers in the Fund, of potentially having to pick up any shortfall in respect of Admission Bodies ceasing with an unpaid deficit.

Note (i) (New Transferee Admission Bodies)

A new TAB usually joins the Fund as a result of the letting/outsourcing of some services from an existing employer (normally a Scheduled Body such as a council or academy) to another organisation (a "contractor"). This involves the TUPE transfer of some staff from the letting employer to the contractor. Consequently, for the duration of the contract, the contractor is a new participating employer in the Fund so that the transferring employees maintain their eligibility for LGPS membership. At the end of the contract the employees revert to the letting employer or to a replacement contractor.

The Fund's standard approach is for the TAB to be set up in the Fund as a new employer with responsibility for all the accrued benefits of the transferring employees; in this case, the contractor would usually be assigned an initial asset allocation equal to the past service liability value of the employees' Fund benefits. The quid pro quo is that the contractor is then expected to ensure that its share of the Fund is also fully funded at the end of the contract: see Note (j).

Employers which "outsource" have flexibility in the way that they can deal with the pension risk potentially taken on by the contractor. In particular there are three different routes that such employers may wish to adopt. Clearly as the risk ultimately resides with the employer letting the contract, it is for them to agree the appropriate route with the contractor:

i) Pooling

Under this option the contractor is pooled with the letting employer. In this case, the contractor pays the same rate as the letting employer, which may be under a stabilisation approach.

ii) Letting employer retains pre-contract risks

Under this option the letting employer would retain responsibility for assets and liabilities in respect of service accrued prior to the contract commencement date. The contractor would be responsible for the future liabilities that accrue in respect of transferred staff. The contractor's contribution rate could vary from one valuation to the next. It would be liable for any deficit (or entitled to any surplus) at the end of the contract term in respect of assets and liabilities attributable to service accrued during the contract term. Please note, the level of exit credit (if any) payable on cessation would be determined by the Administering Authority in accordance with the Regulations and this FSS.

iii) Fixed contribution rate agreed

Under this option the contractor pays a fixed contribution rate throughout its participation in the Fund and on cessation does not pay any cessation deficit or receive an exit credit. In other words, the pension risks "pass through" to the letting employer.

The Administering Authority is willing to administer any of the above options as long as the approach is documented in the Admission Agreement as well as the transfer agreement.

Alternatively, letting employers and Transferee Admission Bodies may operate any of the above options by entering into a separate Side Agreement. The Administering Authority would not necessarily be a party to this side agreement, but must be made aware of any side agreements that are put in place. In addition, the Administering Authority may treat the Admission Agreement as if it incorporates the side agreement terms where this is permitted by legislation or alternatively agreed by all parties.

Any risk sharing agreement should ensure that some element of risk transfers to the contractor where it relates to their decisions and it is unfair to burden the letting employer with that risk. For example the contractor should typically be responsible for pension costs that arise from:

- above average pay increases, including the effect in respect of service prior to contract commencement even if the letting employer takes on responsibility for the latter under (ii) above; and
- redundancy and early retirement decisions.

Note (j) (Admission Bodies Exiting the Fund)

Notwithstanding the provisions of the Admission Agreement, the Administering Authority may consider any of the following as triggers for the cessation of an admission agreement with any type of body:

- Last active member ceasing participation in the Fund (NB recent LGPS Regulation changes mean that the Administering Authority has the discretion to defer taking action for up to three years, so that if the employer acquires one or more active Fund members during that period then cessation is not triggered. The current Fund policy is that this is left as a discretion and may or may not be applied in any given case);
- The insolvency, winding up or liquidation of the Admission Body;
- Any breach by the Admission Body of any of its obligations under the Agreement that they have failed to remedy to the satisfaction of the Fund;
- A failure by the Admission Body to pay any sums due to the Fund within the period required by the Fund; or
- The failure by the Admission Body to renew or adjust the level of the bond or indemnity, or to confirm an appropriate alternative guarantor, as required by the Fund; or

- On termination of a deferred debt agreement.

On cessation, in the absence of a deferred debt arrangement, the Administering Authority will instruct the Fund actuary to carry out a cessation valuation to determine whether there is any deficit or surplus.

Payment of cessation debt

Where there is a deficit, payment of this amount in full would normally be sought from the Admission Body. The Fund's normal policy is that this cessation debt is paid in a single lump sum within 30 days of the employer being notified.

However, in line with the Regulations and when in the best interests of all parties, the Fund may agree for this payment to be spread over an agreed period, however, such agreement would only be permitted at the Fund's discretion, where payment of the debt in a single immediate lump sum could be shown to be materially detrimental to the employer's normal operations. In cases where payment is spread, the Fund reserves the right to require that the ceasing employer provides some form of security (such as a charge over assets, bond indemnity or guarantee) relating to the unpaid amount of debt at any given time.

Consideration of surplus / exit credit

Where there is a surplus, the Administering Authority will determine the amount of exit credit to be paid in accordance with the Regulations. In making this determination, the Administering Authority will consider:

(i) the extent of any surplus,

(ii) the proportion of surplus arising as a result of the employer's contributions,

(iii) any representations (such as risk sharing agreements or guarantees) made by the exiting employer and any employer providing a guarantee (or some other form of employer assistance/support) and

(iv) any other factors the Administering Authority deem relevant.

Exit Credit Policy

Please note that the Fund's Exit Credit Policy titled 'London Borough of Tower Hamlets Exit Credit Policy Statement' is available on request.

Allowance for McCloud on cessation

As discussed in Section 2.7, the LGPS benefit structure from 1 April 2014 is currently under review following the Government's loss of the right to appeal the McCloud and other similar court cases. The Fund has considered how it will reflect the current uncertainty regarding the outcome of this judgement in its approach to cessation valuations. For cessation valuations that are carried out before any changes to the LGPS benefit structure (from 1 April 2014) are confirmed, the Fund's policy is that the actuary will apply a 0.3% uplift to the ceasing employer's active and deferred member liability values where the employer is ceasing on a "gilts exit" basis, as an estimate of the possible impact of resulting benefit changes.

For non-Transferee Admission Bodies whose participation is voluntarily ended either by themselves or the Fund, or where a cessation event has been triggered, the Administering Authority must look to protect the interests of other ongoing employers. The actuary will therefore adopt an approach which, to the extent reasonably practicable, protects the other employers from the likelihood of any material loss emerging in future:

(a) Where a guarantor does not exist then, in order to protect other employers in the Fund, the cessation liabilities and final surplus/deficit will normally be calculated using a "gilts exit basis", which is more prudent than the ongoing participation basis. This has no allowance for potential future investment outperformance above gilt yields, and has added allowance for future improvements in life expectancy. This could give rise to significant cessation debts being required.

(b) Where there is a guarantor for future deficits and contributions, the details of the guarantee will be considered prior to the cessation valuation being carried out. In some cases the guarantor is simply guarantor of last resort and therefore the cessation valuation will be carried out consistently with the approach taken had there been no guarantor in place. Alternatively, where the guarantor is not simply guarantor of last resort, the cessation may be calculated using the ongoing participation basis or contractor exit basis as described in Appendix E;

(c) Again, depending on the nature of the guarantee, it may be possible to simply transfer the former Admission Body's liabilities and assets to the guarantor, without needing to crystallise any deficit or surplus. This approach may be adopted where the employer cannot pay the contributions due, and this is within the terms of the guarantee.

Under (a) and (b), any shortfall would usually be levied on the departing Admission Body as a single lump sum payment. If this is not possible then the Fund may spread the payment subject to there being some security in place for the employer such as a bond indemnity or guarantee. The approach to calculating the cessation payment will be as per the Admission Body's Admission Agreement.

In the event that the Fund is not able to recover the required payment in full, then the unpaid amounts fall to be shared amongst all of the other employers in the Fund. This may require an immediate revision to the Rates and Adjustments Certificate affecting other employers in the Fund, or instead be reflected in the contribution rates set at the next formal valuation following the cessation date.

<u>Deferred Debt Agreement ("DDA") alternative to immediate cessation</u>

As an alternative, where the ceasing Admission Body is continuing in business, the Administering Authority may enter into a written agreement with the Admission Body to defer their obligations to make an exit payment and continue to make secondary contributions (a 'Deferred Debt Agreement' as described in Regulation 64 (7A)). The Admission Body must meet all active employer requirements and pay the secondary rate of contributions as determined by the Fund Actuary until the termination of the deferred debt agreement.

The Administering Authority will consider deferred debt agreements in the following circumstances:

- The Admission Body requests the Fund consider a deferred debt agreement;
- The Admission Body is expected to have a deficit if a cessation valuation was carried out;
- The Admission Body is expected to be a going concern; and
- The covenant of the Admission Body is considered sufficient by the Administering Authority.

The Administering Authority will normally require:

- Security be put in place covering the Admission Body's deficit on their cessation basis;
- Regular monitoring of the contribution requirements and security requirements;
- All costs of the arrangement are met by the Admission Body, such as the cost of advice to the Fund, ongoing monitoring of the arrangement, and correspondence on any ongoing contribution and security requirements.

A deferred debt agreement will normally terminate on the first date on which one of the following events occurs:

- the Admission Body enrols new active Fund members;
- the period specified, or as varied, under the deferred debt agreement elapses;
- the take-over, amalgamation, insolvency, winding up or liquidation of the Admission Body;
- the Administering Authority serves a notice on the Admission Body that the Administering Authority is reasonably satisfied that the Admission Body's ability to meet the contributions payable under the deferred debt arrangement has weakened materially or is likely to weaken materially in the next 12 months;
- the Fund actuary assesses that the Admission Body has paid sufficient secondary contributions to cover all (or almost all) of the exit payment due if the employer becomes an exiting employer on the calculation date (i.e. Admission Body is now largely fully funded on their cessation basis);
- the Fund actuary assesses that the Admission Body's value of liabilities has fallen below an agreed *de minimis* level, if the employer becomes an exiting employer on the calculation date; or
- The Admission Body requests early termination of the agreement and settles the exit payment in full as calculated by the Fund actuary on the calculation date (i.e. the Admission Body pays their outstanding cessation debt on their cessation basis).

On the termination of a deferred debt agreement, the Admission Body will become an exiting employer and a cessation valuation will be completed in line with this FSS.

3.4 Pooled contributions

From time to time, with the advice of the Actuary, the Administering Authority may set up pools for employers with similar or complementary characteristics. This will always be in line with its broader funding strategy. Currently the pools in place within the Fund are as follows:

- Schools generally are also pooled with their funding Council. However there may be exceptions for specialist or independent schools.
- Smaller Transferee Admission Bodies may be pooled with the letting employer, provided all parties (particularly the letting employer) agree.

The intention of the pool is to minimise contribution rate volatility which would otherwise occur when members join, leave, take early retirement, receive pay rises markedly different from expectations, etc. Such events can cause large changes in contribution rates for very small employers in particular, unless these are smoothed out for instance by pooling across a number of employers.

On the other hand it should be noted that the employers in the pool will still have their own individual funding positions tracked by the Actuary, so that some employers will be much better funded, and others much more poorly funded, than the pool average. This therefore means that if any given employer was funding on a stand-alone basis, as opposed to being in the pool, then its contribution rate could be much higher or lower than the pool contribution rate.

It should also be noted that, if an employer is considering ceasing from the Fund, its required contributions would be based on its own funding position (rather than the pool average), and the cessation terms would also apply: this would mean potentially very different (and in particular possibly much higher) contributions would be required from the employer in that situation.

Those employers which have been pooled are identified in the Rates and Adjustments Certificate.

Employers who are permitted to enter (or remain in) a pool at the 2019 valuation will not normally be advised of their individual contribution rate unless agreed by the Administering Authority.

Community Admission Bodies that are deemed by the Administering Authority to have closed to new entrants are not usually permitted to participate in a pool.

3.5 Additional flexibility in return for added security

The Administering Authority may permit greater flexibility to the employer's contributions if the employer provides added security to the satisfaction of the Administering Authority.

Such flexibility includes a reduced rate of contribution, an extended time horizon, or permission to join a pool with another body (e.g. the Local Authority).

Such security may include, but is not limited to, a suitable bond, a legally-binding guarantee from an appropriate third party, or security over an employer asset of sufficient value.

The degree of flexibility given may take into account factors such as:

- the extent of the employer's deficit;
- the amount and quality of the security offered;
- the employer's financial security and business plan; and
- whether the admission agreement is likely to be open or closed to new entrants.

3.6 Non ill health early retirement costs

It is assumed that members' benefits are payable from the earliest age that the employee could retire without incurring a reduction to their benefit (and without requiring their employer's consent to retire). (**NB** the relevant age may be different for different periods of service, following the benefit changes from April 2008 and April 2014). Employers are required to pay additional contributions ('strain') wherever an employee retires before attaining this age. The actuary's funding basis makes no allowance for premature retirement except on grounds of ill-health.

The payment will be paid immediately, unless otherwise agreed with the Administering Authority.

3.7 Ill health early retirement costs

In the event of a member's early retirement on the grounds of ill-health, a funding strain will usually arise, which can be very large. Such strains are currently met by each employer, although individual employers may elect to take external insurance (see 3.8 below).

3.8 Ill health risk management

The Fund recognises ill health early retirement costs can have a significant impact on an employer's funding and contribution rate, which could ultimately jeopardise their continued operation.

If an employer provides satisfactory evidence to the Administering Authority of a current external insurance policy covering ill health early retirement strains, then:

- the employer's contribution to the Fund each year is reduced by the amount of that year's insurance premium, so that the total contribution is unchanged, and
- there is no need for monitoring of allowances.

When an active member retires on ill health early retirement the claim amount will be paid directly from the insurer to the insured employer. This amount should then be paid to the Fund to allow the employer's asset share to be credited.

The employer must keep the Administering Authority notified of any changes in the insurance policy's coverage or premium terms, or if the policy is ceased.

3.9 Employers with no remaining active members

In general an employer ceasing in the Fund, due to the departure of the last active member, will pay a cessation debt or receive an exit credit on an appropriate basis (see 3.3, Note (j)) and consequently have no further obligation to the Fund. Thereafter it is expected that one of two situations will eventually arise:

a) The employer's asset share runs out before all its ex-employees' benefits have been paid. In this situation the other Fund employers will be required to contribute to pay all remaining benefits: this will be done by the Fund actuary apportioning the remaining liabilities on a pro-rata basis at successive formal valuations;

b) The last ex-employee or dependant dies before the employer's asset share has been fully utilised. In this situation the remaining assets would be apportioned pro-rata by the Fund's actuary to the other Fund employers.

c) In exceptional circumstances the Fund may permit an employer with no remaining active members and a cessation deficit to continue contributing to the Fund. This would require the provision of a suitable security or guarantee, as well as a written ongoing commitment to fund the remainder of the employer's obligations over an appropriate period. The Fund would reserve the right to invoke the cessation requirements in the future, however. The Administering Authority may need to seek legal advice in such cases, as the employer would have no contributing members.

3.10 Policies on bulk transfers

The Fund has a separate written policy which covers bulk transfer payments into, out of and within the Fund. Each case will be treated on its own merits, but in general:

- The Fund will not pay bulk transfers greater than the lesser of (a) the asset share of the transferring employer in the Fund, and (b) the value of the past service liabilities of the transferring members;
- The Fund will not grant added benefits to members bringing in entitlements from another Fund unless the asset transfer is sufficient to meet the added liabilities; and
- The Fund may permit shortfalls to arise on bulk transfers if the Fund employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer's Fund contributions to increase between valuations.

4 Funding strategy and links to investment strategy

4.1 What is the Fund's investment strategy?

The Fund has built up assets over the years, and continues to receive contribution and other income. All of this must be invested in a suitable manner, which is the investment strategy.

Investment strategy is set by the Administering Authority, after consultation with the employers and after taking investment advice. The precise mix, manager make up and target returns are set out in the Investment Strategy Statement which is available to members and employers.

The investment strategy is set for the long-term, but is reviewed from time to time. Normally a full review is carried out as part of each actuarial valuation, and is kept under review annually between actuarial valuations to ensure that it remains appropriate to the Fund's liability profile.

The same investment strategy is currently followed for all employers.

4.2 What is the link between funding strategy and investment strategy?

The Fund must be able to meet all benefit payments as and when they fall due. These payments will be met by contributions (resulting from the funding strategy) or asset returns and income (resulting from the investment strategy). To the extent that investment returns or income fall short, then higher cash contributions are required from employers, and vice versa

Therefore, the funding and investment strategies are inextricably linked.

4.3 How does the funding strategy reflect the Fund's investment strategy?

In the opinion of the Fund actuary, the current funding policy is consistent with the current investment strategy of the Fund. The actuary's assumptions for future investment returns (described further in Appendix E) are based on the current benchmark investment strategy of the Fund. The future investment return assumptions underlying each of the fund's three funding bases include a margin for prudence, and are therefore considered to be consistent with the requirement to take a "prudent longer-term view" of the funding of liabilities as required by the UK Government (see Appendix A1).

In the short term – such as the three yearly assessments at formal valuations – there is the scope for considerable volatility in asset values. However, the actuary takes a long term view when assessing employer contribution rates and the contribution rate setting methodology takes into account this potential variability.

The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

4.4 Does the Fund monitor its overall funding position?

The Administering Authority monitors the relative funding position, i.e. changes in the relationship between asset values and the liabilities value, annually. It reports this to the regular Pensions Committee meetings.

5 Statutory reporting and comparison to other LGPS Funds

5.1 Purpose

Under Section 13(4)(c) of the Public Service Pensions Act 2013 ("Section 13"), the Government Actuary's Department must, following each triennial actuarial valuation, report to the Ministry of Housing Communities & Local Government (MHCLG) on each of the LGPS Funds in England & Wales. This report will cover whether, for each Fund, the rate of employer contributions are set at an appropriate level to ensure both the solvency and the long term cost efficiency of the Fund.

This additional MHCLG oversight may have an impact on the strategy for setting contribution rates at future valuations.

5.2 Solvency

For the purposes of Section 13, the rate of employer contributions shall be deemed to have been set at an appropriate level to ensure solvency if:

(a) the rate of employer contributions is set to target a funding level for the Fund of 100%, over an appropriate time period and using appropriate actuarial assumptions (where appropriateness is considered in both absolute and relative terms in comparison with other funds); and either

(b) employers collectively have the financial capacity to increase employer contributions, and/or the Fund is able to realise contingent assets should future circumstances require, in order to continue to target a funding level of 100%; or

(c) there is an appropriate plan in place should there be, or if there is expected in future to be, a material reduction in the capacity of fund employers to increase contributions as might be needed.

5.3 Long Term Cost Efficiency

The rate of employer contributions shall be deemed to have been set at an appropriate level to ensure long term cost efficiency if:

i. the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual,

ii. with an appropriate adjustment to that rate for any surplus or deficit in the Fund.

In assessing whether the above condition is met, MHCLG may have regard to various absolute and relative considerations. A relative consideration is primarily concerned with comparing LGPS pension funds with other LGPS pension funds. An absolute consideration is primarily concerned with comparing Funds with a given objective benchmark.

Relative considerations include:

1. the implied deficit recovery period; and
2. the investment return required to achieve full funding after 20 years.

Absolute considerations include:

1. the extent to which the contributions payable are sufficient to cover the cost of current benefit accrual and the interest cost on any deficit;
2. how the required investment return under "relative considerations" above compares to the estimated future return being targeted by the Fund's current investment strategy;
3. the extent to which contributions actually paid have been in line with the expected contributions based on the extant rates and adjustment certificate; and
4. the extent to which any new deficit recovery plan can be directly reconciled with, and can be demonstrated to be a continuation of, any previous deficit recovery plan, after allowing for actual Fund experience.

MHCLG may assess and compare these metrics on a suitable standardised market-related basis, for example where the local funds' actuarial bases do not make comparisons straightforward.

Appendix A – Regulatory framework

A1 Why does the Fund need an FSS?

The Ministry of Housing Communities and Local Government (MHCLG) has stated that the purpose of the FSS is:

- *"to establish a **clear and transparent fund-specific strategy** which will identify how employers' pension liabilities are best met going forward;*
- *to support the regulatory framework to maintain **as nearly constant employer contribution rates as possible**; and*
- *to take a **prudent longer-term view** of funding those liabilities."*

These objectives are desirable individually, but may be mutually conflicting.

The requirement to maintain and publish a FSS is contained in LGPS Regulations which are updated from time to time. In publishing the FSS the Administering Authority has to have regard to any guidance published by Chartered Institute of Public Finance and Accountancy (CIPFA) (most recently in 2016) and to its Statement of Investment Principles / Investment Strategy Statement.

This is the framework within which the Fund's actuary carries out triennial valuations to set employers' contributions and provides recommendations to the Administering Authority when other funding decisions are required, such as when employers join or leave the Fund. The FSS applies to all employers participating in the Fund.

A2 Does the Administering Authority consult anyone on the FSS?

Yes. This is required by LGPS Regulations. It is covered in more detail by the most recent CIPFA guidance, which states that the FSS must first be subject to "consultation with such persons as the authority considers appropriate", and should include "a meaningful dialogue at officer and elected member level with council tax raising authorities and with corresponding representatives of other participating employers".

In practice, for the Fund, the consultation process for this FSS was as follows:

a) A draft version of the FSS was issued to all participating employers on 8 March 2021 for comment;

b) Following the end of the consultation period the FSS was updated where required and final version presented to Pensions Committee. A copy would be made available on the Fund's website once up and running.

A3 How is the FSS published?

The FSS is made available through the following routes:

- The Fund has no website, it is not possible at this stage to make a web version available;
- A copy sent by e-mail to each participating employer in the Fund;
- Copies sent to investment managers and independent advisers;
- Copies made available on request.

A4 How often is the FSS reviewed?

The FSS is reviewed in detail at least every three years as part of the triennial valuation. (which may move to every four years in future – see Section 2.8). This version is expected to remain unaltered until it is consulted upon as part of the formal process for the next valuation.

It is possible that (usually slight) amendments may be needed within the three year period. These would be needed to reflect any regulatory changes, or alterations to the way the Fund operates (e.g. to accommodate a new class of employer). Any such amendments would be consulted upon as appropriate:

- trivial amendments would be simply notified at the next round of employer communications,
- amendments affecting only one class of employer would be consulted with those employers,
- other more significant amendments would be subject to full consultation.

In any event, changes to the FSS would need agreement by the Pensions Committee and would be included in the relevant Committee Meeting minutes.

A5 How does the FSS fit into other Fund documents?

The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues, for example there are a number of separate statements published by the Fund including the Investment Strategy Statement, Governance Strategy and Communications Strategy. In addition, the Fund publishes an Annual Report and Accounts with up to date information on the Fund.

These documents can be found on the web at www.towerhamletspensionfund.org.

Appendix B – Responsibilities of key parties

The efficient and effective operation of the Fund needs various parties to each play their part.

B1 The Administering Authority should:-

- operate the Fund as per the LGPS Regulations;
- effectively manage any potential conflicts of interest arising from its dual role as Administering Authority and a Fund employer;
- collect employer and employee contributions, and investment income and other amounts due to the Fund;
- ensure that cash is available to meet benefit payments as and when they fall due;
- pay from the Fund the relevant benefits and entitlements that are due;
- invest surplus monies (i.e. contributions and other income which are not immediately needed to pay benefits) in accordance with the Fund's Investment Strategy Statement (ISS) and LGPS Regulations;
- communicate appropriately with employers so that they fully understand their obligations to the Fund;
- take appropriate measures to safeguard the Fund against the consequences of employer default;
- manage the valuation process in consultation with the Fund's actuary;
- provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
- prepare and maintain a FSS and a ISS, after consultation;
- notify the Fund's actuary of material changes which could affect funding (this is covered in a separate agreement with the actuary); and
- monitor all aspects of the fund's performance and funding and amend the FSS and ISS as necessary and appropriate.

B2 The Individual Employer should:-

- deduct contributions from employees' pay correctly;
- pay all contributions, including their own as determined by the actuary, promptly by the due date;
- have a policy and exercise discretions within the regulatory framework;
- make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain; and
- notify the Administering Authority promptly of all changes to its circumstances, prospects or membership, which could affect future funding.

B3 The Fund Actuary should:-

- prepare valuations, including the setting of employers' contribution rates. This will involve agreeing assumptions with the Administering Authority, having regard to the FSS and LGPS Regulations, and targeting each employer's solvency appropriately;
- provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
- provide advice relating to new employers in the Fund, including the level and type of bonds or other forms of security (and the monitoring of these);
- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters;
- assist the Administering Authority in considering possible changes to employer contributions between formal valuations, where circumstances suggest this may be necessary;
- advise on the termination of employers' participation in the Fund; and
- fully reflect actuarial professional guidance and requirements in the advice given to the Administering Authority.

B4 Other parties:-

- investment advisers (either internal or external) should ensure the Fund's ISS remains appropriate, and consistent with this FSS;
- investment managers, custodians and bankers should all play their part in the effective investment (and dis-investment) of Fund assets, in line with the ISS;
- auditors should comply with their auditing standards, ensure Fund compliance with all requirements, monitor and advise on fraud detection, and sign off annual reports and financial statements as required;
- governance advisers may be appointed to advise the Administering Authority on efficient processes and working methods in managing the Fund;
- legal advisers (either internal or external) should ensure the Fund's operation and management remains fully compliant with all regulations and broader local government requirements, including the Administering Authority's own procedures;
- the Ministry of Housing Communities and Local Government (assisted by the Government Actuary's Department) and the Scheme Advisory Board, should work with LGPS Funds to meet Section 13 requirements.

Appendix C – Key risks and controls

C1 Types of risk

The Administering Authority has an active risk management programme in place. The measures that it has in place to control key risks are summarised below under the following headings:

- financial;
- demographic;
- regulatory; and
- governance.

C2 Financial risks

Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning the valuation of liabilities and contribution rates over the long-term.	Only anticipate long-term returns on a relatively prudent basis to reduce risk of under-performing. Assets invested on the basis of specialist advice, in a suitably diversified manner across asset classes, geographies, managers, etc. Analyse progress at three yearly valuations for all employers. Inter-valuation roll-forward of liabilities between valuations at whole Fund level.
Inappropriate long-term investment strategy.	Overall investment strategy options considered as an integral part of the funding strategy. Used asset liability modelling to measure 4 key outcomes. Chosen option considered to provide the best balance.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers relative to their index benchmark.
Effect of possible asset underperformance as a result of climate change	The Fund's Investment Strategy Statement contains details of climate change considerations.
Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies	An explicit stabilisation mechanism has been agreed as part of the funding strategy. Other measures are also in place to limit sudden increases in contributions.

Risk	Summary of Control Mechanisms
Orphaned employers give rise to added costs for the Fund	The Fund seeks a cessation debt (or security/guarantor) to minimise the risk of this happening in the future. If it occurs, the Actuary calculates the added cost spread pro-rata among all employers – (see 3.9).

C3 Demographic risks

Risk	Summary of Control Mechanisms
Pensioners living longer, thus increasing cost to Fund.	Set mortality assumptions with some allowance for future increases in life expectancy. The Fund Actuary has direct access to the experience of over 50 LGPS funds which allows early identification of changes in life expectancy that might in turn affect the assumptions underpinning the valuation.
Maturing Fund – i.e. proportion of actively contributing employees declines relative to retired employees.	Continue to monitor at each valuation, consider seeking monetary amounts rather than % of pay and consider alternative investment strategies.
Deteriorating patterns of early retirements	Employers are charged the extra cost of non ill-health retirements following each individual decision. Employer ill health retirement experience is monitored, and insurance is an option.
Reductions in payroll causing insufficient deficit recovery payments	In many cases this may not be sufficient cause for concern, and will in effect be caught at the next formal valuation. However, there are protections where there is concern, as follows: Employers in the stabilisation mechanism may be brought out of that mechanism to permit appropriate contribution increases (see Note (b) to 3.3).

Risk	Summary of Control Mechanisms
	For other employers, review of contributions is permitted in general between valuations (see Note (f) to 3.3) and may require a move in deficit contributions from a percentage of payroll to fixed monetary amounts.

C4 Regulatory risks

Risk	Summary of Control Mechanisms
Changes to national pension requirements and/or HMRC rules e.g. changes arising from public sector pensions reform.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. The Administering Authority is monitoring the progress on the McCloud court case and will consider an interim valuation or other appropriate action once more information is known. The government's long term preferred solution to GMP indexation and equalisation - conversion of GMPs to scheme benefits - was built into the 2019 valuation.
Time, cost and/or reputational risks associated with any MHCLG intervention triggered by the Section 13 analysis (see Section 5).	Take advice from Fund Actuary on position of Fund as at prior valuation, and consideration of proposed valuation approach relative to anticipated Section 13 analysis.
Changes by Government to particular employer participation in LGPS Funds, leading to impacts on funding and/or investment strategies.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. Take advice from Fund Actuary on impact of changes on the Fund and amend strategy as appropriate.

C5 Governance risks

Risk	Summary of Control Mechanisms
Administering Authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements) or not advised of an employer closing to new entrants.	The Administering Authority has a close relationship with employing bodies and communicates required standards e.g. for submission of data. The Actuary may revise the rates and Adjustments certificate to increase an employer's contributions between triennial valuations Deficit contributions may be expressed as monetary amounts.
Actuarial or investment advice is not sought, or is not heeded, or proves to be insufficient in some way	The Administering Authority maintains close contact with its specialist advisers. Advice is delivered via formal meetings involving Elected Members, and recorded appropriately. Actuarial advice is subject to professional requirements such as peer review.
Administering Authority failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body.	The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes. Community Admission Bodies' memberships are monitored and, if active membership decreases, steps will be taken.
An employer ceasing to exist with insufficient funding or adequacy of a bond.	The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure. The risk is mitigated by: Seeking a funding guarantee from another scheme employer, or external body, where-ever possible (see Notes (h) and (j) to 3.3). Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice. Vetting prospective employers before admission.

Risk	Summary of Control Mechanisms
	Where permitted under the regulations requiring a bond to protect the Fund from various risks. Requiring new Community Admission Bodies to have a guarantor. Reviewing bond or guarantor arrangements at regular intervals (see Note (f) to 3.3). Reviewing contributions well ahead of cessation if thought appropriate (see Note (a) to 3.3).
An employer ceasing to exist resulting in an exit credit being payable	The Administering Authority regularly monitors admission bodies coming up to cessation The Administering Authority invests in liquid assets to ensure that exit credits can be paid when required.

Appendix D – The calculation of Employer contributions

In Section 2 there was a broad description of the way in which contribution rates are calculated. This Appendix considers these calculations in much more detail.

As discussed in Section 2, the actuary calculates the required contribution rate for each employer using a three-step process:

- Calculate the funding target for that employer, i.e. the estimated amount of assets it should hold in order to be able to pay all its members' benefits. See Appendix E for more details of what assumptions we make to determine that funding target;
- Determine the time horizon over which the employer should aim to achieve that funding target. See the table in 3.3 and Note (c) for more details;
- Calculate the employer contribution rate such that it has at least a given likelihood of achieving that funding target over that time horizon, allowing for various possible economic outcomes over that time horizon. See the table in 3.3 Note (e) for more details.

The calculations involve actuarial assumptions about future experience, and these are described in detail in Appendix E.

D1 What is the difference between calculations across the whole Fund and calculations for an individual employer?

Employer contributions are normally made up of two elements:

a) the estimated cost of ongoing benefits being accrued, referred to as the "Primary contribution rate" (see D2 below); plus

b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the "Secondary contribution rate" (see D3 below).

The contribution rate for each employer is measured as above, appropriate for each employer's assets, liabilities and membership. The whole Fund position, including that used in reporting to MHCLG (see section 5), is calculated in effect as the sum of all the individual employer rates. MHCLG currently only regulates at whole Fund level, without monitoring individual employer positions.

D2 How is the Primary contribution rate calculated?

The Primary element of the employer contribution rate is calculated with the aim that these contributions will meet benefit payments in respect of members' **future** service in the Fund. This is based upon the cost (in excess of members' contributions) of the benefits which employee members earn from their service each year.

The Primary rate is calculated separately for all the employers, although employers within a pool will pay the contribution rate applicable to the pool as a whole. The Primary rate is calculated such that it is projected to:

1. meet the required funding target for all future years' accrual of benefits*, excluding any accrued assets,

2. within the determined time horizon (see note 3.3 Note (c) for further details),
3. with a sufficiently high likelihood, as set by the Fund's strategy for the category of employer (see 3.3 Note (e) for further details).

* The projection is for the current active membership where the employer no longer admits new entrants, or additionally allows for new entrants where this is appropriate.

The projections are carried out using an economic modeller (the "Economic Scenario Service") developed by the Fund's actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as asset returns (based on the Fund's investment strategy), inflation, and bond yields. Further information about this model is included in Appendix E. The measured contributions are calculated such that the proportion of outcomes meeting the employer's funding target (at the end of the time horizon) is equal to the required likelihood.

The approach includes expenses of administration to the extent that they are borne by the Fund, and includes allowances for benefits payable on death in service and on ill health retirement.

D3 How is the Secondary contribution rate calculated?

The Secondary rate is calculated as the balance over and above the Primary rate, such that the contribution rate is projected to:

1 meet the required funding target relating to combined past and future service benefit accrual, including accrued asset share (see D5 below)

2 at the end of the determined time horizon (see 3.3 Note (c) for further details)

3 with a sufficiently high likelihood, as set by the Fund's strategy for the category of employer (see 3.3 Note (e) for further details).

The projections are carried out using an economic modeller developed by the Fund Actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as asset returns (based on the Fund's investment strategy), inflation, and bond yields. The measured contributions are calculated such that the proportion of outcomes with at least 100% solvency (by the end of the time horizon) is equal to the required likelihood.

The Administering Authority, after taking advice from the Fund's actuary, may choose to calculate Primary and Secondary contribution rates differently if particular circumstances apply to an employer.

D4 What affects a given employer's valuation results?

The results of these calculations for a given individual employer will be affected by:

1. past contributions relative to the cost of accruals of benefits;
2. different liability profiles of employers (e.g. mix of members by age, gender, service vs. salary);
3. the effect of any differences in the funding target, i.e. the valuation basis used to value the employer's liabilities at the end of the time horizon;
4. any different time horizons;
5. the difference between actual and assumed rises in pensionable pay;

6. the difference between actual and assumed increases to pensions in payment and deferred pensions;
7. the difference between actual and assumed retirements on grounds of ill-health from active status;
8. the difference between actual and assumed amounts of pension ceasing on death;
9. the additional costs of any non ill-health retirements relative to any extra payments made; and/or
10. differences in the required likelihood of achieving the funding target.

D5 How is each employer's asset share calculated?

The Administering Authority does not operate separate bank accounts or investment mandates for each employer. Therefore it cannot account for each employer's assets separately. Instead, the Fund Actuary must apportion the assets of the whole Fund between the individual employers. There are broadly two ways to do this:

A technique known as "analysis of surplus" in which the Fund actuary estimates the surplus/deficit of an employer at the current valuation date by analysing movements in the surplus/deficit from the previous actuarial valuation date. The estimated surplus/deficit is compared to the employer's liability value to calculate the employer's asset value. The actuary will quantify the impact of investment, membership and other experience to analyse the movement in the surplus/deficit. This technique makes a number of simplifying assumptions due to the unavailability of certain items of information. This leads to a balancing, or miscellaneous, item in the analysis of surplus, which is split between employers in proportion to their asset shares.

A 'cashflow approach' in which an employer's assets are tracked over time allowing for cashflows paid in (contributions, transfers in etc.), cashflows paid out (benefit payments, transfers out etc.) and investment returns on the employer's assets.

Until 31 March 2016 the Administering Authority used the 'analysis of surplus' approach to apportion the Fund's assets between individual employers.

Since then, the Fund has adopted a cashflow approach for tracking individual employer assets.

The Fund Actuary tracks employer assets on an annual basis. Starting with each employer's assets from the previous year end, cashflows paid in/out and investment returns achieved on the Fund's assets over the course of the year are added to calculate an asset value at the year end. The approach has some simplifying assumptions in that all cashflows and investment returns are assumed to have occurred uniformly over the course of the year. As the actual timing of cashflows and investment returns are not allowed for, the sum of all employers' asset values will deviate from the whole fund asset total over time (the deviation is expected to be minor). The difference is split between employers in proportion to their asset shares at each triennial valuation.

The Fund is satisfied that this new approach provides the most accurate asset allocations between employers that is reasonably possible at present.

D6 How does the Fund adjust employer asset shares when an individual member moves from one employer in the Fund to another?

Under the cashflow approach for tracking employer asset shares, the Fund has allowed for any individual members transferring from one employer in the Fund to another, via the transfer of a sum from the ceding employer's asset share to the receiving employer's asset share. This sum is equal to the member's Cash Equivalent Transfer Value (CETV) as advised by the Fund's administrators.

Appendix E – Actuarial assumptions

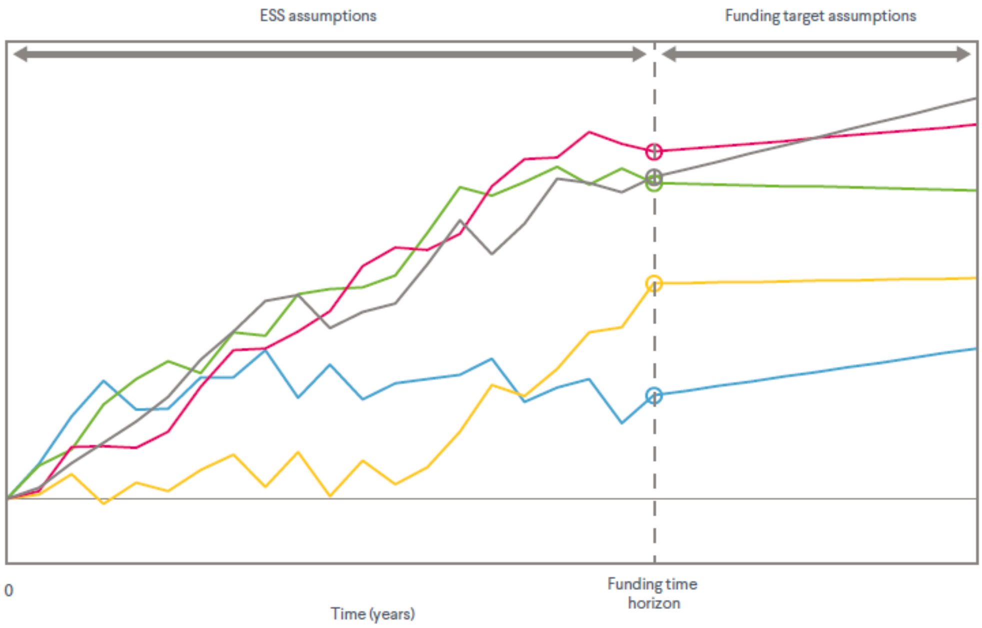
E1 What are the actuarial assumptions used to calculate employer contribution rates?
These are expectations of future experience used to place a value on future benefit payments ("the liabilities"). Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, likelihoods of ill-health early retirement, and proportions of member deaths giving rise to dependants' benefits.

Changes in assumptions will affect the funding target and required contribution rate. However, different assumptions will not of course affect the actual benefits payable by the Fund in future.

The actuary's approach to calculating employer contribution rates involves the projection of each employer's future benefit payments, contributions and investment returns into the future under 5,000 possible economic scenarios. Future inflation (and therefore benefit payments) and investment returns for each asset class (and therefore employer asset values) are variables in the projections. By projecting the evolution of an employer's assets and benefit payments 5,000 times, a contribution rate can be set that results in a sufficient number of these future projections (determined by the employer's required likelihood) being successful at the end of the employer's time horizon. In this context, a successful contribution rate is one which results in the employer having met its funding target at the end of the time horizon.

Setting employer contribution rates therefore requires two types of assumptions to be made about the future:

1. Assumptions to project the employer's assets, benefits and cashflows to the end of the funding time horizon. For this purpose the actuary uses Hymans Robertson's proprietary stochastic economic model - the Economic Scenario Service ("ESS").
2. Assumptions to assess whether, for a given projection, the funding target is satisfied at the end of the time horizon. For this purpose, the Fund has three different funding bases.



Details on the ESS assumptions and funding target assumptions are included below (in E2 and E3 respectively).

E2 What assumptions are used in the ESS?

The actuary uses Hymans Robertson's ESS model to project a range of possible outcomes for the future behaviour of asset returns and economic variables. With this type of modelling, there is no single figure for an assumption about future inflation or investment returns. Instead, there is a range of what future inflation or returns will be which leads to likelihoods of the assumption being higher or lower than a certain value.

The ESS is a complex model to reflect the interactions and correlations between different asset classes and wider economic variables. The table below shows the calibration of the model as at 31 March 2019. All returns are shown net of fees and are the annualised total returns over 5, 10 and 20 years, except for the yields which refer to the simulated yields at that time horizon.

		Annualised total returns									
		Cash	Index Linked Gilts (medium)	Fixed Interest Gilts (medium)	UK Equity	Overseas Equity	Property	A rated corporate bonds (medium)	RPI inflation expectation	17 year real govt bond yield	17 year govt bond yield
5 years	16th %'ile	-0.4%	-2.3%	-2.9%	-4.1%	-4.1%	-3.5%	-2.7%	1.9%	-2.5%	0.8%
	50th %'ile	0.7%	0.5%	0.3%	4.0%	4.1%	2.4%	0.8%	3.3%	-1.7%	2.1%
	84th %'ile	2.0%	3.3%	3.4%	12.7%	12.5%	8.8%	4.0%	4.9%	-0.8%	3.6%
10 years	16th %'ile	-0.2%	-1.8%	-1.3%	-1.5%	-1.4%	-1.5%	-0.9%	1.9%	-2.0%	1.2%
	50th %'ile	1.3%	0.0%	0.2%	4.6%	4.7%	3.1%	0.8%	3.3%	-0.8%	2.8%
	84th %'ile	2.9%	1.9%	1.7%	10.9%	10.8%	7.8%	2.5%	4.9%	0.4%	4.8%
20 years	16th %'ile	0.7%	-1.1%	0.1%	1.2%	1.3%	0.6%	0.7%	2.0%	-0.7%	2.2%
	50th %'ile	2.4%	0.3%	1.0%	5.7%	5.8%	4.3%	1.9%	3.2%	0.8%	4.0%
	84th %'ile	4.5%	2.0%	2.0%	10.3%	10.4%	8.1%	3.0%	4.7%	2.2%	6.3%
	Volatility (Disp) (1 yr)	1%	7%	10%	17%	17%	14%	11%	1%		

E3 What assumptions are used in the funding target?

At the end of an employer's funding time horizon, an assessment will be made – for each of the 5,000 projections – of how the assets held compare to the value of assets required to meet the future benefit payments (the funding target). Valuing the cost of future benefits requires the actuary to make assumptions about the following financial factors:

- Benefit increases and CARE revaluation
- Salary growth
- Investment returns (the "discount rate")

Each of the 5,000 projections represents a different prevailing economic environment at the end of the funding time horizon and so a single, fixed value for each assumption is unlikely to be appropriate for every projection. For example, a high assumed future investment return (discount rate) would not be prudent in projections with a weak outlook for economic growth. Therefore, instead of using a fixed value for each assumption, the actuary references economic indicators to ensure the assumptions remain appropriate for the prevailing economic environment in each projection. The economic indicators the actuary uses are: future inflation expectations and the prevailing risk free rate of return (the yield on long term UK government bonds is used as a proxy for this rate).

The Fund has three funding bases which will apply to different employers depending on their type. Each funding basis has a different assumption for future investment returns when determining the employer's funding target.

Funding basis	**Ongoing participation basis**	**Contractor exit basis**	**Low risk exit basis**
Employer type	All employers except Transferee Admission Bodies and closed Community Admission Bodies	Transferee Admission Bodies	Community Admission Bodies that are closed to new entrants
Investment return assumption underlying the employer's funding target (at the end of its time horizon)	Long term government bond yields plus an asset outperformance assumption (AOA) of 2.0% p.a.	Long term government bond yields plus a 2.0% p.a. AOA	Long term government bond yields with no allowance for outperformance on the Fund's assets

E4 What other assumptions apply?

The following assumptions are those of the most significance used in both the projection of the assets, benefits and cashflows and in the funding target.

a) Salary growth

After discussion with Fund officers, the salary increase assumption at the 2019 valuation has been set to be a blended rate combined of:

- 4%, 2.5%, 2.5% each year until 31 March 2022, followed by
- 1% below the retail prices index (RPI) p.a. thereafter.

This gives a single "blended" assumption of CPI plus 0.2%. This is a change from the previous valuation, which assumed a blended assumption of CPI less 0.1% per annum. The change has led to an increase in the funding target (all other things being equal).

b) Pension increases

Since 2011 the consumer prices index (CPI), rather than RPI, has been the basis for increases to public sector pensions in deferment and in payment. Note that the basis of such increases is set by the Government, and is not under the control of the Fund or any employers.

At this valuation, we have continued to assume that CPI is 1.0% per annum lower than RPI. (Note that the reduction is applied in a geometric, not arithmetic, basis).

c) Life expectancy

The demographic assumptions are intended to be best estimates of future experience in the Fund based on past experience of LGPS funds which participate in Club Vita, the longevity analytics service used by the Fund, and endorsed by the actuary.

The longevity assumptions that have been adopted at this valuation are a bespoke set of "VitaCurves", produced by the Club Vita's detailed analysis, which are specifically tailored to fit the membership profile of the Fund. These curves are based on the data provided by the Fund for the purposes of this valuation.

Allowance has been made in the ongoing valuation basis for future improvements in line with the 2018 version of the Continuous Mortality Investigation model published by the Actuarial Profession and a 1.25% per annum minimum underpin to future reductions in mortality rates. This updated allowance for future improvements will generally result in lower life expectancy assumptions and hence a reduced funding target (all other things being equal).

The approach taken is considered reasonable in light of the long term nature of the Fund and the assumed level of security underpinning members' benefits.

d) General

The same financial assumptions are adopted for most employers (on the ongoing participation basis identified above), in deriving the funding target underpinning the Primary and Secondary rates: as described in (3.3), these calculated figures are translated in different ways into employer contributions, depending on the employer's circumstances.

The demographic assumptions, in particular the life expectancy assumption, in effect vary by type of member and so reflect the different membership profiles of employers.

Appendix F – Glossary

Administering Authority The council with statutory responsibility for running the Fund, in effect the Fund's "trustees".

Admission Bodies Employers where there is an Admission Agreement setting out the employer's obligations. These can be Community Admission Bodies or Transferee Admission Bodies. For more details (see 2.3).

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.

Designating Employer Employers such as town and parish councils that are able to participate in the LGPS via resolution. These employers can designate which of their employees are eligible to join the Fund.

Employer An individual participating body in the Fund, which employs (or used to employ) **members** of the Fund. Normally the assets and **funding target** values for each employer are individually tracked, together with its **Primary rate** at each **valuation**.

Funding Basis The combined set of assumptions made by the actuary, regarding the future, to calculate the value of the funding target at the end of the employer's time horizon. The main assumptions will relate to the level of future investment returns, salary growth, pension increases and longevity. More prudent assumptions will give a higher funding target, whereas more optimistic assumptions will give a lower funding target.

Gilt A UK Government bond, i.e. a promise by the Government to pay interest and capital as per the terms of that particular gilt, in return for an initial payment of capital by the purchaser. Gilts can be "fixed interest", where the interest payments are level throughout the gilt's term, or "index-linked" where the interest payments vary each year in line with a specified index (usually RPI). Gilts can be bought as assets by the Fund, but are also used in funding as an objective measure of a risk-free rate of return.

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.

Letting employer	An employer which outsources or transfers a part of its services and 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. A letting employer will usually be a local authority, but can sometimes be another type of employer such as an Academy.
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 eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 100 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.
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).
Primary contribution rate	The employer contribution rate required to pay for ongoing accrual of active members' benefits (including an allowance for administrative expenses). See Appendix D for further details.
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 vs their salary levels, etc. A membership (or liability) profile might be measured for its **maturity** also.
Rates and Adjustments Certificate	A formal document required by the LGPS Regulations, which must be updated 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 period until the next valuation is completed.

Scheduled Bodies	Types of employer explicitly defined in the LGPS Regulations, whose employees must be offered membership of their local LGPS Fund. These include Councils, colleges, universities, academies, police and fire authorities etc, other than employees who have entitlement to a different public sector pension scheme (e.g. teachers, police and fire officers, university lecturers).
Secondary contribution rate	The difference between the employer's actual and **Primary contribution rates**. See Appendix D for further details.
Stabilisation	Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund.
Valuation	A risk management exercise to review the liabilities, future service contribution rate and common contribution rate for a Fund, and usually individual employers too.

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Non-Executive Report of the: **PENSIONS COMMITTEE** **25 March 2021**	TOWER HAMLETS
Report of Kevin Bartle, Interim Corporate Director, Resources	**Classification:** Unrestricted
Funding Update at 31 December 2020	

Originating Officer(s)	Miriam Adams, Interim Head of Pensions & Treasury
Wards affected	All

Summary

The funding update is provided to illustrate the estimated funding position from 31 March 2019 to 31 December 2020 and the funding impact, risks and mitigation of risks associated with the ongoing COVID-19 pandemic.

At the last formal valuation, the Fund assets was £1,552m and the liabilities were £1,525m. This represented a surplus of £27m and equated to a funding level of 102%. At 31 December 2020, with assets at £1,948m and estimated liabilities £1,716m, the actuarial estimate is that the funding level is 114%.

The Fund actuary Hymans will present to Members their outlook on funding position and risk principles.

Recommendations:

Pensions Committee is recommended to:

1. Note the whole Fund actuarial update at 31 December 2020
2. Note that any investment decisions taken which fail to provide the desired returns will impact estimated funding levels.

1. REASONS FOR THE DECISIONS

1.1 Tower Hamlets Council as the Fund's administering authority recognises that effective risk management is an essential part of good governance.

1.2 The purpose of the valuation is to review the current funding strategy and ensure the Fund has a contribution plan and investment strategy in place that will enable it to pay members' benefits as they fall due. This report is for noting.

2. ALTERNATIVE OPTIONS

2.1 This report serves as a monitoring tool for funding level as well as acting as a risk management tool.

3. DETAILS OF REPORT

31 December 2020 funding and risk

3.1 The 2019 triennial actuarial valuation was completed in March 2020. It is undertaken to determine the funding position and investment strategy that can support sustainable contributions from employers.

The triennial actuarial review covers three main elements: processing and validation of data, funding strategy and covenant assessment.

3.2 The last 24 months since the 2019 valuation has seen market volatility and the COVID-19 pandemic affect investment returns outlook and it is prudent for Members to review any risk mitigation factors that might affect future employer covenants, investment returns and contribution rates.

3.3 The funding update is provided to illustrate the estimated funding position from 31 March 2019 to 31 December 2020. At the last formal valuation, the Fund assets were £1,552m and the liabilities were £1,525m. This represented a surplus of £27m and equated to a funding level of 102%. At 31 December 2020, the actuary estimated that the estimated funding level is 114%as detailed in the table below.

Actuarial Funding Position at 31 March 2020				
31 December 2020	Ongoing Funding (£m)		Surplus/ (deficit)	£m
Assets	1,948		Surplus/(deficit) as at 31/3/2019	27
			Contributions (less benefits accruing)	(7)
Liabilities	1,716		Interest on surplus/ (deficit)	(0)
			Excess return on assets	368
Surplus/(deficit)	232		Change in inflation & expected future investment return	(155)
Funding level	**114%**		**Surplus/(deficit) as at 31/12/2020**	**232**

Market movement impact

3.4 Hymans the Fund actuary have prepared a presentation (attached as Appendix A) to review the whole Funding level at 31 December 2020.

	31/3/2019	31/12/2020
Market yields (p.a)		
Fixed interest gilts	1.49%	0.67%
Index-linked gilts	-1.81%	-2.31%
Implied inflation	3.36%	3.05%
AA corporate bond yield	2.36%	1.35%
Price Index		
FTSE All Share	3,978	3,674
FTSE 100	7,279	6,461
Expected future investment return (p.a.)		
20yr annualised return on Fund's asset portfolio*	4.0%	3.2%
*There is at least a 70% likelihood of the Fund's investments achieving a return of at least 3.2% p.a. over the next 20 years * There was some extreme volatility in investment markets around the date of 31 December 2020, which may impact the likelihood estimates of expected future investment returns in the estimates calculated by the actuary		

3.5 Majority of employers in the Tower Hamlets Fund are public sector bodies, such as the council and academies where the covenant is strong and backed by statute or the Department of Education (DFE). These kinds of employers are unlikely to pose an insolvency risk to the Fund. Similarly, they are likely to make contributions when they fall due although some may face cash flow challenges.

3.6 Other employers like contractors tend to only participate in the Fund for a number of years depending on their contract duration. Most are closed to new entrants. Charities and other third sector employers may be the group most impacted although some may have reserves to call upon. Employers like leisure centres have been badly hit by lockdown although ceding councils have made support available.

Future monitoring position of employers

3.7 The Fund will continue to monitor the position of all employers, most importantly employers who are expected to cease in the near future and those whose revenue have been hard hit by COVID-19 or likely to be impacted post lock lock down.

4. <u>RISK MITIGATION MEASURES</u>

4.1 The Fund will apply the following measures to mitigate risks.

- Market movements – monitor funding level, outlook for the long-term economy and asset returns on a regular basis.

- Employer covenant and risks – the policy for contribution deferral policy, ensure contracts, bonds and guarantees are in place and up to date. The Committee during this meeting will approve updated Funding Strategy Statement which includes policies on Debt deferral and contribution flexibility. The Fund will engage directly employers and review funding position for employers likely to cease before 2023.

- Higher death rates - the Fund will ensure liquidity availability to pay increased death benefit payments. The Committee, in September 2020, agreed to utilise £20m cash from Equity Protection to plug any operational cash flow deficit for the next 3 years.

- Continue to monitor scheme longevity via Hymans Club Vita which is involved with longevity studies within Hymans LGPS clients.

5. COMMENTS OF THE CHIEF FINANCE OFFICER

5.1 The performance of the Pension Fund's investments affects the required level of
contributions due from employers.

5.2 The employers' contribution rate for the whole Fund remains at a whole Fund primary rate of 19.9% as a result of the 2019 triennial reported.

6. LEGAL COMMENTS

6.1 The Constitution delegates to the Pensions Committee the function of setting the overall strategic objectives for the Pension Fund.

6.2 Regulation 58 of the Local Government Pension Scheme Regulations 2013 requires the Council as an administering authority to publish and maintain a funding strategy statement. This report provides the Committee with an update on the whole Fund's actuarial position as at 31st December 2020.

6.3 When preparing, maintaining or publishing the funding strategy statement, the Council is required to make such revisions as it considers appropriate following a material change to the policy set out in the statement; any revisions must be made following consultation with such persons as the Authority considers appropriate.

7. ONE TOWER HAMLETS CONSIDERATIONS

7.1 The London Borough of Tower Hamlets Pension Fund represents an asset to the Council in terms of its ability for attracting and retaining staff who deliver services to residents. The adoption of a Work Plan should lead to more effective management of the Fund.

7.2 A significant element of the Council's budget is the employer's contribution to the Fund. Therefore, any improvement in the efficiency of the Fund that leads to improvement in investment performance or cost savings will likely reduce contributions from the Council and release funds for other corporate priorities.

8. BEST VALUE (BV) IMPLICATIONS

8.1 The preparation and production of a Funding Strategy Statement ought to result in a more efficient process of managing the Pension Fund.

8.2 Without sound financial management of the Pension Fund, the Council and other employers in the Pension Fund could see increased volatility in their contribution rates and increases in the cost of providing for the benefits of scheme members.

9. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

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

10. RISK MANAGEMENT IMPLICATIONS

10.1 All material, financial and business issues and possibility of risks have been considered and addressed within the report and its appendices, and that the actuarial report and funding strategy statement will provide the Pension Fund with a solid framework in which to achieve a full funding status over the long term.

11. CRIME AND DISORDER REDUCTION IMPLICATIONS

11.1 There are no any crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report - NONE

Appendices
Funding Position at 31 December 2020

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report –
Hymans Robertson Funding and Risk report at 31 December 2020

Officer contact details for documents:
Miriam Adams, Interim Head of Pensions & Treasury
Email: miriam.adams@towerhamlets.gov.uk

Tel: 0207 364 4248

HYMANS ROBERTSON

London Borough of Tower Hamlets Pension Fund

Funding and risk report as at 31 December 2020

HEADLINE

31 December 2020	Ongoing Funding (£m)
Assets	1,948
Liabilities	1,716
Surplus/(deficit)	232
Funding level	114%

Summary

This funding update is provided to illustrate the estimated development of the funding position from 31 March 2019 to 31 December 2020, for the London Borough of Tower Hamlets Pension Fund ("the Fund"). It is addressed to London Borough of Tower Hamlets in its capacity as the Administering Authority of the Fund and has been prepared in my capacity as your actuarial adviser.

At the last formal valuation, the Fund assets were £1,552m and the liabilities were £1,525m. This represented a surplus of £27m and equated to a funding level of 102%. Since the valuation the funding level has increase by 12% to 114%. However, the impact on the Consumer Prices Index (CPI) inflation assumption of the recent announcements regarding the Retail Prices Index (RPI) switching to CPIH (a measure of CPI including owner occupiers housing costs) from 2030 is still being assessed. This could have an impact on the estimated funding level shown throughout this report.

Investment returns of 24% over the period since the valuation have been higher than expected. However, the outlook for future investment returns over the next 20 years on the Fund's portfolio of assets has fallen (from 4% to 3.2%), increasing the value placed on liabilities. A full breakdown of the impact of these changes on the funding surplus is included in the dashboard.

Should you have any queries please contact me.

Barry Dodds FFA

Reliances and limitations

This report was commissioned by and is addressed to the London Borough of Tower Hamlets in their capacity as the Administering Authority and is provided to assist in monitoring certain funding and investment metrics. It should not be used for any other purpose. It should not be released or otherwise disclosed to any third party except as required by law or with our prior written consent, in which case it should be released in its entirety. **Decisions should not be taken based on the information herein without written advice from your consultant.** Neither I nor Hymans Robertson LLP accept any liability to any other party unless we have expressly accepted such liability in writing.

The method and assumptions used to calculate the updated funding position are consistent with those disclosed in the documents associated with the last formal actuarial valuation as at 31 March 2019, although the financial assumptions have been updated to reflect known changes in market conditions. The calculations contain approximations and the accuracy of this type of funding update declines with time from the valuation; differences between the position shown in this report and the position which a new valuation would show can be significant. This funding update has been carried out as at a date of 31 December 2020. There has been extreme volatility in investment markets in response to the COVID-19 global pandemic. This may impact both asset and liability valuations, but in particular may impact the estimate of future investment returns. It is not possible to assess its accuracy without carrying out a full actuarial valuation. This update complies with Technical Actuarial Standard 100.

London Borough of Tower Hamlets Pension Fund | Strategy and Risk Management dashboard

HEADLINE

31 December 2020	Ongoing Funding (£m)
Assets	1,948
Liabilities	1,716
Surplus/(deficit)	232
Funding level	114%

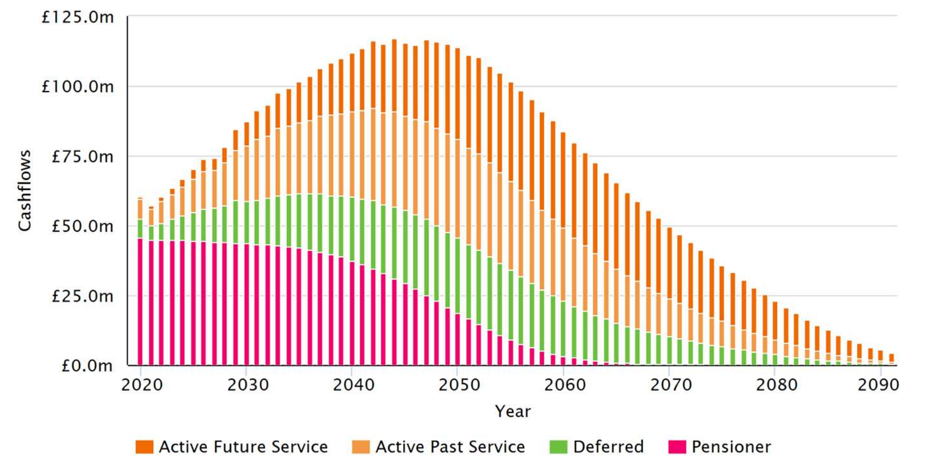
Surplus/(deficit)	£m
Surplus/(deficit) as at 31/03/2019	27
Contributions (less benefits accruing)	(7)
Interest on surplus/(deficit)	(0)
Excess return on assets	368
Change in inflation & expected future investment return	(155)
Surplus/(deficit) as at 31/12/2020	232

	31 March 2019	31 December 2020
Market yields (p.a.)		
Fixed interest gilts	1.49%	0.67%
Index-linked gilts	-1.81%	-2.31%
Implied inflation	3.36%	3.05%
AA corporate bond yield	2.36%	1.35%
Price Index		
FTSE All Share	3,978	3,674
FTSE 100	7,279	6,461
Expected future investment return (p.a.)		
20yr annualised return on Fund's asset portfolio*	4.0%	3.2%

*There is at least a 70% likelihood of the Fund's investments achieving a return of at least 3.2% p.a. over the next 20 years

*There was some extreme volatility in investment markets around the date of 31 December 2020, which may impact the likelihood estimates of expected future investment returns in this report.

HEADLINE



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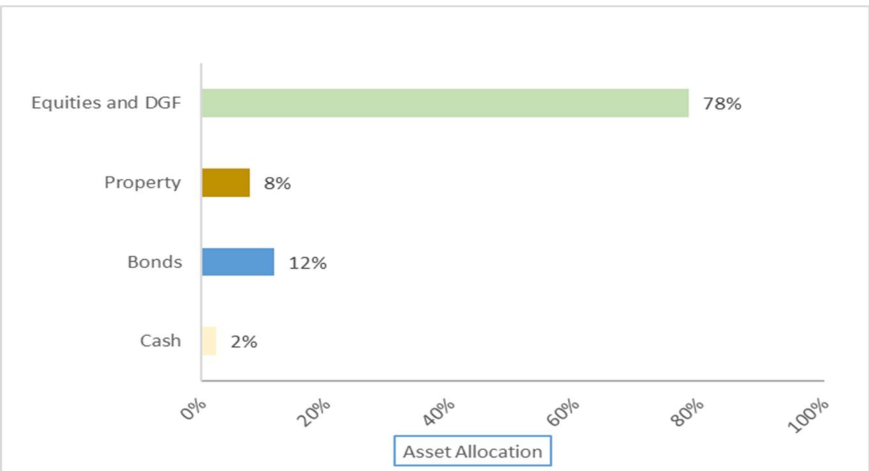

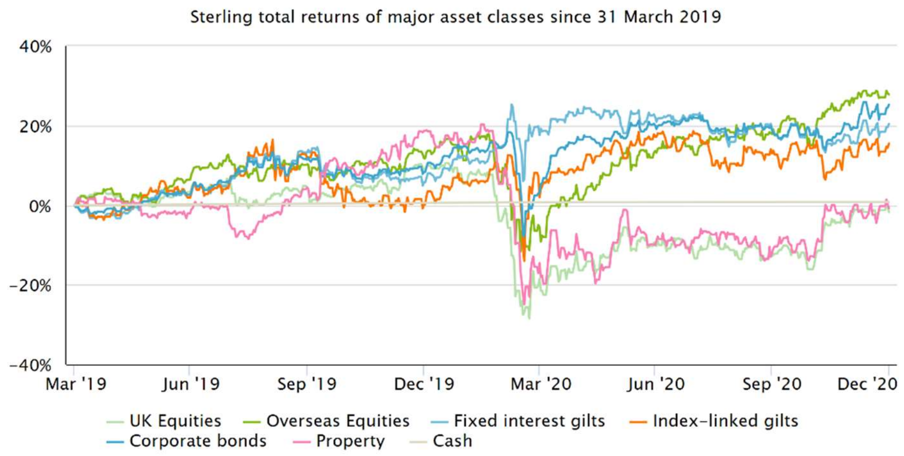

Sensitivity Matrix as at 31 December 2020 for Ongoing funding basis (£m)

Shift in equity level (using FTSE 100 levels as proxy)

Shift in expected future investment return (% p.a.)	4,522 -30%	5,168 -20%	5,814 - 10%	6,461	7,107 + 10%	7,753 + 20%	8,399 + 30%
+0.6	(91)	77	244	412	580	747	915
+0.4	(147)	21	188	356	524	691	859
+0.2	(207)	(39)	129	296	464	631	799
0.0	(271)	(103)	65	232	400	567	735
-0.2	(339)	(171)	(3)	164	332	499	667
-0.4	(412)	(244)	(76)	91	259	426	594
-0.6	(490)	(322)	(154)	13	181	348	516

less than 50% | 50% - 85% | 85% - 95% | 95% - 100% | 100% - 105% | 105% - 115% | greater than 115%

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Non-Executive Report of the: **Pensions Committee** 25 March 2021	TOWER HAMLETS
Report of Kevin Bartle, Interim Corporate Director, Resources	**Classification:** Unrestricted

Report on 2020/21 to 2022/23 Liquidity Forecast

Originating Officer(s)	Miriam Adams, Interim Head of Pensions & Treasury
Wards affected	All wards

Summary

This report provides an update on the Pension Fund's projected cash flow forecast for 2020/21 to 2022/23. The Fund is projecting a £20.335m projected cash balance. This includes the £20m draw down from proceeds of equity protection which the Committee agreed in July for operational use and projected cash flow short falls identified in 2021/22 and 22/23. No further shortfall is forecast for the next 2 financial years.

Recommendations

The Pensions Committee is recommended to:

- Note the cash flow forecast from operational activities (Appendix A)

1. REASONS FOR THE DECISION

1.1 The London Borough of Tower Hamlets Pension Fund is part of the wider Local Government Pension Scheme LGPS). The Scheme as with other LGPS schemes is funded and distinct from 'pay as you go' schemes which are unfunded.

1.2 The Fund receives contributions and investment income from current members, employers and fund assets which is used to pay benefits as they fall due. Consequently, one of the main objectives of the Fund is to ensure that sufficient funds are available to meet all benefits as they fall due for payment. However, this objective may be jeopardised if the Fund does not maintain sufficient liquidity. The Pension Committee is charged with meeting the duties of the Council in respect of the Pension Fund.

2. ALTERNATIVE OPTION

2.1 The Fund is bound by legislation to ensure that members of the Fund receive benefits as they fall due under the Fund's terms. Although the Fund is free to determine how best to fund its liabilities as they fall due. It is expected to meet such obligations to its retired members.

3. DETAILS OF REPORT

3.1 Although the Funding Strategy Statement has assumed that the Fund will mature at some point in the future, it is difficult to be exact about the day at which the Fund will become cash flow negative given the potential impact of transfers in/out and payment of lump sum amounts, both of which are very difficult to predict. Nevertheless, based on actuals to date and current forecast, it is expected that the Fund will remain cash flow positive for the next 2 years. This healthy cash flow position is due to the £20m cash received from Equity Protection proceeds.

3.3 The table below shows the membership over the last 4 years.

Membership Type	**2017/18**	**2018/19**	**2019/20**	**Dec 20**
Actives	6,809	6,740	7,120	7,338
Deferred	7,817	7,744	7,845	7,913
Pensioners	6,333	6,465	6,660	6,679

3.5 The general belief is that LGPS funds have lot of assets, but don't hold lots of cash. There good reasons for this – funds generally invest for the longer term. Holding too much cash leads to lost opportunities on other assets that offer higher expected returns. Funds are therefore constantly trying to balance the need to hold enough cash to meet all benefit payments against the need to invest to invest in return seeking assets. Over the last decade LGPS funds are beginning to reach a mature age profile. Although 2018/19 figures released by the LGPS Scheme Advisory Board (SAB) showed that overall, in England and Wales LGPS funds till remain cash flow positive including investment income.

3 OPTIONS TO IMPROVE FUND LIQUIDITY

3.3.1 Given the current cash flow position for 2020/21 and next 2 years, there are no immediate plans to liquidate assets. Officers will continue to report the cash flow position of the Fund to the Committee on an annual basis and more frequently if necessary

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 Finance comments are included in the report.

5. LEGAL COMMENTS

5.1 The Council as administering authority of the pension fund must ensure that it complies with its statutory duties in relation to the proper management of the pension funds. It is necessary and appropriate for the Pensions Committee to receive information on the performance of the fund in relation to the fund liquidity as set out in this report.

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance will reduce the contribution and increase the funds available for other corporate priorities.

7. BEST VALUE (BV) IMPLICATIONS

7.1 The Pension Fund accounts demonstrate the financial stewardship of the scheme members and employers' assets.

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 Any form of investment inevitably involves a degree of risk.

9.2 To minimise risk, the Pensions Committee attempts to achieve a diversified portfolio. Diversification relates to asset classes and management styles.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- None

Appendices

- **Cash flow forecast 2020/21 – 2022/23 (Appendix A)**

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

Officer contact details for documents:

- Miriam Adams, Interim Head of Pensions & Treasury x4248
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Cash flow 2020/21 to 2022/23 **Appendix A**

	2019/20 Actual £'000	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000
CASH IN				
Contributions				
From Employers	-39,250	-39,647	-40,147	-40,447
From Employees	-11,049	-12,425	-12,725	-13,025
Payment of Deficit Contributions	-53	-13,677	-13,677	-13,677
Other miscellaneous credits		-643		
Transfer Values In	-8,596	-6,544	-8,000	-9,000
Other Income				
From Returned Pensions Payroll Bacs				
From Pensions Over payments	-42	-145	-140	-140
Interest on internal cash	-55	0		
Income from Recoverable Taxes	-249	-171	-100	-100
Income from Fund Manager Fee Rebates	-94	-97	-66	-66
	-59,388	-73,349	-74,855	-76,455
Cash from Money Market Funds				
Cash from divestments	-13,000	-20,000	0	0
TOTAL CASH IN	**-72,388**	**-93,349**	**-74,855**	**-76,455**
CASH OUT				
Benefit Payable	49,808	50,535	52,535	54,035
Lump Sums, Retirement Allowances & Death Grants	14,283	14,013	15,000	16,000
Payment to and on account of leavers				
Refund of Contributions	756	208	200	200
Transfer Values Out	8,608	6,844	9,000	10,000
Other Miscellaneous Payments	0	1,682		
Expenses				
Fund manager fees paid in house	1,123	901	950	1,100
Custodian fees	100	53	60	70
Other admin expenses	1,188	1,812	2,312	2,712
Prevous Year's recharges paid				
	75,866	76,048	80,057	84,117
NET INCOME/EXPENDITURE	**3,478**	**-17,301**	**5,202**	**7,662**
Opening Cash balance	-512	-3,034	-335	-133
Closing balance MMF for operational Use	-6,000	0	-20,000	-15,000
FORECAST CLOSING CASH POSITION	**-3,034**	**-20,335**	**-15,133**	**-7,471**

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Agenda Item 6.3

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Agenda Item 6.4

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